

NORWOOD FINANCIAL CORP  
Form 10-Q  
November 09, 2012

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2012

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 0-28366

Norwood Financial Corp.  
(Exact name of Registrant as specified in its charter)

Pennsylvania  
(State or other jurisdiction of  
Incorporation or organization)

23-2828306  
(I.R.S. employer identification no.)

717 Main Street, Honesdale, Pennsylvania  
(Address of principal executive offices)

18431  
(Zip Code)

(570) 253-1455  
(Registrant's telephone number, including area code)

NA

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check (x) 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  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  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 the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

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Non-accelerated filer  Smaller reporting company   
(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 Exchange Act):   
] Yes[X] No

Class	Outstanding as of November 1, 2012
Common stock, par value \$0.10 per share	3,277,607

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FORM 10-Q  
FOR THE QUARTER ENDED SEPTEMBER 30, 2012

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## PART I. FINANCIAL INFORMATION

## Item 1. Financial Statements

## NORWOOD FINANCIAL CORP.

## Consolidated Balance Sheets (unaudited)

(dollars in thousands, except share and per share data)

	September 30, 2012	December 31, 2011
<b>ASSETS</b>		
Cash and due from banks	\$ 10,514	\$ 8,974
Interest bearing deposits with banks	24,825	12,449
Cash and cash equivalents	35,339	21,423
Securities available for sale, at fair value	147,639	150,263
Securities held to maturity, fair value 2012: \$175, 2011: \$177	172	171
Loans receivable, net of unearned income	479,501	457,907
Less: Allowance for loan losses	5,341	5,458
Net loans receivable	474,160	452,449
Investment in Federal Home Loan Bank Stock, at cost	2,932	3,593
Bank premises and equipment, net	7,453	7,479
Bank owned life insurance	12,234	11,887
Accrued interest receivable	2,589	2,468
Foreclosed real estate owned	659	2,910
Goodwill	9,715	9,715
Other intangibles	684	800
Other assets	5,121	5,656
<b>TOTAL ASSETS</b>	<b>\$ 698,697</b>	<b>\$ 668,814</b>
<b>LIABILITIES</b>		
Deposits:		
Non-interest bearing demand	\$ 89,218	\$ 71,959
Interest-bearing	452,372	453,808
Total deposits	541,590	525,767
Short-term borrowings	32,386	21,794
Other borrowings	27,533	27,670
Accrued interest payable	1,462	1,321
Other liabilities	3,775	4,201
<b>TOTAL LIABILITIES</b>	<b>606,746</b>	<b>580,753</b>
<b>STOCKHOLDERS' EQUITY</b>		
Common stock, \$.10 par value per share, authorized 10,000,000; shares issued 2012: 3,371,849 shares, 2011: 3,371,866 shares	337	337
Surplus	24,728	24,660
Retained earnings	66,005	62,308
Treasury stock at cost: 2012: 94,242 shares, 2011: 87,370 shares	(2,739)	(2,559)
Accumulated other comprehensive income	3,620	3,315
<b>TOTAL STOCKHOLDERS' EQUITY</b>	<b>91,951</b>	<b>88,061</b>
<b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>	<b>\$ 698,697</b>	<b>\$ 668,814</b>

See accompanying notes to the unaudited consolidated financial statements.

