PATHFINDER BANCORP INC
Form 10-Q
November 14, 2006

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

FORM 10-Q

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ending September 30, 2006

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 Registrant as Specified in its Charter)

FEDERAL	16-1540137
(State or Other Jurisdiction of Incorporation or Organization	(I.R.S. Employer Identification Number)

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

(315) 343-0057
(Registrant'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 twelve 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 [X] No [ ].

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

Large Accelerated Filer [ ] Accelerated Filer [ ] Non-Accelerated Filer[X]

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes [ ] No [X]

As of November 13, 2006 there were 2,951,819 shares issued and 2,464,532 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, 2006 (UNAUDITED) AND DECEMBER 31, 2005

ASSETS	September 30, 2006
(Dollars in thousands)	
Cash and due from banks	$ 8,547
Interest earning deposits	257
Total cash and cash equivalents	8,804

Investment securities, at fair value		69,058
Federal Home Loan Bank stock, at cost		1,772
Loans		197,463
Less: Allowance for loan losses		1,631
Loans receivable, net		195,832
Premises and equipment, net		7,602
Accrued interest receivable		1,636
Foreclosed real estate		497
Goodwill		3,840
Intangible asset, net		238
Bank owned life insurance		6,137
Other assets		2,587
Total assets	$	298,003
LIABILITIES AND SHAREHOLDERS' EQUITY		
Deposits:		
Interest-bearing	$	216,026
Non interest-bearing		21,89
Total deposits		237,921
Short-term borrowings		3,300
Long-term borrowings		27,360
Junior subordinated debentures		5,155
Other liabilities		2,902
Total liabilities		276,638
Shareholders' equity:		
Preferred stock, authorized shares 1,000,000; no shares issued or outstanding		
Common stock, par value $.01; authorized 10,000,000 shares; 2,951,819 and 2,950,419 shares issued; and 2,464,532 and 2,463,132 shares outstanding, respectively		29
Additional paid in capital		7,732
Retained earnings		21,083
Accumulated other comprehensive loss		(977
Treasury stock, at cost; 487,287 shares		(6,502
Total shareholders' equity		21,365
Total liabilities and shareholders' equity	$	298,003

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

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

	For the three months ended	For mon

(Dollars in thousands, except per share data)	September 30, 2006	Septem
INTEREST INCOME:		
Loans, including fees	$ 3,222	$
Debt securities:		
Taxable	561	
Tax-exempt	98	
Dividends	82	
Other	4	
Total interest income	3,967	
INTEREST EXPENSE:		
Interest on deposits	1,376	
Interest on short-term borrowings	78	
Interest on long-term borrowings	456	
Total interest expense	1,910	
Net interest income	2,057	
Provision for loan losses	-	
Net interest income after provision for loan losses	2,057	
OTHER INCOME:		
Service charges on deposit accounts	338	
Loan servicing fees	55	
Earnings on bank owned life insurance	50	
Net losses on sales of investment securities	-	
Net (losses) gains on sales of loans and foreclosed real estate	(29)	
Other charges, commissions and fees	130	
Total other income	544	
OTHER EXPENSES:		
Salaries and employee benefits	1,307	
Building occupancy	291	
Data processing expenses	328	
Professional and other services	121	
Amortization of intangible asset	55	
Other expenses	289	
Total other expenses	2,391	
Income before income taxes	210	
Provision for income tax expense (benefit)	40	
NET INCOME	$ 170	$
NET INCOME PER SHARE - BASIC	$ 0.07	$
NET INCOME PER SHARE - DILUTED	$ 0.07	$
DIVIDENDS PER SHARE	$ 0.1025	$

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

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

(Dollars in thousands, except per share data)	For the nine months ended September 30, 2006	For the months September
INTEREST INCOME:		
Loans, including fees	$ 9,416	$
Debt securities:		
Taxable	1,828	
Tax-exempt	294	
Dividends	210	
Other	16	
Total interest income	11,764	
INTEREST EXPENSE:		
Interest on deposits	3,904	
Interest on short-term borrowings	263	
Interest on long-term borrowings	1,344	
Total interest expense	5,511	
Net interest income	6,253	
Provision for loan losses	23	
Net interest income after provision for loan losses	6,230	
OTHER INCOME:		
Service charges on deposit accounts	1,059	
Loan servicing fees	160	
Earnings on bank owned life insurance	150	
Net losses on sales of securities	(9)	
Net (losses) gains on sales of loans/real estate	(34)	
Other charges, commissions & fees	417	
Total other income	1,743	
OTHER EXPENSES:		
Salaries and employee benefits	3,765	
Building occupancy	913	
Data processing expenses	958	
Professional and other services	352	
Amortization of intangible asset	166	
Other expenses	958	
Total other expenses	7,112	
Income before income taxes	861	
Provision for income tax expense (benefit)	148	

NET INCOME	$ 713	$
NET INCOME PER SHARE - BASIC	$ 0.29	$
NET INCOME PER SHARE - DILUTED	$ 0.29	$
DIVIDENDS PER SHARE	$ 0.3075	$

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

PATHFINDER BANCORP, INC.
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
NINE MONTHS ENDED SEPTEMBER 30, 2006 AND SEPTEMBER 30, 2005
(unaudited)

