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

FORM 10-Q

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

For the quarterly period ended September 30, 2019

OR

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

For the transition period from _______ to _______

PathFinder BANCORP, INC.

(Exact Name of Company as Specified in its Charter)

Maryland	001-36695	38-3941859
(State of Other Jurisdiction of Incorporation)	(Commission File No.)	(I.R.S. Employer Identification No.)

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

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

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common Stock, $0.01 par value	PBHC	The NASDAQ Stock Market LLC

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

Indicate by check mark whether the registrant has submitted electronically Interactive Data File required to be submitted 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 such files).
YES ☒ NO ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company or an emerging growth company. See definitions of “large accelerated filer,” “accelerated filer”, “smaller reporting company” and “emerging growth company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer ☐ Accelerated filer ☐ Non-accelerated filer ☒ Smaller reporting company ☒ Emerging growth company ☐

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

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

As of November 11, 2019, there were 4,707,875 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
(Unaudited)

(In thousands, except share and per share data)	September 30, 2019	December 31, 2018
ASSETS:		
Cash and due from banks	$ 19,849	$ 9,610
Interest-earning deposits (including restricted balances of $0 and $3,993, respectively)	19,924	16,706
Total cash and cash equivalents	39,773	26,316
Available-for-sale securities, at fair value	120,002	177,664
Held-to-maturity securities, at amortized cost (fair value of $116,187 and $53,769, respectively)	114,349	53,908
Marketable equity securities, at fair value	514	453
Federal Home Loan Bank stock, at cost	4,210	5,937
Loans	725,900	620,270
Less: Allowance for loan losses	8,330	7,306
Loans receivable, net	717,570	612,964
Premises and equipment, net	22,411	20,623
Operating lease right-of-use assets	2,422	-
Accrued interest receivable	3,313	3,068
Foreclosed real estate	148	1,173
Intangible assets, net	153	165
Goodwill	4,536	4,536
Bank owned life insurance	17,296	16,941
Other assets	9,423	9,367
Total assets	$ 1,056,120	$ 933,115
LIABILITIES AND SHAREHOLDERS' EQUITY:		
Deposits:		
Interest-bearing	$ 748,384	$ 623,936
Noninterest-bearing	111,225	103,124
Total deposits	859,609	727,060
Short-term borrowings	18,238	39,000
Long-term borrowings	61,014	79,534
Subordinated loans	15,119	15,094
Accrued interest payable	468	304
Operating lease liabilities	2,681	-
Other liabilities	9,800	7,664
Total liabilities	966,929	868,656
Shareholders' equity:		
Preferred stock, par value $0.01 per share; no liquidation preference; 10,000,000 and 0 shares authorized, respectively; 1,155,283 and 0 shares issued and outstanding, respectively	12	-
Common stock, par value $0.01; 25,000,000 authorized shares; 4,707,657 and 4,362,328 shares issued and outstanding, respectively	47	44
Additional paid in capital	49,236	29,139
Retained earnings	43,332	42,114
Accumulated other comprehensive loss	(2,766)	(6,042)
Unearned ESOP	(899)	(1,034)
Total Pathfinder Bancorp, Inc. shareholders' equity	88,962	64,221
Noncontrolling interest	229	238
Total equity	89,191	64,459
Total liabilities and shareholders' equity	$ 1,056,120	$ 933,115

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

Pathfinder Bancorp, Inc.
Consolidated Statements of Income
(Unaudited)

(In thousands, except per share data)	For the three months ended September 30, 2019	For the three months ended September 30, 2018	For the nine months ended September 30, 2019	For the nine months ended September 30, 2018
Interest and dividend income:				
Loans, including fees	$ 8,817	$ 7,213	$ 24,614	$ 20,949
Debt securities:				
Taxable	1,770	1,348	5,224	3,647
Tax-exempt	11	143	170	608
Dividends	63	61	214	190
Federal funds sold and interest earning deposits	72	65	288	161
Total interest and dividend income	10,733	8,830	30,510	25,555
Interest expense:				
Interest on deposits	2,845	1,839	7,930	4,750
Interest on short-term borrowings	89	41	314	204
Interest on long-term borrowings	378	338	1,158	716
Interest on subordinated loans	216	216	650	629
Total interest expense	3,528	2,434	10,052	6,299
Net interest income	7,205	6,396	20,458	19,256
Provision for loan losses	600	291	1,354	1,201
Net interest income after provision for loan losses	6,605	6,105	19,104	18,055
Noninterest income:				
Service charges on deposit accounts	399	291	1,029	838
Earnings and gain on bank owned life insurance	133	138	355	319
Loan servicing fees	57	25	144	108
Net gains (losses) on sales and redemptions of investment securities	121	(60)	232	(189)
Gains on marketable equity securities	4	-	61	26
Net gains on sales of loans and foreclosed real estate	38	8	43	24
Debit card interchange fees	166	141	497	432
Insurance agency revenue	170	174	631	639
Other charges, commissions & fees	198	223	606	662
Total noninterest income	1,286	940	3,598	2,859
Noninterest expense:				
Salaries and employee benefits	3,275	3,191	10,379	9,381
Building and occupancy	699	601	1,986	1,689
Data processing	587	492	1,749	1,404
Professional and other services	352	359	1,068	1,095
Advertising	238	158	719	626
FDIC assessments	130	152	371	407
Audits and exams	104	104	304	314
Insurance agency expense	190	190	618	679
Community service activities	110	142	392	370
Foreclosed real estate expenses	28	19	324	93
Other expenses	569	504	1,622	1,440
Total noninterest expense	6,282	5,912	19,532	17,498
Income before income taxes	1,609	1,133	3,170	3,416
Provision for income taxes	324	157	750	505
Net income attributable to noncontrolling interest and Pathfinder Bancorp, Inc.	1,285	976	2,420	2,911
Net (loss) income attributable to noncontrolling interest	(10)	(9)	4	(23)
Net income attributable to Pathfinder Bancorp Inc.	$ 1,295	$ 985	$ 2,416	$ 2,934
Convertible preferred stock dividends	70	-	139	-
Warrant dividends	7	-	15	-
Undistributed earnings allocated to participating securities	206	-	195	-
Net income available to common shareholders	$ 1,012	$ 985	$ 2,067	$ 2,934
Earnings per common share - basic	$ 0.22	$ 0.23	$ 0.47	$ 0.71
Earnings per common share - diluted	$ 0.22	$ 0.23	$ 0.47	$ 0.69
Dividends per common share	$ 0.06	$ 0.06	$ 0.18	$ 0.18