## NORWOOD FINANCIAL CORP.

## Consolidated Statements of Income (unaudited)

(dollars in thousands, except per share data)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	2011	2012	2011
<b>INTEREST INCOME</b>				
Loans receivable, including fees	\$6,429	\$6,521	\$19,233	\$16,917
Securities	971	1,116	3,004	3,341
Other	9	18	20	42
Total interest income	7,409	7,655	22,257	20,300
<b>INTEREST EXPENSE</b>				
Deposits	897	1,054	2,800	2,871
Short-term borrowings	14	24	38	75
Other borrowings	246	314	733	992
Total interest expense	1,157	1,392	3,571	3,938
NET INTEREST INCOME	6,252	6,263	18,686	16,362
PROVISION FOR LOAN LOSSES	900	425	1,650	1,075
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	5,352	5,838	17,036	15,287
<b>OTHER INCOME</b>				
Service charges and fees	561	581	1,674	1,722
Income from fiduciary activities	96	106	274	324
Net realized gains on sales of securities	631	544	1,318	768
Gains on sale of loans and servicing rights	83	41	143	282
Other	220	234	679	611
Total other income	1,591	1,506	4,088	3,707
<b>OTHER EXPENSES</b>				
Salaries and employee benefits	2,102	2,129	6,300	5,662
Occupancy, furniture & equipment	512	489	1,489	1,295
Data processing related	222	233	670	635
Taxes, other than income	150	142	451	414
Professional fees	157	171	583	296
Merger related expenses	-	16	18	771
Federal Deposit Insurance Corporation insurance assessment	94	102	290	317
Foreclosed real estate owned expense (income)	(23)	) 372	184	408
Other	743	700	2,076	2,026
Total other expenses	3,957	4,354	12,061	11,824
INCOME BEFORE INCOME TAXES	2,986	2,990	9,063	7,170
INCOME TAX EXPENSE	786	775	2,419	1,811
NET INCOME	\$2,200	\$2,215	\$6,644	\$5,359
BASIC EARNINGS PER SHARE	\$.67	\$.67	\$2.03	\$1.79

DILUTED EARNINGS PER SHARE	\$ .67	\$ .67	\$ 2.02	\$ 1.79
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See accompanying notes to the unaudited consolidated financial statements.

NORWOOD FINANCIAL CORP  
 Consolidated Statement of Comprehensive Income (unaudited)  
 (dollars in thousands)

	Three Months Ended September 30, 2012		Three Months Ended September 30, 2011
Net income	\$ 2,200		\$ 2,215
Other Comprehensive Income:			
Investment securities available for sale:			
Unrealized holding gains	1,331		2,021
Tax effect	(453)	)	(688)
Reclassification of gains recognized in net income	(631)	)	(544)
Tax effect	214		185
Other Comprehensive Income	461		974
Comprehensive Income	\$ 2,661		\$ 3,189

	Nine Months Ended September 30, 2012		Nine Months Ended September 30, 2011
Net income	\$ 6,644		\$ 5,359
Other Comprehensive Income:			
Investment securities available for sale:			
Unrealized holding gains	1,775		3,648
Tax effect	(602)	)	(1,241)
Reclassification of gains recognized in net income	(1,318)	)	(768)
Tax effect	450		261
Other Comprehensive Income	305		1,900
Comprehensive Income	\$ 6,949		\$ 7,259

See accompanying notes to unaudited consolidated financial statements.

## NORWOOD FINANCIAL CORP.

Consolidated Statements of Changes in Stockholders' Equity (unaudited)

Nine Months Ended September 30, 2012

(dollars in thousands, except share and per share data)

	Common Stock		Surplus	Retained Earnings	Treasury Stock		Accumulated Other Comprehensive	Total
	Shares	Amount			Income			
Balance December 31, 2011	3,371,866	\$337	\$24,660	\$62,308	87,370	\$(2,559 )	\$ 3,315	\$88,061
Net Income				6,644				6,644
Other comprehensive income							305	305
Cash dividends declared \$.90 per share				(2,947 )				(2,947 )
Acquisition of treasury stock					11,647	(320 )		(320 )
Compensation expense related to stock options			98					98
Stock options exercised			(41 )		(4,775 )	140		99
Tax benefit on stock options			11					11
North Penn exchange adjustment		(17)						
Balance, September 30, 2012	3,371,849	\$337	\$24,728	\$66,005	94,242	\$(2,739 )	\$ 3,620	\$91,951

See accompanying notes to the unaudited consolidated financial statements.