	Common Stock Shares	Common Stock Amount	Additional Paid in Capital	Retained Earnings
(Dollars in thousands, except per share data)				
BALANCE, DECEMBER 31, 2005	2,950,419	$ 29	$ 7,721	$ 20,965
Comprehensive income				
Net income				713
Other comprehensive income, net of tax				
Unrealized net gains on securities				
Total Comprehensive Income				
Stock options exercised	1,400	-	11	
Dividends declared ($.3075 per share)				(595)
BALANCE, SEPTEMBER 30, 2006	2,951,819	$ 29	$ 7,732	$ 21,083
BALANCE, DECEMBER 31, 2004	2,937,419	$ 29	$ 7,453	$ 21,186
Comprehensive income				
Net income				499
Other comprehensive income, net of tax				
Unrealized net losses on securities				
Total Comprehensive Income				
ESOP shares earned			55	
Stock options exercised	13,000	-	86	
Dividends declared ($.3075 per share)				(593)
BALANCE, SEPTEMBER 30, 2005	2,950,419	$ 29	$ 7,594	$ 21,092

(Dollars in thousands, except per share data)	Treasury Stock	Total
BALANCE, DECEMBER 31, 2005	$ (6,502)	$20,928
Comprehensive income		
Net income		713
Other comprehensive income, net of tax		
Unrealized net gains on securities		308
Total Comprehensive Income		1,021
Stock options exercised		11
Dividends declared ($.3075 per share)		(595)
BALANCE, SEPTEMBER 30, 2006	$ (6,502)	$21,365
BALANCE, DECEMBER 31, 2004	$ (6,502)	$21,826
Comprehensive income		
Net income		499
Other comprehensive income, net of tax		
Unrealized net losses on securities		(328)
Total Comprehensive Income		171
ESOP shares earned		88
Stock options exercised		86
Dividends declared ($.3075 per share)		(593)
BALANCE, SEPTEMBER 30, 2005	$ (6,502)	$21,578

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

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

(Dollars in thousands)	For the nine months ended September 30, 2006	For the nine months ends September 30, 2005
OPERATING ACTIVITIES		
Net income	$ 713	$ 499
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	23	229
ESOP shares earned	-	88

Deferred income tax expense	277	133
Realized losses (gains) on sale of:		
Real estate through foreclosure	34	7
Loans	-	(37)
Available-for-sale investment securities	9	192
Premises and equipment	(13)	-
Depreciation	561	518
Amortization of intangible asset	166	166
Amortization of deferred financing costs	23	23
Amortization of mortgage servicing rights	77	22
Earnings on bank owned life insurance	(150)	(133)
Net amortization of premiums on investment securities	116	279
Decrease (increase) in interest receivable	42	(139)
Net change in other assets and liabilities	(214)	(259)
NET CASH PROVIDED BY OPERATING ACTIVITIES	1,664	1,588
INVESTING ACTIVITIES		
Purchase of investment securities available-for-sale	(10,985)	(19,642)
Net (purchase) redemption of FHLB stock	33	131
Proceeds from maturities and principal reductions of investment securities available-for-sale	15,792	9,183
Proceeds from sale:		
Portfolio loans	-	8,897
Real estate acquired through foreclosure	456	414
Available-for-sale investment securities	771	-
Premises and equipment	145	-
Net increase in loans	(7,114)	(6,021)
Purchase of premises and equipment	(275)	(949)
NET CASH USED IN INVESTING ACTIVITIES	(1,177)	(7,987)
FINANCING ACTIVITIES		
Net decrease in demand deposits, NOW accounts savings accounts, money market deposit accounts and escrow deposits	(10,226)	(4,641)
Net increase in time deposits	11,770	8,821
Increase in short-term borrowings	1,300	1,000
Payments on long-term borrowings	(2,000)	(4,000)
Proceeds from exercise of stock options	11	86
Cash dividends paid	(433)	(429)
NET CASH PROVIDED BY FINANCING ACTIVITIES	422	837
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	909	(5,562)
Cash and cash equivalents at beginning of period	7,895	14,325
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ 8,804	$ 8,763
NONCASH INVESTING ACTIVITY:		
Conversion of Parent Company advances to loans receivable	$ 1,101	$ -
Transfer of loans to foreclosed real estate	249	558

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

PATHFINDER BANCORP, INC.

Notes to Financial Statements

(1) BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements of Pathfinder Bancorp, Inc. and its wholly owned subsidiaries (the "Company") have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information and 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 U.S. generally accepted accounting principles. Certain amounts in the 2005 consolidated financial statements have been reclassified to conform to the current period presentation. These reclassifications had no effect on net income as previously reported. 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" was 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, 2005 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 nine months ended September 30, 2006 are not necessarily indicative of the results that may be expected for the year ending December 31, 2006.

(2) EARNINGS PER SHARE

Basic earnings per share have been computed by dividing net income by the weighted average number of common shares outstanding throughout the three months and nine months ended September 30, 2006 and 2005, using 2,463,482 and 2,461,328 weighted average common shares outstanding for the three months ended, and 2,463,250 and 2,453,744 for the nine months ended, respectively. Diluted earnings per share for the three months and nine months ended September 30, 2006 and 2005 have been computed using 2,483,465 and 2,488,418 for the three months ended and 2,482,069 and 2,487,478 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.