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

Pathfinder Bancorp, Inc.
Consolidated Statements of Comprehensive Income
(Unaudited)

	For the three months ended		For the nine months ended	
(In thousands)	September 30, 2019	September 30, 2018	September 30, 2019	September 30, 2018
Net Income	$ 1,285	$ 976	$ 2,420	$ 2,911
Other Comprehensive Income (Loss)				
Retirement Plans:				
Retirement plan net losses recognized in plan expenses	84	43	252	129
Unrealized holding gains (losses) on available-for-sale securities				
Unrealized holding gains (losses) arising during the period	357	(618)	4,105	(3,120)
Reclassification adjustment for net (gains) losses included in net income	(121)	60	(232)	189
Net unrealized gains (losses) on available-for-sale securities	236	(558)	3,873	(2,931)
Accretion of net unrealized loss on securities transferred to held-to-maturity(1)	6	5	22	168
Other comprehensive income (loss), before tax	326	(510)	4,147	(2,634)
Tax effect	(68)	133	(871)	688
Other comprehensive income (loss), net of tax	258	(377)	3,276	(1,946)
Comprehensive income	$ 1,543	$ 599	$ 5,696	$ 965
Comprehensive (loss) income, attributable to noncontrolling interest	$ (10)	$ (9)	$ 4	$ (23)
Comprehensive income attributable to Pathfinder Bancorp, Inc.	$ 1,553	$ 608	$ 5,692	$ 988
Tax Effect Allocated to Each Component of Other Comprehensive Income (Loss)				
Retirement plan net losses recognized in plan expenses	$ (17)	$ (12)	$ (54)	$ (34)
Unrealized holding gains (losses) arising during the period	(75)	162	(861)	815
Reclassification adjustment for net (gains) losses included in net income	25	(16)	49	(49)
Accretion of net unrealized loss on securities transferred to held-to-maturity(1)	(1)	(1)	(5)	(44)
Income tax effect related to other comprehensive income (loss)	$ (68)	$ 133	$ (871)	$ 688

(1) The accretion of the unrealized holding losses in accumulated other comprehensive loss at the date of transfer at September 30, 2013 partially offsets the amortization of the difference between the par value and the fair value of the investment securities at the date of transfer, and is an adjustment of yield.

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

Pathfinder Bancorp, Inc.
Consolidated Statements of Changes in Shareholders' Equity
Three months ended September 30, 2019 and September 30, 2018
(Unaudited)

(In thousands, except share and per share data)	Preferred Stock	Common Stock	Additional Paid in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Unearned ESOP	Non-controlling Interest	Total
Balance, June 30, 2019	$ 12	$ 47	$ 49,125	$ 42,389	$ (3,024)	$ (944)	$ 239	$ 87,844
Net income	-	-	-	1,295	-	-	(10)	1,285
Other comprehensive income, net of tax	-	-	-	-	258	-	-	258
ESOP shares earned (6,110 shares)	-	-	37	-	-	45	-	82
Stock based compensation	-	-	74	-	-	-	-	74
Common stock dividends declared ($0.06 per share)	-	-	-	(275)	-	-	-	(275)
Preferred stock dividends declared ($0.06 per share)	-	-	-	(70)	-	-	-	(70)
Warrant dividends declared ($0.06 per share)	-	-	-	(7)	-	-	-	(7)
Balance, September 30, 2019	$ 12	$ 47	$ 49,236	$ 43,332	$ (2,766)	$ (899)	$ 229	$ 89,191
Balance, June 30, 2018	$ -	$ 43	$ 28,629	$ 40,540	$ (5,471)	$ (1,124)	$ 252	$ 62,869
Net income	-	-	-	985	-	-	(9)	976
Other comprehensive loss, net of tax	-	-	-	-	(377)	-	-	(377)
ESOP shares earned (6,110 shares)	-	-	49	-	-	45	-	94
Stock based compensation	-	-	97	-	-	-	-	97
Stock options exercised	-	1	158	-	-	-	-	159
Common stock dividends declared ($0.06 per share)	-	-	-	(255)	-	-	-	(255)
Balance, September 30, 2018	$ -	$ 44	$ 28,933	$ 41,270	$ (5,848)	$ (1,079)	$ 243	$ 63,563

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, 2019 and September 30, 2018
(Unaudited)