## NORWOOD FINANCIAL CORP.

## Consolidated Statements of Cash Flows (Unaudited)

(dollars in thousands)

	Nine Months Ended September 30,	
	2012	2011
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net Income	\$ 6,644	\$ 5,359
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	1,650	1,075
Depreciation	420	369
Amortization of intangible assets	116	68
Deferred income taxes	(404 )	(31 )
Net amortization of securities premiums and discounts	888	564
Net realized gain on sales of securities	(1,318 )	(768 )
Net increase in value of life insurance	(395 )	(299 )
Loss (gain) on sale of foreclosed real estate	(24 )	54
Net gain on sale of mortgage loans	(163 )	(282 )
Mortgage loans originated for sale	(4,343 )	(8,677 )
Proceeds from sale of mortgage loans originated for sale	4,506	8,959
Compensation expense related to stock options	98	126
Decrease in accrued interest receivable and other assets	1,434	2,049
(Decrease) increase in accrued interest payable and other liabilities	(281 )	675
Net cash provided by operating activities	8,828	9,241
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Securities available for sale:		
Proceeds from sales	23,265	27,734
Proceeds from maturities and principal reductions on mortgage-backed securities	25,251	23,180
Purchases	(45,780 )	(35,043 )
Redemption of FHLB stock	661	527
Net (increase) decrease in loans	(24,261 )	15,975
Purchase of bank premises and equipment	(394 )	(135 )
Proceeds from sale of bank premises and equipment and foreclosed real estate	3,229	346
Acquisition, net of cash acquired	-	4,544
Net cash (used in) provided by investing activities	(18,029 )	37,128
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Net increase (decrease) in deposits	15,823	(2,786 )
Net increase (decrease) in short-term borrowings	10,592	(1,333 )
Repayments of other borrowings	(137 )	(18,060 )
Stock options exercised	99	-
Tax benefit of stock options exercised	11	-
Acquisition of treasury stock	(320 )	(207 )
Cash dividends paid	(2,951 )	(2,559 )
Net cash provided by (used in) financing activities	23,117	(24,945 )
Increase in cash and cash equivalents	13,916	21,424

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CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	21,423	16,625
CASH AND CASH EQUIVALENTS, END OF PERIOD	\$ 35,339	\$ 38,049

See accompanying notes to the unaudited consolidated financial statements.

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## CONSOLIDATED STATEMENTS OF CASH FLOWS (CONTINUED)

(dollars in thousands)

	Nine Months Ended September 30,	
	2012	2011
Supplemental Disclosures of Cash Flow Information		
Cash payments for:		
Interest paid to depositors and borrowers	\$ 3,430	\$ 3,985
Income taxes paid, net of refunds	\$ 1,408	\$ 1,409
Supplemental Schedule of Noncash Investing Activities		
Investment purchases	\$ (774 )	\$ -
Transfers of loans to foreclosed real estate and repossession of other assets	\$ 954	\$ 3,051

See accompanying notes to the unaudited consolidated financial statements.

## Notes to the Unaudited Consolidated Financial Statements

## 1. Basis of Presentation

The unaudited consolidated financial statements include the accounts of Norwood Financial Corp. (Company) and its wholly-owned subsidiary, Wayne Bank (Bank) and the Bank's wholly-owned subsidiaries, WCB Realty Corp., Norwood Investment Corp., Norwood Settlement Services, LLC, and WTRO Properties. All significant intercompany transactions have been eliminated in consolidation.

The accompanying unaudited consolidated financial statements have been prepared in conformity with generally accepted accounting principles for interim financial statements and with instructions to Form 10-Q. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In preparing the financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the balance sheet and revenues and expenses for the period. Actual results could differ from those estimates. The financial statements reflect, in the opinion of management, all normal, recurring adjustments necessary to present fairly the financial position and results of operations of the Company. The operating results for the three and nine month periods ended September 30, 2012 are not necessarily indicative of the results that may be expected for the year ending December 31, 2012 or any other future interim period.