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(3) PENSION BENEFITS

The composition of net periodic benefit plan cost for the three months and nine months ended September 30, 2006 and 2005 is as follows:

	FOR THE THREE MONTHS ENDED SEPTEMBER 30,		FOR THE NINE MONTHS ENDED SEPTEMBER 30,	
	2006	2005	2006	2005

(In thousands)				
Service cost	$ 48	$ 38	$ 144	$ 114
Interest cost	63	57	189	171
Expected return on plan assets	(92)	(71)	(276)	(213)
Amortization of net losses	28	24	84	72
Net periodic benefit cost	$ 47	$ 48	$ 141	$ 144

The Company previously disclosed in its financial statements for the year ended December 31, 2005, that it expected to contribute $192,000 to its pension plan in 2006. As of September 30, 2006, $135,000 had been contributed to the pension plan.

(4) COMPREHENSIVE INCOME (LOSS)

The components of other comprehensive income (loss) and related tax effects for the three and nine month periods ended September 30, 2006 and 2005 are as follows:

	FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2006	2005	FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2006	2005
(In thousands)				
Gross change in unrealized gains (losses) on securities available for sale	$ 1,430	$ (175)	$ 513	$ (739)
Reclassification adjustment for (gains) losses included in net income	-	192	9	192
	1,430	17	522	(547)
Tax effect	(572)	(7)	(214)	219
Net of tax amount	$ 858	$ 10	$ 308	$ (328)

(5) 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 $216,000 of standby letters of credit as of September 30, 2006. 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, 2006 for guarantees under standby letters of credit issued is not material.

(6) STOCK BASED COMPENSATION

Prior to 2006, the Company accounted for stock-based compensation issued to directors and employees using the intrinsic value method in accordance with Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" (APB 25). This method required that compensation expense be recognized to the extent that the fair value of the stock exceeds the exercise price of the stock award at the grant date. The Company generally did not recognize compensation expense related to stock option awards because the stock options generally had fixed terms and exercise prices that were equal to or greater than the fair value of the Company's common stock at the grant date.

Effective January 1, 2006, the Company adopted Financial Accounting Standards Board (FASB) Statement No. 123(R), Share-Based Payment, ("SFAS 123(R)"). SFAS 123(R) requires compensation costs related to share-based payment transactions to be recognized in the income statement (with limited exceptions) using the modified prospective method based on the grant-date fair value of the stock-based compensation issued. Compensation costs are recognized over the period that an employee provides service in exchange for the award. As of the date of adoption of SFAS 123(R), the Company's options were fully granted and vested, and accordingly, there was no impact to the Company's consolidated financial position or results of operations.

In conjunction with SFAS 123(R), the Company also adopted FASB Staff Position ("FSP") SFAS 123(R)-2, "Practical Accommodation to the Application of Grant Date as Defined in SFAS 123(R)" effective January 1, 2006. FSP 123(R)-2 provides guidance on the application of grant date as defined in SFAS 123(R). In accordance with this standard a grant date of an award exists if (a) the award is a unilateral grant, and (b) the key terms and conditions of the award are expected to be communicated to an individual recipient within a relatively short time period from the date of approval. The adoption of this standard did not impact our consolidated financial position, results of operations or cash flows for the three or nine-month periods ended September 30, 2006.

In November 2005, the FASB issued final FSP No. 123(R)-3, "Transition Election Related to Accounting for the Tax Effects of Share-Based Payment Awards." The FSP provides an alternative method of calculating excess tax benefits (the Additional Paid-in Capital "APIC"pool) from the method defined in SFAS 123(R) for share-based payments. A one-time election to adopt the transition method in this FSP is available to those entities adopting SFAS 123(R) using either the modified retrospective or modified prospective method. Up to one year from the initial adoption of SFAS 123(R) or effective date of the FSP is provided to make this one-time election. However, until an entity makes its election, it must follow the guidance in SFAS 123(R). We are currently evaluating the potential impact of calculating the APIC pool with this alternative method and have not yet determined which method we will adopt, or the expected impact on our consolidated financial position or results of operations.

In February 2006, the FASB issued FSP No. 123(R)-4, "Classifications of Options and Similar Instruments Issued as Employee Compensation That Allow for Cash Settlement upon the Occurrence of a Contingent Event." The position amends SFAS 123(R) to incorporate that a cash settlement feature that can be exercised only upon the occurrence of a contingent event that is outside the employee's control does not meet certain conditions in SFAS 123(R) until it becomes probable that the event will occur. The guidance in this FSP was required to be applied upon initial adoption of SFAS 123(R). The Company does not have any option grants that allow for cash settlement.

(7) NEW ACCOUNTING PRONOUNCEMENTS

In February 2006, the FASB issued SFAS No. 155, Accounting for Certain Hybrid Financial Instruments ("SFAS 155"). SFAS 155 amends FASB Statement No. 133 and FASB Statement No. 140, and improves the financial reporting of certain hybrid financial instruments by requiring more consistent accounting that eliminates exemptions and provides a means to simplify the accounting for these instruments. Specifically, SFAS 155 allows financial instruments that have embedded derivatives to be accounted for as a whole (eliminating the need to bifurcate the derivative from its host) if the holder elects to account for the whole instrument on a fair value basis. The Company is required to adopt the provisions of SFAS 155, as applicable, beginning in 2007. Management does not believe the adoption of SFAS 155 will have a material impact on the Company's consolidated financial position and results of operations.

In March 2006, the FASB issued SFAS No. 156, Accounting for Servicing of Financial Assets -An Amendment of FASB Statement No. 140 ("SFAS 156"). SFAS 156 requires that all separately recognized servicing assets and servicing liabilities be initially measured at fair value, if practicable. The statement permits, but does not require, the subsequent measurement of servicing assets and servicing liabilities at fair value. SFAS 156 is effective for the Company beginning in 2007. The Company does not believe that the adoption of SFAS 156 will have a significant effect on its consolidated financial statements.