(In thousands, except share and per share data)	Preferred Stock	Common Stock	Additional Paid in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Unearned ESOP	Non-controlling Interest	Total
Balance, January 1, 2019	$ -	$ 44	$ 29,139	$ 42,114	$ (6,042)	$ (1,034)	$ 238	$ 64,459
Net income	-	-	-	2,416	-	-	4	2,420
Other comprehensive income, net of tax	-	-	-	-	3,276	-	-	3,276
Proceeds of common stock private placement, net of expenses (1)	-	3	3,823	-	-	-	-	3,826
Proceeds of preferred stock private placement, net of expenses (1)	12	-	15,358	-	-	-	-	15,370
Effect of warrant issued from private placement (1)	-	-	373	-	-	-	-	373
ESOP shares earned (18,332 shares)	-	-	123	-	-	135	-	258
Restricted stock units (13,436 shares)	-	-	-	-	-	-	-	-
Stock based compensation	-	-	220	-	-	-	-	220
Stock options exercised	-	-	200	-	-	-	-	200
Cumulative effect of change in measurement of operating leases (2)	-	-	-	(239)	-	-	-	(239)
Common stock dividends declared ($0.18 per share)	-	-	-	(805)	-	-	-	(805)
Preferred stock dividends declared ($0.12 per share)	-	-	-	(139)	-	-	-	(139)
Warrant dividends declared ($0.12 per share)	-	-	-	(15)	-	-	-	(15)
Distributions from affiliates	-	-	-	-	-	-	(13)	(13)
Balance, September 30, 2019	$ 12	$ 47	$ 49,236	$ 43,332	$ (2,766)	$ (899)	$ 229	$ 89,191
Balance, January 1, 2018	$ -	$ 43	$ 28,170	$ 39,020	$ (4,208)	$ (1,214)	$ 333	$ 62,144
Net income (loss)	-	-	-	2,934	-	-	(23)	2,911
Other comprehensive loss, net of tax	-	-	-	-	(1,946)	-	-	(1,946)
ESOP shares earned (18,332 shares)	-	-	150	-	-	135	-	285
Restricted stock units (14,490 shares)	-	-	-	-	-	-	-	-
Stock based compensation	-	-	259	-	-	-	-	259
Stock options exercised	-	1	362	-	-	-	-	363
Cumulative effect of change in measurement of equity securities (3)	-	-	-	53	(53)	-	-	-
Cumulative effect of change in investment securities transfer (4)	-	-	-	-	359	-	-	359
Common stock dividends declared ($0.18 per share)	-	-	-	(752)	-	-	-	(752)
Cumulative effect of affiliate capital allocation	-	-	(8)	15	-	-	(7)	-
Distributions from affiliates	-	-	-	-	-	-	(60)	(60)
Balance, September 30, 2018	$ -	$ 44	$ 28,933	$ 41,270	$ (5,848)	$ (1,079)	$ 243	$ 63,563

(1) On May 8, 2019, the Company entered into a Securities Purchase Agreement with an institutional investor, in which it sold: (i) 37,700 shares of the Company's common stock, (ii) 1,155,283 shares of a new series of preferred stock, Series B convertible perpetual preferred stock; and (iii) a warrant to purchase 125,000 shares of common stock in a private placement transaction. The Company also entered into Subscription Agreements with certain directors and executive officers of the Company as well as other accredited investors. Pursuant to the Subscription Agreements, the investors purchased an aggregate of 269,277 shares of common stock.

(2) Cumulative effect of the adoption of ASU 2016-02, Leases (Topic 842), based on the difference in the right-of-use asset and lease liability as of January 1, 2019.

(3) Cumulative effect of unrealized gain on marketable equity securities based on the adoption of ASU 2016-01 - Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Liabilities.

(4) Cumulative effect of unrealized gains on the transfer of 52 investment securities from held-to-maturity classification to available-for-sale classification based on the adoption of ASU 2017-12: Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities.

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

Pathfinder Bancorp, Inc.
Consolidated Statements of Cash Flows
(Unaudited)

(In thousands)	For the nine months ended September 30, 2019	2018
OPERATING ACTIVITIES		
Net income attributable to Pathfinder Bancorp, Inc.	$ 2,416	$ 2,934
Adjustments to reconcile net income to net cash flows from operating activities:		
Provision for loan losses	1,354	1,201
Amortization of operating leases	21	-
Proceeds from sales of loans	912	216
Originations of loans held-for-sale	(903)	(212)
Realized (gains) losses on sales, redemptions and calls of:		
Real estate acquired through foreclosure	(24)	(22)
Loans	(19)	(2)
Available-for-sale investment securities	(246)	177
Held-to-maturity investment securities	14	12
Premises and equipment	-	(8)
Marketable equity securities	(61)	(26)
Depreciation	1,133	869
Amortization of mortgage servicing rights	(2)	3
Amortization of deferred loan costs	194	240
Amortization of deferred financing from subordinated debt	25	26
Earnings and gain on bank owned life insurance	(355)	(319)
Net amortization of premiums and discounts on investment securities	861	1,339
Amortization of intangible assets	12	13
Stock based compensation and ESOP expense	478	544
Net change in accrued interest receivable	(245)	132
Pension plan contribution	-	(825)
Net change in other assets and liabilities	990	(309)
Net cash flows from operating activities	6,555	5,983
INVESTING ACTIVITIES		
Purchase of investment securities available-for-sale	(50,479)	(55,284)
Purchase of investment securities held-to-maturity	(72,346)	-
Purchase of Federal Home Loan Bank stock	(6,125)	(6,439)
Proceeds from redemption of Federal Home Loan Bank stock	7,852	6,107
Proceeds from maturities and principal reductions of investment securities available-for-sale	24,935	33,650
Proceeds from maturities and principal reductions of investment securities held-to-maturity	11,273	5,238
Proceeds from sales, redemptions and calls of:		
Available-for-sale investment securities	86,555	33,421
Held-to-maturity investment securities	549	953
Real estate acquired through foreclosure	1,552	542
Premise and equipment	-	14
Purchase of bank owned life insurance	-	(5,000)
Proceeds from bank owned life insurance	-	228
Net change in loans	(106,657)	(41,111)
Purchase of premises and equipment	(2,921)	(2,176)
Net cash flows from investing activities	(105,812)	(29,857)

FINANCING ACTIVITIES		
Net change in demand deposits, NOW accounts, savings accounts, money management deposit accounts, MMDA accounts and escrow deposits	17,133	(19,633)
Net change in time deposits	49,401	43,260
Net change in brokered deposits	66,015	8,974
Net change in short-term borrowings	(20,762)	(28,600)
Payments on long-term borrowings	(26,200)	(2,000)
Proceeds from long-term borrowings	7,680	36,348
Proceeds from exercise of stock options	200	362
Cash dividends paid to common shareholders	(808)	(764)
Cash dividends paid to preferred shareholders	(69)	-
Cash dividends paid on warrants	(8)	-
Net proceeds from common stock private placement	4,199	-
Net proceeds from preferred stock private placement	15,370	-
Proceeds from finance lease transaction	572	-
Change in noncontrolling interest, net	(9)	(90)
Net cash flows from financing activities	112,714	37,857
Change in cash and cash equivalents	13,457	13,983
Cash and cash equivalents at beginning of period	26,316	21,991
Cash and cash equivalents at end of period	$ 39,773	$ 35,974
CASH PAID DURING THE PERIOD FOR:		
Interest	$ 9,888	$ 6,159
Income taxes	300	662
NON-CASH INVESTING ACTIVITY		
Real estate acquired in exchange for loans	503	320
RESTRICTED CASH		
Federal Reserve Bank Reserve Requirements included in interest earning deposits	-	4,478