These statements should be read in conjunction with the consolidated financial statements and related notes which are incorporated by reference in the Company's Annual Report on Form 10-K for the year-ended December 31, 2011.

## 2. Earnings Per Share

Basic earnings per share represents income available to common stockholders divided by the weighted average number of common shares outstanding during the period. Diluted earnings per share reflects additional common shares that would have been outstanding if dilutive potential common shares had been issued, as well as any adjustment to income that would result from the assumed issuance. Potential common shares that may be issued by the Company relate solely to outstanding stock options and are determined using the treasury stock method.

The following table sets forth the weighted average shares outstanding used in the computations of basic and diluted earnings per share:

(in thousands)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	2011	2012	2011
Basic EPS weighted average shares outstanding	3,278	3,292	3,279	3,001
Dilutive effect of stock options	8	1	5	1
Diluted EPS weighted average shares outstanding	3,286	3,293	3,284	3,002

Stock options which had no intrinsic value, because their effect would be anti-dilutive and therefore were not included in the diluted earnings per share calculation were 60,000 and 165,150 as of September 30, 2012 and 2011, respectively, based upon the closing price of Norwood common stock of \$30.20 and \$24.02 per share on September 30, 2012 and 2011, respectively.

## 3. Stock-Based Compensation

As of September 30, 2012, there was \$33,000 of total unrecognized compensation cost related to non-vested options granted in 2011 under the plan, which will be fully amortized by December 31, 2012.



A summary of stock options from all plans, adjusted for stock dividends declared, is shown below.

	Options	Weighted Average Exercise Price Per Share	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value (in thousands)
Outstanding at January 1, 2012	209,914	\$ 28.43	6.3 Yrs.	\$ 113
Granted	-	-	-	-
Exercised	(4,775)	20.72	.8 Yrs.	31
Forfeited	(12,225)	29.65	5.2 Yrs.	-
Outstanding at September 30, 2012	192,914	28.54	5.7 Yrs.	370
Exercisable at September 30, 2012	164,914	28.72	5.0 Yrs.	293

Intrinsic value represents the amount by which the market price of the stock on the measurement date exceeded the exercise price of the option. The stock price was \$30.20 as of September 30, 2012 and \$27.47 as of December 31, 2011.

#### 4. Off-Balance Sheet Financial Instruments and Guarantees

The Bank is a party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit and letters of credit. Those instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the balance sheets.

The Bank's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and letters of credit is represented by the contractual amount of those instruments. The Bank uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments.

A summary of the Bank's financial instrument commitments is as follows:

(in thousands)	September 30,	
	2012	2011
Unfunded availability under loan commitments	\$ 38,297	\$ 37,649
Unfunded commitments under lines of credit	37,081	31,183
Standby letters of credit	11,277	11,960
	\$ 86,655	\$ 80,792

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since some of the commitments are expected to expire without being drawn upon, the total commitment amount does not necessarily represent future cash requirements. The Bank evaluates each customer's credit worthiness on a case-by-case basis. The amount of



collateral obtained, if deemed necessary by the Bank upon extension of credit, is based on management's credit evaluation of the customer and generally consists of real estate.

The Bank 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 Bank 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 Bank, generally, holds collateral and/or personal guarantees supporting these commitments. 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 payments required under the corresponding guarantees. The current amount of the liability as of September 30, 2012 for guarantees under standby letters of credit issued is not material.

## 5. Securities

The amortized cost and fair value of securities were as follows:

	Amortized Cost	September 30, 2012		Fair Value
		Gross Unrealized Gains	Gross Unrealized Losses	
(In Thousands)				
Available for Sale:				
U.S. Government agencies	\$ 6,999	\$ 43	\$ -	\$ 7,042
States and political subdivisions	55,445	3,249	(2 )	58,692
Corporate obligations	9,041	341	-	9,382
Mortgage-backed securities-government sponsored entities	70,292	1,869	(39 )	72,122
	141,777	5,502	(41 )	147,238
Equity securities-financial services	374	27	-	401