In July 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes-an interpretation of FASB Statement No. 109" (FIN 48), which clarifies the accounting for uncertainty in tax positions. This Interpretation requires that companies recognize in their financial statements the impact of a tax position, if that position is more likely than not of being sustained on audit, based on the technical merits of the position. The provisions of FIN 48 are effective for fiscal years beginning after December 15, 2006, with the cumulative effect of the change in accounting principle recorded as an adjustment to opening retained earnings. The Company is evaluating the impact of this new pronouncement on its consolidated financial statements.

In September 2006, the FASB issued FASB Statement No. 157, Fair Value Measurements, which defines fair value, establishes a framework for measuring fair value under GAAP, and expands disclosures about fair value measurements. FASB Statement No. 157 applies to other accounting pronouncements that require or permit fair value measurements. The new guidance is effective for financial statements issued for fiscal years beginning after November 15, 2007, and for interim periods within those fiscal years. We are currently evaluating the potential impact, if any, of the adoption of FASB Statement No. 157 on our consolidated financial position, results of operations and cash flows.

On September 29, 2006, the Financial Accounting Standards Board "FASB" issued SFAS No. 158, Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans ("SFAS 158"), which amends SFAS 87 and SFAS 106 to require recognition of the overfunded or underfunded status of pension and other postretirement benefit plans on the balance sheet. Under SFAS 158, gains and losses, prior service costs and credits, and any remaining transition amounts under SFAS 87 and SFAS 106 that have not yet been recognized through net periodic benefit cost will be recognized in accumulated other comprehensive income, net of tax effects, until they are amortized as a component of net periodic cost. The measurement date - the date at which the benefit obligation and plan assets are measured - is required to be the company's fiscal year end. SFAS 158 is effective for publicly-held companies for fiscal years ending after December 15, 2006, except for the measurement date provisions, which are effective for fiscal years ending after December 15, 2008. The Company is currently analyzing the effects of SFAS 158 but does not expect its implementation will have a significant impact on the Company's financial conditions or results of operations.

On September 13, 2006, the Securities and Exchange Commission "SEC" issued Staff Accounting Bulletin No. 108 ("SAB 108"). SAB 108 provides interpretive guidance on how the effects of the carryover or reversal of prior year misstatements

should be considered in quantifying a potential current year misstatement. Prior to SAB 108, companies might evaluate the materiality of financial statement misstatements using either the income statement or balance sheet approach, with the income statement approach focusing on new misstatements added in the current year, and the balance sheet approach focusing on the cumulative amount of misstatement present in a company's balance sheet. Misstatements that would be material under one approach could be viewed as immaterial under another approach, and not be corrected. SAB 108 now requires that companies view financial statement misstatements as material if they are material according to either the income statement or balance sheet approach. The Company has analyzed SAB 108 and determined that upon adoption it will have no impact on the reported results of operations or financial conditions.

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

GENERAL

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, Inc. are the wholly owned subsidiaries of Pathfinder Bank. At September 30, 2006, Pathfinder Bancorp, MHC, the Company's mutual holding company parent, whose activities are not included in the MD&A, held 64.2% of the Company's common stock while the public held 35.8% of the Company's common stock.

The following discussion reviews the Company's financial condition at September 30, 2006 and the results of operations for the three and nine months ended September 30, 2006 and September 30, 2005.

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 other income, including income from fees and service charges on deposit accounts, net gains and losses on sales of securities, loans and foreclosed real estate, and other expenses such as salaries and employee benefits, building 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.

APPLICATION OF CRITICAL ACCOUNTING POLICIES

The Company's consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America 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 consolidated 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 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 2005 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 consolidated 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 September 30, 2006, 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 consolidated 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.

EXECUTIVE SUMMARY

Net income was $170,000, or $0.07 per diluted share, for the three months ended September 30, 2006 as compared to $116,000, or $0.05 per diluted share, for the same period in 2005. For the nine months ended September 30, 2006, the Company reported net income of $713,000, or $0.29 per diluted share as compared to $499,000, or $0.20 per diluted share, for the same period in 2005. The Company continued its efforts toward transforming its traditional thrift balance sheet with mostly residential loans as interest earning assets toward that of a community bank with a more diverse mix of residential, consumer and commercial loans. On an average balance basis, commercial loans comprise 26.2% of the total gross loan portfolio for the nine months ended September 30, 2006, as compared to 25.0% of the portfolio in 2005. Asset quality continues to improve

during 2006 as reflected by the improvement in the ratio of non-performing loans to period end loans to 0.69% at September 30, 2006, from 0.88% at September 30, 2005.

On April 23, 2006, Alliance Bank N.A. announced it had reached a definitive agreement to merge with the parent company of Oswego County National Bank (OCNB). OCNB, formerly, Oswego County Savings Bank has been domiciled in the city of Oswego since its founding in 1870 and has been the primary local competitor for Pathfinder Bank. In management's view, the absorption of OCNB into Alliance Bank, a $900 million bank headquartered in Syracuse, NY, will provide both challenges and opportunities for Pathfinder Bank. The challenge will be the ability of a larger competitor to more actively and aggressively market within the primary business area of Pathfinder Bank. Opportunities exist, as management believes that it's unique competencies and differentiators are more closely matched by a locally domiciled bank, than one headquartered outside our primary market area. Opportunities may exist to garner additional business relationships with the traditional customer base of OCNB that is more apt to conduct its business with a local bank.