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

Note 1: Basis of Presentation

The accompanying unaudited consolidated financial statements of Pathfinder Bancorp, Inc., (the “Company”), Pathfinder Bank (the “Bank”) and its other wholly owned subsidiaries have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information, the instructions for Form 10-Q and Article 8 of Regulation S-X. Accordingly, they do not include all of the information and footnotes necessary for a complete presentation of consolidated financial condition, results of operations and cash flows in conformity with generally accepted accounting principles. In the opinion of management, all adjustments, consisting of normal recurring accruals considered necessary for a fair presentation, have been included. Certain amounts in the 2018 consolidated financial statements may have been reclassified to conform to the current period presentation. These reclassifications had no effect on net income or comprehensive income as previously reported. Operating results for the three and nine months ended September 30, 2019 are not necessarily indicative of the results that may be expected for the full year ending December 31, 2019 or any other interim period.

The Company's consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States and follow practices within the banking industry. Application of these principles requires management to make estimates, assumptions, and judgments that affect the amounts reported in the 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 accounting 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 unaffiliated third-party sources, when available. When third party information is not available, valuation adjustments are estimated in good faith by management.

Although the Company owns, through its subsidiary Pathfinder Risk Management Company, Inc., 51% of the membership interest in FitzGibbons Agency, LLC (“Agency”), the Company is required to consolidate 100% of the Agency within the consolidated financial statements. The 49% of which the Company does not own is accounted for separately as noncontrolling interests within the consolidated financial statements.

Note 2: New Accounting Pronouncements

The Financial Accounting Standards Board (“FASB”) and, to a lesser extent, other authoritative rulemaking bodies promulgate generally accepted accounting principles (“GAAP”) to regulate the standards of accounting in the United States. From time to time, the FASB issues new GAAP standards, known as Accounting Standards Updates (“ASUs”) some of which, upon adoption, may have the potential to change the way in which the Company recognizes or reports within its consolidated financial statements. The following presentation provides a description of the accounting standards that are not currently effective, but could have an impact on the Company's consolidated financial statements upon adoption.

Standards Not Yet Adopted as of September 30, 2019

Standard: Measurement of Credit Losses on Financial Instruments (*ASU 2016-13: Financial Instruments—Credit Losses [Topic 326]: Measurement of Credit Losses on Financial Instruments*)

Description: The amended guidance replaces the current incurred loss model for determining the allowance for credit losses. The guidance requires financial assets measured at amortized cost to be presented at the net amount expected to be collected. The allowance for credit losses will represent a valuation account that is deducted from the amortized cost basis of the financial assets to present their net carrying value at the amount expected to be collected. The income statement will reflect the measurement of credit losses for newly recognized financial assets as well as expected increases or decreases of expected credit losses that have taken place during the period. When determining the allowance, expected credit losses over the contractual term of the financial asset(s) (taking into account prepayments) will be estimated considering relevant information about past events, current conditions, and reasonable and supportable forecasts that affect the collectability of the reported amount. The amended guidance also requires recording an allowance for credit losses for purchased financial assets with a more-than-insignificant amount of credit deterioration since origination. The initial allowance for these assets will be added to the purchase price at acquisition rather than being reported as an expense. Subsequent changes in the allowance will be recorded through the income statement as an expense adjustment. In addition, the amended guidance requires credit losses relating to available-for-sale debt securities to be recorded through an allowance for credit losses. The calculation of credit losses for available-for-sale securities will be similar to how it is determined under existing guidance.

Required Date of Implementation: January 1, 2023 (early adoption permitted as of January 1, 2019).

Effect on Consolidated Financial Statements: The Company is assessing the new guidance to determine what modifications to existing credit estimation processes may be required. The Company expects that the new guidance will result in an increase in its allowance for credit losses as a result of considering credit losses over the expected life of its loan and debt securities portfolios. Increases in the level of allowances will also reflect new requirements to include estimated credit losses on investment securities classified as held-to-maturity, if any. The Company has formed an Implementation Committee, whose membership includes representatives of senior management, to develop plans that will encompass: (1) internal methodology changes (2) data collection and management activities, (3) internal communication requirements, and (4) estimation of the projected impact of this guidance. The amount of any change in the allowance for credit losses resulting from the new guidance will ultimately be impacted by the provisions of this guidance as well as by the loan and debt security portfolios composition and asset quality at the adoption date, and economic conditions and forecasts at the time of adoption.

Standard: Transition Relief for the Implementation of ASU-2016-13 (*ASU 2019-5: Financial Instruments—Credit Losses [Topic 326]: Targeted Transition Relief*)

Description: The amendments in this ASU provide entities that have certain instruments within the scope of Subtopic 326-20, Financial Instruments—Credit Losses— Measured at Amortized Cost, with an option to irrevocably elect the fair value option in Subtopic 825-10, Financial Instruments—Overall, applied on an instrument-by-instrument basis for eligible instruments, upon adoption of Topic 326. The fair value option election does not apply to held-to-maturity debt securities. An entity that elects the fair value option should subsequently apply the guidance in Subtopics 820-10, Fair Value Measurement—Overall, and 825-10.

General guidance for the use of the fair value option is contained in Subtopic 825-10. The irrevocable election of the fair value option must be applied on an instrument-by-instrument basis for eligible instruments, whose characteristics are within the scope of Subtopic 326-20. Upon adoption of Topic 326, for items measured at fair value in accordance with paragraph 326-10-65-1(i), the difference between the carrying amount and the fair value shall be recorded by means of a cumulative-effect adjustment to the opening retained earnings balance as of the beginning of the first reporting period that an entity has adopted ASU 2016-13. Those differences may include, but are not limited to: (1) unamortized deferred costs, fees, premiums, and discounts (2) valuation allowances (for example, allowance for loan losses), or (3) accrued interest.