RESULTS OF OPERATIONS

The return on average assets and return on shareholders' equity were 0.23% and 3.21%, respectively, for the three months ended September 30, 2006, compared with 0.15% and 2.16%, respectively, for the three months ended September 30, 2005. During the third quarter of 2006, when compared to the third quarter of 2005, net interest income decreased $145,000, combined with a decrease in other income, exclusive of net gains on sales of securities and loans/real estate, by

$26,000, or 4%, offset by a $102,000, or 4%, reduction in other expenses. No provision for loan losses was made in the quarter.

The return on average assets and return on shareholders' equity were 0.32% and 4.53%, respectively, for the nine months ended September 30, 2006, compared with 0.22% and 3.10%, respectively, for the nine months ended September 30, 2005. For the nine months ended September 30, 2006, net interest income decreased $409,000, or 6%, when compared to the nine months ended September 30, 2005. This decrease was offset by a reduction in other expenses of $311,000, or 4%, an increase in other income, exclusive of net gains on sales of securities and loans/real estate, of $140,000, or 9%, and a 90%, or $206,000, reduction in provision for loan losses.

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 interest earning assets, interest-bearing liabilities, related yields and associated funding costs.

For the three months ended September 30, 2006, net interest income, on a tax-equivalent basis, decreased to $2.1 million from $2.2 million, when compared to the same quarter of 2005. The Company's net interest margin for the third quarter of 2006 decreased to 3.11% from 3.21% when compared to the same quarter in 2005. Management expects continued margin compression to adversely impact earnings, as we anticipate the yield curve will continue to be flat or inverted over the near term. The decline in net interest income was attributable to the higher rates paid of 54 basis points on both deposits and borrowings, offset by an increase of 40 basis points in average interest-earning asset yields. Average interest-earning assets decreased 3% to $270.3 million for the three months ended September 30, 2006 as compared to $279.6 million for the three months ended September 30, 2005. The decrease in average interest-earning assets was primarily attributable to a $14.4 million decrease in investment securities, offset by a $5.0 million increase in loans receivable. Average interest-bearing liabilities decreased $9.7 million, and the cost of funds increased 54 basis

points to 3.03% for the quarter ended September 30, 2006, from 2.49% for the same period in 2005. The decrease in the average balance of interest- bearing liabilities resulted primarily from an $8.3 million decrease in borrowed funds and a $1.4 million decrease in average deposits. The decrease in deposits principally occurred in the municipal money management accounts due to fluctuating deposit activities of the local municipal entities. The increase in cost of funds can be attributed to the 175 basis point increase in short-term interest rates over the past 12 months, combined with a change in the composition of deposits as $8.2 million in deposits shifted from lower cost savings accounts to higher cost certificates of deposit.

For the nine months ended September 30, 2006, net interest income, on a tax-equivalent basis, decreased $417,000, to $6.4 million, from $6.8 million for the nine months ended September 30, 2005. Net interest margin decreased 12 basis points, to 3.12% for the nine months ended September 30, 2006 from 3.24% for the nine months ended September 30, 2005. Average interest-earning assets decreased 3% to $273.1 million for the nine months ended September 30, 2006 as compared to $280.3 million for the nine months ended September 30, 2005, while the yield on interest-earning assets increased 36 basis points to 5.81% from

5.45% for the comparable periods. The decrease in average interest-earning assets was primarily attributable to an $8.3 million decrease in investment securities and a $3.3 million decrease in interest-earning deposits, partially offset by a $4.4 million increase in loans receivable. Average interest-bearing liabilities decreased $7.6 million while the cost of funds increased 52 basis points to 2.86% for the nine months ended September 30, 2006, from 2.34% for the same period in 2005. The decrease in the average balance of interest-bearing liabilities resulted from a $5.2 million decrease in average deposits and a $2.4 million decrease in borrowed funds.

INTEREST INCOME

Total interest income, on a tax-equivalent basis, for the quarter ended September 30, 2006 increased $137,000, or 4%, to $4.0 million from $3.9 million for the quarter ended September 30, 2005. The average balance of loans increased $5.0 million to $194.7 million, with yields increasing 29 basis points to 6.64% for the third quarter of 2006. Average commercial real estate loans increased $6.6 million, and the yield on those loans increased to 7.77% from 7.30% in 2005. Average commercial loans increased $2.5 million, and experienced an increase in the average yield of 19 basis points, to 8.59% from 8.40%, in 2005. Average consumer loans increased $915,000, or 5%, and experienced an increase in yield of 88 basis points. The increase in the yield on commercial and consumer loans was primarily the result of new loan originations occurring at market rates higher than the weighted average existing portfolio rate as well as the adjustable rate portions of the portfolios repricing upward in connection with Federal Reserve increases in the prime rate. Increases in the average balance of consumer and commercial loan portfolios were offset by decreases in the average balance of residential real estate loan portfolios and municipal loans. The average balance of the residential real estate portfolio decreased $4.1 million, or 3%, combined with a slight decrease in yield to 5.75% from 5.79% for the same period in 2005. The Company's municipal loan portfolio decreased $951,000, or 5%, when comparing the third quarter of 2006 to the same period in 2005. The average tax equivalent yield on the municipal loan portfolio increased to 5.87% in the third quarter of 2006 from 4.32% for the same period in 2005.

Average investment securities (taxable and tax-exempt) for the quarter ended September 30, 2006 decreased by $14.4 million when compared to the same period a year ago, with a decrease in tax-equivalent interest income from investments of $79,000, or 9%, compared to the third quarter of 2005. The average tax-equivalent yield of the portfolio increased 31 basis points, to 4.13% from 3.82%. The decrease in average investment securities was primarily due to the December 2005 sale of agency and municipal securities which had been purchased as collateral for the additional municipal deposit relationships acquired during 2004 and 2005. Additional securities were sold during the first and second quarters of 2006 following the decrease in municipal deposits.

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Total interest income, on a tax-equivalent basis, for the nine months ended September 30, 2006 increased $442,000, or 4%, when compared to the nine months ended September 30, 2005. Average loans increased $4.4 million, with average yields increasing 27 basis points to 6.54% from 6.27%. The average balance of commercial real estate increased $4.9 million, with average yields increasing to 7.72% from 7.39%, average commercial loans increased $2.9 million, with average yields increasing to 8.16% from 7.31% and average consumer loans increased $764,000 with average yields increasing to 8.06% from 7.24% for the nine moths September 30, 2005. These increases were offset by decreases in the average balance of residential real estate and municipal loans of $3.5 million and $712,000, respectively.

For the nine months ended September 30, 2006, tax-equivalent interest income from investment securities decreased $109,000, or 4%, compared to the same period in 2005. The average tax-equivalent yield of the portfolio increased 22 basis points, to 4.06% from 3.84%, offset by an $8.3 million decrease in the average balance of investment securities.

INTEREST EXPENSE

Total interest expense increased $283,000 for the three months ended September 30, 2006, when compared to the same quarter in 2005. Deposit expense for the comparable periods increased $315,000, or 30%, as the average rate paid on higher cost money management accounts increased 46 basis points to 2.52% in 2006 from 2.06% in 2005. The cost of time deposits also increased 86 basis points as existing time deposits matured and rolled over into higher cost deposits. In addition, the Bank introduced new higher cost promotional deposit products, combined with a 14% increase in the average balance of time deposit accounts to $104.7 million in 2006 from $92.2 million in 2005. The cost of other interest-bearing deposits increased slightly to 0.47% from 0.45%, offset by a 6%, or $4.8 million, decrease in the average balance of these deposits. Interest expense on borrowings decreased by $32,000, or 6%, from the prior period, resulting from a decrease in the average balance of borrowed funds of $8.3 million, or 17%, offset by an increase in the cost of borrowed funds to 5.42% from 4.75%. The increase in the cost of borrowings primarily resulted from an increase in the cost of the $5.0 million LIBOR (London Interbank Offered Rate) based junior subordinated debentures to 8.88% from 6.91%. The cost of the junior subordinated debenture adjusts quarterly.

For the nine months ended September 30, 2006, interest expense increased $859,000, or 19%, to $5.5 million from $4.7 million for the same period in 2005. The average deposit balance decreased $5.2 million, offset by a 53 basis point increase in the cost of deposits to 2.41% from 1.88%. The cost of borrowed funds increased 53 basis points to 5.24% from 4.71%, partially offset by a decrease in the average balance of borrowed funds by $2.4 million, or 6%.

PROVISION FOR LOAN LOSSES

No provision for loan losses was made for the quarter ended September 30, 2006 reflecting the Bank's improved asset quality. The Company's ratio of allowance for loan losses to period end loans has decreased to 0.83% at September 30, 2006 from 0.97% at September 30, 2005. Nonperforming loans to period end loans decreased to 0.68% at September 30, 2006 from 0.89% at September 30, 2005.

For the nine months ended September 30, 2006, the provision for loan losses was $23,000 as compared to $229,000 for the same period in 2005 primarily resulting from a decrease in the level of charge-offs to $86,000 for the nine months ended September 30, 2006 compared to $255,000 in 2005 and continued improvement in overall asset quality.

NONINTEREST INCOME

The Company's noninterest income is primarily comprised of fees charged 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 periods indicated:

	Three Months Ended September 30, 2006	2005	$Change	% Change
(Dollars in thousands)				
Service charges on deposit accounts	$ 338	$ 356	$ (18)	-5.1%
Loan servicing fees	55	61	(6)	-9.8%
Earnings on bank owned life insurance	50	44	6	13.6%
Other operating income	130	138	(8)	-5.8%
Core other income	573	599	(26)	-4.3%
Net gains/(losses) on sale of loans/ foreclosed real estate	(29)	42	(71)	-169.0%
Net losses on sales of securities	-	(192)	192	-100.0%
Total other income	$ 544	$ 449	$ 95	21.2%

	Nine Months Ended September 30, 2006	2005	$Change	% Change
(Dollars in thousands)				
Service charges on deposit accounts	$ 1,059	$ 949	$ 110	11.6%
Loan servicing fees	160	146	14	9.6%
Earnings on bank owned life insurance	150	133	17	12.8%
Other operating income	417	418	(1)	-0.2%
Core other income	1,786	1,646	140	8.5%
Net gains/(losses) on sale of loans/ foreclosed real estate	(34)	30	(64)	-213.3%
Net losses on sales of securities	(9)	(192)	183	-95.3%
Total other income	$1,743	$1,484	$ 259	17.5%

For the three months ended September 30, 2006, core other income reflected a decrease of $26,000, or 4%, when compared with the three months ended September 30, 2005. Income from service charges on deposit accounts decreased primarily due to lower net collected fees on checking account activity. The decrease in other operating income primarily resulted from a decrease in fees associated with foreign ATM usage, partially offset by an increase in Pathfinder Bank debit card usage.