Required Date of Implementation: See comments above related to ASU 2016-13.

Effect on Consolidated Financial Statements: See comments above related to ASU 2016-13.

Standard: Simplifying the Test for Goodwill Impairment (*ASU 2017-04: Intangibles—Goodwill and Other [Topic 350]: Simplifying the Test for Goodwill Impairment*)

Description: Current guidance requires a two-step approach to determining if recorded goodwill is impaired. In Step 1, reporting entities must first evaluate whether or not the carrying value of a reporting unit is greater than its fair value. In Step 2, if a reporting unit's carrying value is greater than its fair value, then the entity should calculate the implied fair value of goodwill. If the carrying value of goodwill is more than the implied fair value, an impairment charge for the difference must be recorded. The amended guidance eliminates Step 2 from the goodwill impairment test. Therefore, under the new guidance, if the carrying value of a reporting unit is greater than its fair value, a goodwill impairment charge will be recorded for the difference (up to the carrying value of the recorded goodwill).

Required Date of Implementation: January 1, 2020 (early adoption permitted).

Effect on Consolidated Financial Statements: The amendments should be applied using a prospective transition method. The Company does not expect the guidance will have a material impact on its consolidated financial statements, unless at some point in the future one of its reporting units were to fail Step 1 of the goodwill impairment test.

Standard: Fair Value Measurement (*ASU 2018-13: Fair Value Measurement [Topic 820]: Disclosure Framework Changes to the Disclosure Requirements for Fair Value Measurement*
Description: The FASB is issuing the amendments in this ASU as part of the disclosure framework project. The disclosure framework project's objective and primary focus are to improve the effectiveness of disclosures in the notes to financial statements by facilitating clear communication of the information required by GAAP that is most important to users of each entity's financial statements. The amendments in this ASU modify the disclosure requirements for entities such as the Company on fair value measurements in Topic 820, Fair Value Measurement.

The following disclosure requirements were removed from Topic 820:
1. The amount of and reasons for transfers between Level 1 and Level 2 of the fair value hierarchy.
2. The policy for timing of transfers between levels.
3. The valuation processes for Level 3 fair value measurements.

The following disclosure requirements were modified in Topic 820:
1. For investments in certain entities that calculate net asset value, an entity is required to disclose the timing of liquidation of an investee's assets and the date when restrictions from redemption might lapse only if the investee has communicated the timing to the entity or announced the timing publicly.
2. The amendments clarify that the measurement uncertainty disclosure is to communicate information about the uncertainty in measurement as of the reporting date.

The following disclosure requirements were added to Topic 820:
1. The changes in unrealized gains and losses for the period included in other comprehensive income for recurring Level 3 fair value measurements held at the end of the reporting period.
2. The range and weighted average of significant unobservable inputs used to develop Level 3 fair value measurements. For certain unobservable inputs, an entity may disclose other quantitative information (such as the median or arithmetic average) in lieu of the weighted average if the entity determines that other quantitative information would be a more reasonable and rational method to reflect the distribution of unobservable inputs used to develop Level 3 fair value measurements.

Required Date of Implementation: The amendments in this ASU are effective for all entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019. The amendments on changes in unrealized gains and losses, the range and weighted average of significant unobservable inputs used to develop Level 3 fair value measurements, and the narrative description of measurement uncertainty should be applied prospectively for only the most recent interim or annual period presented in the initial fiscal year of adoption. All other amendments should be applied retrospectively to all periods presented upon their effective date. Early adoption is permitted upon issuance of this Update. An entity is permitted to early adopt any removed or modified disclosures upon issuance of this ASU and delay adoption of the additional disclosures until their effective date.

Effect on Consolidated Financial Statements: The Company does not expect the new guidance will have a material impact to its consolidated statements of condition or income.

Standard: Compensation (*ASU 2018-14: Compensation - Retirement Benefits - Defined Benefit Plans - General [Subtopic 715 – 20]: Disclosure Framework - Changes to the Disclosure Requirements for Defined Benefit Plans)*
Description: The FASB is issuing the amendments in this ASU as part of the disclosure framework project. The amendments in this ASU modify the disclosure requirements for employers that sponsor defined benefit pension or other postretirement plans.

The following disclosure requirements are removed from Subtopic 715-20:
1. The amounts in accumulated other comprehensive income expected to be recognized as components of net periodic benefit cost over the next fiscal year.
2. The amount and timing of plan assets expected to be returned to the employer.
3. Related party disclosures about the amount of future annual benefits covered by insurance and annuity contracts and significant transactions between the employer or related parties and the plan.
4. The effects of a one-percentage-point change in assumed health care cost trend rates on the (a) aggregate of the service and interest cost components of net periodic benefit costs and (b) benefit obligation for postretirement health care benefits.

The following disclosure requirements are added to Subtopic 715-20:
1. The weighted-average interest crediting rates for cash balance plans and other plans with promised interest crediting rates.
2. An explanation of the reasons for significant gains and losses related to changes in the benefit obligation for the period.

The amendments in this ASU also clarify the disclosure requirements in paragraph 715-20-50-3, which state that the following information for defined benefit pension plans should be disclosed:
1. The projected benefit obligation (PBO) and fair value of plan assets for plans with PBOs in excess of plan assets.
2. The accumulated benefit obligation (ABO) and fair value of plan assets for plans with ABOs in excess of plan assets.

Required Date of Implementation: The amendments in this ASU are effective for fiscal years ending after December 15, 2020, for public business entities and for fiscal years ending after December 15, 2021, for all other entities. Early adoption is permitted for all entities.

Effect on Consolidated Financial Statements: The Company does not expect the new guidance will have a material impact to its consolidated statements of condition or income.

Standard: Leases (*ASU 2019-01: Leases [Topic 842] Codification Improvements)*

Description: On February 25, 2016, the FASB issued Accounting Standards ASU No. 2016-02, Leases [Topic 842], to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing essential information about leasing transactions. ASU 2019-01 addresses three Issues: (1) Determining the fair value of the underlying asset by lessors that are not manufacturers or dealers; (2) Presentation on the statement of cash flows for sales-type and direct financing leases; and (3) Transition disclosures related to Topic 250, *Accounting Changes and Error Corrections*.

The amendments in this ASU address Issue 1, described above, and reinstate the exception in Topic 842 for lessors that are not manufacturers or dealers (generally financial institutions and captive finance companies). Specifically, those lessors will use their cost, reflecting any volume or trade discounts that may apply, as the fair value of the underlying asset. However, if significant time lapses between the acquisition of the underlying asset and lease commencement, those lessors will be required to apply the definition of fair value (exit price) in Topic 820.

Topic 840 does not provide guidance on how cash received from leases by lessors from sales-type and direct financing leases should be presented in the cash flow statement. The amendments in this ASU address Issue 2, described above, as to the concerns of lessors within the scope of Topic 942 about where "principal payments received under leases" should be presented. Specifically, lessors that are depository and lending institutions within the scope of Topic 942 will present all "principal payments received under leases" within investing activities in the Statement of Cash Flows.

Required Date of Implementation: The amendments in this ASU amend Topic 842. The effective date of those amendments for public business entities, such as the Company, is for fiscal years beginning after December 15, 2019 and interim periods within those fiscal years.

Effect on Consolidated Financial Statements: The Company does not expect that the new guidance will have a material impact to its consolidated statements of condition or income.

Standard: Various Codification Improvements *(ASU 2019-04: Codification Improvements to Topic 326, Financial Instruments—Credit Losses, Topic 815, Derivatives and Hedging, and Topic 825, Financial Instruments)*

Description: Since 2016, the FASB has issued the following Updates related to financial instruments:

1. Accounting Standards Update No. 2016-01, *Financial Instruments— Overall [Subtopic 825-10]: Recognition and Measurement of Financial Assets and Financial Liabilities*;
2. Accounting Standards Update No. 2016-13, *Financial Instruments— Credit Losses [Topic 326]: Measurement of Credit Losses on Financial Instruments;* and
3. Accounting Standards Update No. 2017-12, *Derivatives and Hedging [Topic 815]: Targeted Improvements to Accounting for Hedging Activities.*

The FASB has an ongoing project on its agenda for improving the Codification or correcting its unintended application. The items addressed in that project generally are not expected to have a significant effect on current accounting practice or to create a significant administrative cost for most entities. The amendments in this ASU are similar to those items and are summarized below.

For Codification Improvements specific to ASU 2016-01, the following topics were covered within ASU 2019-04:

- Scope Clarifications
- Held-to-Maturity Debt Securities Fair Value Disclosures
- Applicability of Topic 820 to the Measurement Alternative
- Remeasurement of Equity Securities at Historical Exchange Rates

The amendments to Topic 326 and other Topics in this Update include items related to the amendments in Update 2016-13 discussed at the June 2018 and November 2018 Credit Losses Transition Resource Group ("TRG") meetings.

The amendments clarify or address stakeholders' specific issues about certain aspects of the amendments in Update 2016-13 on a number of different topics, including the following:

- Accrued Interest
- Transfers between Classifications or Categories for Loans and Debt Securities
- Recoveries
- Consideration of Prepayments in Determining the Effective Interest Rate
- Consideration of Estimated Costs to Sell When Foreclosure Is Probable
- Vintage Disclosures— Line-of-Credit Arrangements Converted to Term Loans
- Contractual Extensions and Renewals

The ASU also covered a number of issues that related to hedge accounting (ASU-2017-12) including:

- Partial-Term Fair Value Hedges of Interest Rate Risk
- Amortization of Fair Value Hedge Basis Adjustments
- Disclosure of Fair Value Hedge Basis Adjustments
- Consideration of the Hedged Contractually Specified Interest Rate under the Hypothetical Derivative Method
- Scoping for Not-for-Profit Entities
- Hedge Accounting Provisions Applicable to Certain Private Companies and Not-for- Profit Entities
- Application of a First- Payments-Received Cash Flow Hedging Technique to Overall Cash Flows on a Group of Variable Interest Payments
- Transition Guidance

Required Dates of Implementation: This ASU 2019-04 has various implementation dates dependent on a number of factors as it pertains to the above items. The Company has adopted ASU 2016-01.

Effect on Consolidated Financial Statements: The Company does not expect that the new guidance will have a material impact to its consolidated statements of condition or income.

Note 3: Earnings per Common Share

The Company entered into a securities purchase agreement with Castle Creek Capital Partners VII, L.P. on May 8, 2019, pursuant to which the Company sold: (i) 37,700 shares of the Company's common stock, par value $0.01 per share, at a purchase price of $14.25 per share; (ii) 1,155,283 shares of a new series of preferred stock, Series B convertible perpetual preferred stock, par value $0.01 per share, at a purchase price of $14.25 per share; and (iii) a warrant, with an approximate fair value of $373,000, to purchase 125,000 shares of common stock at an exercise price equal to $14.25 per share, in a private placement transaction (the "Private Placement") for gross proceeds of approximately $17.0 million. As a result of the securities purchase agreement, the Company has common stock, preferred stock and a warrant that are all eligible to participate in dividends equal to the common stock dividends on a per share basis. Securities that participate in dividends, such as the Company's preferred stock and warrant, are considered "participating securities." The Company calculates net income available to common shareholders using the two-class method required for capital structures that include participating securities.

In applying the two-class method for the three and nine months ended September 30, 2019, basic net income per share was calculated by dividing net income (less any dividends on participating securities) by the weighted average number of shares of common stock and participating securities outstanding for the period. Diluted earnings per share may include the additional effect of other securities, if dilutive, in which case the dilutive effect of such securities is calculated by applying either the two-class method or the Treasury Stock method to the assumed exercise or vesting of potentially dilutive common shares. The method yielding the more dilutive result is ultimately reported for the applicable period. Potentially dilutive common stock equivalents primarily consist of employee stock options and restricted stock units. Unallocated common shares held by the ESOP are not included in the weighted average number of common shares outstanding for purposes of calculating earnings per common share until they are committed to be released to plan participants.