For the nine months ended September 30, 2006, core other income increased $140,000 or 9%, when compared with the nine months ended September 30, 2005. The increase was primarily due to a fee enhancement program on deposit accounts which began in the second quarter of 2005.

The increase in the net losses on sales of loans/foreclosed real estate for the three and nine month period was the result of the sale of four ORE properties in the third quarter of 2006. Additionally, a gain on the sale of loans was recorded in the third quarter of 2005. There were no loan sales during the first nine months of 2006.

The decrease in the net losses on sales of investment securities for the three and nine month period was primarily due to a $192,000 other than temporary impairment charge recorded in the third quarter of 2005, with no similar charges taken in 2006.

NONINTEREST EXPENSES

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

	Three Months Ended September 30, 2006	2005	$Change	% Change
(Dollars in thousands)				
Salaries and employee benefits	$ 1,307	$1,290	$ 17	1.3%
Building occupancy	291	318	(27)	-8.5%
Data processing	328	325	3	0.9%
Professional and other services	121	172	(51)	-29.7%
Amortization of intangible assets	55	55	-	0.0%
Other operating	289	333	(44)	-13.2%
Total noninterest expense	$ 2,391	$2,493	$ (102)	-4.1%

	Nine Months Ended September 30, 2006	2005	$Change	% Change
(Dollars in thousands)				
Salaries and employee benefits	$ 3,765	$3,807	$ (42)	-1.1%
Building occupancy	913	880	33	3.8%
Data processing	958	964	(6)	-0.6%
Professional and other services	352	572	(220)	-38.5%
Amortization of intangible assets	166	166	-	0.0%
Other operating	958	1,034	(76)	-7.4%
Total noninterest expense	$ 7,112	$7,423	$ (311)	-4.2%

Total noninterest expense decreased $102,000 for the three months ended September 30, 2006, when compared to the same quarter of 2005. The decrease in building occupancy expense for the three months ended September 30, 2006, was primarily the result of a reduction of machine maintenance expenses and nonrecurring expenses associated with branch facility improvements in 2005. The decrease in professional and other expenses for the three-month period ending September 30, 2006, was primarily due to costs associated with a company wide leadership training program and process improvement initiatives that occurred in 2005. The decrease in other operating expenses was primarily attributable to lower expenses associated with foreclosed real estate, a reduction in office supplies and a reduction in costs associated with home equity loan originations.

Total noninterest expense decreased $311,000 for the nine months ended September 30, 2006 when compared to the same period of 2005. The reduction in salaries and employee benefits was primarily due to a personnel realignment in December 2005 and a reduction of expenses recognized on the employee stock ownership plan. These reductions were offset by an increase in staffing costs for the new branch that opened in June of 2005. The decrease in professional and other services was primarily due to the 2005 expenses associated with the leadership training program and process improvement initiatives. The reduction in other operating expenses was primarily due to a reduction in office supply expenses, lower expenses associated with home equity loan origination costs and mortgage recording tax expenses, a reduction in expenses on ORE property due to the number of foreclosed properties held and the recording of gains recognized on the sale of fixed assets. Building occupancy costs increased primarily due to the full nine months of operation of the new Central Square branch which opened in June 2005, combined with increased depreciation expenses.

INCOME TAX EXPENSE

Income taxes increased $89,000 and $153,000 for the quarter ended and nine months ended September 30, 2006, respectively, as compared to the same period in 2005. These increases were attributable to an increase in the Company's pre-tax income and a decrease in tax-exempt interest income. The effective tax rate was 19.0% for the three months and 17.2% for the nine months ended September 30, 2006. The Company continues to strive to reduce its tax rate from the statutory rate of 34% primarily through the ownership of tax-exempt investment securities, bank owned life insurance and other tax savings strategies. The enactment of proposed state tax legislation, which would limit the benefit derived from Real Estate Investment Trusts, would result in a higher effective state tax rate for the Company, if passed.

CHANGES IN FINANCIAL CONDITION

ASSETS

Total assets increased to $298.0 million at September 30, 2006 from $296.9 million at December 31, 2005. Loans receivable increased $7.9 million, or 4%, offset by a decrease in investment securities of $5.2 million and a $1.9 million reduction in other assets. The increase in loans receivable was primarily the result of a $5.0 million increase in commercial real estate, a $1.9 million increase in commercial loans and a $1.3 million increase in consumer loans. The decrease in investment securities was primarily the result of amortization and prepayments within the mortgage-backed securities and government and agencies portfolio.

At September 30, 2006, the securities balance included a net unrealized loss on available for sale securities of $1.6 million, as compared to a net unrealized loss of $2.2 million at December 31, 2005. These unrealized losses relate principally to changes in interest rates subsequent to the acquisition of specific securities. None of the securities in this category had an unrealized loss that exceeded 8% of the book value of the Company. The Company has the intent and ability to hold the individual securities to maturity or market price recovery.

The decrease in other assets is primarily due to the elimination of inter-company balances between the Bank and the Company which were paid off by the origination of two commercial loans in May of 2006.

LIABILITIES

Total liabilities increased slightly to $276.6 million at September 30, 2006 from $276.0 million at December 31, 2005. The slight increase in liabilities was due to a $1.5 million increase in non-interest bearing deposits and a $1.3 million increase in short-term borrowings, offset by a $2.0 million decrease in long-term borrowings. Short-term borrowings were increased to replace deposit outflows from municipal customers. The increase in non-interest bearing deposits was primarily attributable to new business account relationships and the opening of the new Central Square branch in June of 2005.

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		
(Dollars in thousands)	September 30, 2006	December 31, 2005	September 3 2005
Nonaccrual loans:			
Commercial	$ 468	$ 757	$ 336
Consumer	130	89	126
Real estate - Construction	0	0	0
Mortgage	749	834	1,179
Total nonaccrual loans	1,347	1,680	1,641
Loans past due 90 days or more and still accruing	0	0	0
Total non-performing loans	1,347	1,680	1,641
Foreclosed real estate	497	743	935
Total non-performing assets	$ 1,844	$ 2,423	$ 2,576
Non-performing loans to total loans	0.68%	0.89%	0.88
Non-performing assets to total assets	0.62%	0.82%	0.85

Total nonperforming loans and foreclosed real estate at September 30, 2006 decreased 19.8% when compared to December 31, 2005. The sharp decrease in commercial nonaccrual loans is a result of the workout of one commercial loan relationship and the foreclosure on the real estate of another relationship. No loss of principle or interest was recognized from either situation. Nonperforming loans continued to be addressed primarily through increased collection efforts and foreclosure proceedings. The decrease in foreclosed real estate is a result of a conscious effort on the bank's part to aggressively market foreclosed properties and reduce the amount of time that they are being carried. Management believes that adequate reserves exist for potential losses that may occur.

The allowance for loan losses at September 30, 2006 was $1.6 million, or 0.83% of period end loans, compared to $1.7 million, or 0.89% of period end loans, at December 31, 2005.

CAPITAL

Shareholders' equity increased $437,000, or 2%, to $21.4 million at September 30, 2006. The increase in shareholders' equity primarily resulted from a $308,000 reduction in accumulated other comprehensive loss and $118,000 in retained earnings. The Company added $713,000 to retained earnings through net income and returned $595,000 to its shareholders in the form of cash dividends. The Company's mutual holding company parent, Pathfinder Bancorp, MHC accepted the dividend for the quarter ended September 30, 2006.

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 September 30, 2006, 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%.

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 mortgage backed securities 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, and utilizes short-term borrowings as a source of liquidity when necessary.

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.

The Asset Liability Management Committees of the Company are responsible for implementing the policies and guidelines for the maintenance of prudent levels of liquidity. As of September 30, 2006, management reported to the Board of Directors that the Company is in compliance with its liquidity policy guidelines.

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 Asset-Liability Management Committees which are 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 these committees.

From 2001 until June 2004, the Federal Reserve lowered interest rates thirteen times by a total of 550 basis points. These interest rate reductions have caused significant repricing of Pathfinder 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.

Since June of 2004, the Federal Reserve has raised its key short-term interest rate 425 basis points. Net interest margin compression has resulted as the yield curve flattened from sharp increases in short-term interest rates while longer-term rates have remained relatively stable. Management will continue to seek to minimize any reduction in net interest income in a period of rising short-term 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 September 30, 2006, the total interest-bearing liabilities maturing or repricing within one year exceeded total interest-earning assets maturing or repricing in the same period by $31.4 million, representing a cumulative one-year gap ratio of a negative 10.56%.

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 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. 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.

Change in Interest Rates	NPV Capital Ratio	Percentage Change in Net Interest Income	Percentage Change in Net Portfolio Value
300	7.23%	-17.64%	-33.70%
200	8.23%	-11.60%	-22.82%
100	9.21%	-5.72%	-11.48%
0	----	----	----
-100	10.66%	2.71%	7.40%
-200	10.58%	2.00%	8.44%
-300	10.14%	-0.65%	5.64%

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 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.

PART II - OTHER INFORMATION

ITEM 1 - LEGAL PROCEEDINGS

None

ITEM 1A - RISK FACTORS

There have been no significant changes in the risk factors affecting Pathfinder Bancorp, Inc. that were identified in Item 1A of Part 1 of the Company's Form 10-K for the year ended December 31, 2005.

ITEM 2 - UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

None

ITEM 3 - DEFAULTS UPON SENIOR SECURITIES

None

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

None

ITEM 5 - OTHER INFORMATION

None

ITEM 6 - EXHIBITS

Exhibit No.	Description
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 Officer and Chief Financial Officer

SIGNATURES

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

PATHFINDER BANCORP, INC.
(Registrant)

November 14, 2006 /s/ Thomas W. Schneider
Date: Thomas W. Schneider
President, Chief Executive Officer

November 14, 2006 /s/ James A. Dowd
Date: James A. Dowd
Senior Vice President, Chief Financial Officer

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 certify that:

1. I have reviewed the September 30, 2006 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.

November 14, 2006	/s/ Thomas W. Schneider
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 certify that:

1. I have reviewed the September 30, 2006 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.

November 14, 2006	/s/ James A. Dowd
Date	James A. Dowd Senior 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 September 30, 2006 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.

November 14, 2006	/s/ Thomas W. Schneider
Date	Thomas W. Schneider President and Chief Executive Officer
November 14, 2006	/s/ James A. Dowd
Date	James A. Dowd Senior Vice President and Chief Financial Officer