Basic earnings per share for the three and nine months ended September 30, 2018 were calculated by dividing net income available to common shareholders by the weighted average number of common shares outstanding during the period. Net income available to common shareholders is net income to Pathfinder Bancorp, Inc. less the total of preferred dividends declared, if any. Diluted earnings per share include the potential dilutive effect that could occur upon the assumed exercise of issued stock options using the Treasury Stock method. Unallocated common shares held by the ESOP are not included in the weighted average number of common shares outstanding for purposes of calculating earnings per common share until they are committed to be released to plan participants.

Anti-dilutive shares are common stock equivalents with average exercise prices in excess of the weighted average market price for the period presented. Anti-dilutive stock options, not included in the computation below, were -0- for the three and nine months ended September 30, 2019 and were -0- for the three and nine months ended September 30, 2018.

The following table sets forth the calculation of basic and diluted earnings per share.

	Three months ended September 30,		Nine months ended September 30,	
(In thousands, except per share data)	2019	2018	2019	2018
Net income attributable to Pathfinder Bancorp, Inc.	$ 1,295	$ 985	$ 2,416	$ 2,934
Convertible preferred stock dividends	70	-	139	-
Warrant dividends	7	-	15	-
Undistributed earnings allocated to participating securities	206	-	195	-
Net income available to common shareholders	$ 1,012	$ 985	$ 2,067	$ 2,934
Basic weighted average common shares outstanding	4,579	4,195	4,423	4,157
Effect of assumed exercise of stock options and unvested restricted stock units	-	84	-	100
Diluted weighted average common shares outstanding	4,579	4,279	4,423	4,257
Basic earnings per common share	$ 0.22	$ 0.23	$ 0.47	$ 0.71
Diluted earnings per common share	$ 0.22	$ 0.23	$ 0.47	$ 0.69

Note 4: Investment Securities

The amortized cost and estimated fair value of investment securities are summarized as follows:

	September 30, 2019			
(In thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Available-for-Sale Portfolio				
Debt investment securities:				
US Treasury, agencies and GSEs	$ 7,016	$ -	$ (30)	$ 6,986
State and political subdivisions	4,805	2	-	4,807
Corporate	12,380	301	(16)	12,665
Asset backed securities	14,364	57	(43)	14,378
Residential mortgage-backed - US agency	20,952	82	(40)	20,994
Collateralized mortgage obligations - US agency	42,073	116	(464)	41,725
Collateralized mortgage obligations - Private label	18,166	130	(55)	18,241
Total	119,756	688	(648)	119,796
Equity investment securities:				
Common stock - financial services industry	206	-	-	206
Total	206	-	-	206
Total available-for-sale	$ 119,962	$ 688	$ (648)	$ 120,002
Held-to-Maturity Portfolio				
Debt investment securities:				
US Treasury, agencies and GSEs	$ 1,996	$ 1	$ (2)	$ 1,995
State and political subdivisions	8,523	186	(2)	8,707
Corporate	24,021	600	-	24,621
Asset backed securities	17,461	117	(71)	17,507
Residential mortgage-backed - US agency	16,935	617	(1)	17,551
Collateralized mortgage obligations - US agency	20,415	406	(7)	20,814
Collateralized mortgage obligations - Private label	24,998	59	(65)	24,992
Total held-to-maturity	$ 114,349	$ 1,986	$ (148)	$ 116,187

(In thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
	December 31, 2018			
Available-for-Sale Portfolio				
Debt investment securities:				
US Treasury, agencies and GSEs	$ 17,171	$ 18	$ (158)	$ 17,031
State and political subdivisions	23,661	6	(602)	23,065
Corporate	17,389	220	(409)	17,200
Asset backed securities	18,243	13	(137)	18,119
Residential mortgage-backed - US agency	32,409	34	(777)	31,666
Collateralized mortgage obligations - US agency	48,101	31	(1,691)	46,441
Collateralized mortgage obligations - Private label	24,317	17	(398)	23,936
Total	181,291	339	(4,172)	177,458
Equity investment securities:				
Common stock - financial services industry	206	-	-	206
Total	206	-	-	206
Total available-for-sale	$ 181,497	$ 339	$ (4,172)	$ 177,664
Held-to-Maturity Portfolio				
Debt investment securities:				
US Treasury, agencies and GSEs	$ 3,987	$ -	$ (35)	$ 3,952
State and political subdivisions	5,089	22	(84)	5,027
Corporate	9,924	4	(182)	9,746
Asset backed securities	1,509	-	(13)	1,496
Residential mortgage-backed - US agency	11,601	124	(47)	11,678
Collateralized mortgage obligations - US agency	13,972	93	(13)	14,052
Collateralized mortgage obligations - Private label	7,826	17	(25)	7,818
Total held-to-maturity	$ 53,908	$ 260	$ (399)	$ 53,769

The amortized cost and estimated fair value of debt investments at September 30, 2019 by contractual maturity are shown below. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without penalties.

	Available-for-Sale		**Held-to-Maturity**	
(In thousands)	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
Due in one year or less	$ 3,318	$ 3,319	$ 2,099	$ 2,102
Due after one year through five years	12,814	13,080	18,518	18,762
Due after five years through ten years	17,380	17,392	16,093	16,610
Due after ten years	5,053	5,045	15,291	15,356
Sub-total	38,565	38,836	52,001	52,830
Residential mortgage-backed - US agency	20,952	20,994	16,935	17,551
Collateralized mortgage obligations - US agency	42,073	41,725	20,415	20,814
Collateralized mortgage obligations - Private label	18,166	18,241	24,998	24,992
Totals	$ 119,756	$ 119,796	$ 114,349	$ 116,187

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The Company's debt investment securities' gross unrealized losses and fair value, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, are as follows:

	September 30, 2019														
	Less than Twelve Months					Twelve Months or More					Total				
(Dollars in thousands)	Number of Individual Securities		Unrealized Losses		Fair Value	Number of Individual Securities		Unrealized Losses		Fair Value	Number of Individual Securities		Unrealized Losses		Fair Value
Available-for-Sale Portfolio															
US Treasury, agencies and GSE's	2	$	(30)	$	6,966	-	$	-	$	-	2	$	(30)	$	6,966
Corporate	2		(4)		1,566	4		(12)		2,269	6		(16)		3,835
Asset backed securities	4		(21)		7,266	1		(22)		895	5		(43)		8,161
Residential mortgage-backed - US agency	6		(29)		6,734	4		(11)		2,651	10		(40)		9,385
Collateralized mortgage obligations - US agency	6		(36)		10,468	15		(428)		16,212	21		(464)		26,680
Collateralized mortgage obligations - Private label	3		(22)		5,251	4		(33)		3,433	7		(55)		8,684
Totals	23	$	(142)	$	38,251	28	$	(506)	$	25,460	51	$	(648)	$	63,711
Held-to-Maturity Portfolio															
US Treasury, agencies and GSE's	1	$	(2)	$	998	-	$	-	$	-	1	$	(2)	$	998
State and political subdivisions	1		(2)		2,013	-		-		-	1		(2)		2,013
Asset backed securities	1		(71)		2,722	-		-		-	1		(71)		2,722
Residential mortgage-backed - US agency	-		-		-	1		(1)		221	1		(1)		221
Collateralized mortgage obligations - US agency	1		(7)		1,693	-		-		-	1		(7)		1,693
Collateralized mortgage obligations - Private label	5		(60)		8,318	2		(5)		1,345	7		(65)		9,663
Totals	9	$	(142)	$	15,744	3	$	(6)	$	1,566	12	$	(148)	$	17,310

	December 31, 2018														
	Less than Twelve Months					Twelve Months or More					Total				
(Dollars in thousands)	Number of Individual Securities		Unrealized Losses		Fair Value	Number of Individual Securities		Unrealized Losses		Fair Value	Number of Individual Securities		Unrealized Losses		Fair Value
Available-for-Sale Portfolio															
US Treasury, agencies and GSE's	1	$	(22)	$	977	2	$	(136)	$	12,017	3	$	(158)	$	12,994
State and political subdivisions	5		(76)		5,213	26		(526)		14,206	31		(602)		19,419
Corporate	10		(137)		8,266	4		(272)		3,374	14		(409)		11,640
Asset backed securities	7		(91)		10,470	2		(46)		3,059	9		(137)		13,529
Residential mortgage-backed - US agency	6		(83)		3,519	21		(694)		24,154	27		(777)		27,673
Collateralized mortgage obligations - US agency	3		(98)		2,792	28		(1,593)		35,765	31		(1,691)		38,557
Collateralized mortgage obligations - Private label	7		(275)		14,011	5		(123)		5,907	12		(398)		19,918
Totals	39	$	(782)	$	45,248	88	$	(3,390)	$	98,482	127	$	(4,172)	$	143,730
Held-to-Maturity Portfolio															
US Treasury, agencies and GSE's	1	$	(8)	$	982	3	$	(27)	$	2,970	4	$	(35)	$	3,952
State and political subdivisions	-		-		-	6		(84)		2,310	6		(84)		2,310
Corporate	4		(41)		3,214	2		(141)		2,507	6		(182)		5,721
Asset backed securities	1		(13)		1,496	-		-		-	1		(13)		1,496
Residential mortgage-backed - US agency	3		(8)		1,447	2		(39)		1,769	5		(47)		3,216
Collateralized mortgage obligations - US agency	4		(13)		3,972	-		-		-	4		(13)		3,972
Collateralized mortgage obligations - Private label	-		-		-	2		(25)		1,874	2		(25)		1,874
Totals	13	$	(83)	$	11,111	15	$	(316)	$	11,430	28	$	(399)	$	22,541

Excluding the effects of changes in the characteristics of individual debt securities that potentially give rise to other-than-temporary impairment ("OTTI"), as described below, the fair market value of a debt security as of a particular measurement date is highly dependent upon prevailing market and economic environmental factors at the measurement date relative to the prevailing market and economic environmental factors present at the time the debt security was acquired. The most significant market and environmental factors include, but are not limited to (1) the general level of interest rates, (2) the relationship between shorter-term interest rates and longer-term interest rates (referred to as the "slope" of the interest rate yield curve), (3) general bond market liquidity, (4) the recent and expected near-term volume of new issuances of similar debt securities, and (5) changes in the market values of individual loan collateral underlying mortgage-backed debt securities. Changes in interest rates affect the fair market values of debt securities by influencing the discount rate applied to the securities' future expected cash flows. The higher the discount rate, the lower the resultant security price. Conversely, the lower the discount rate, the higher the resultant security price. In addition, the cumulative amount and timing of undiscounted cash flows of debt securities may be also affected by changes in interest rates. For any given level of movement in the general market and economic environmental factors described above, the magnitude of any particular debt security's price changes will also depend heavily upon security-specific factors such as (1) the duration of the security, (2) imbedded optionality contractually granted to the issuer of the security with respect to principal prepayments, and (3) changes in the level of market premiums demanded by investors for securities with imbedded credit risk (where applicable).

The Company conducts a formal review of investment securities on a quarterly basis for the presence of OTTI. The Company assesses whether OTTI is present when the fair value of a debt security is less than its amortized cost basis at the statement of condition date. Under these circumstances, OTTI is considered to have occurred (1) if we intend to sell the security; (2) if it is "more likely than not" we will be required to sell the security before recovery of its amortized cost basis; or (3) the present value of expected cash flows is not anticipated to be sufficient to recover the entire amortized cost basis. The guidance requires that credit-related OTTI is recognized in earnings while non-credit-related OTTI on securities not expected to be sold is recognized in other comprehensive income ("OCI"). Non-credit-related OTTI is based on other factors, including illiquidity and changes in the general interest rate environment. Presentation of OTTI is made in the consolidated statement of income on a gross basis, including both the portion recognized in earnings as well as the portion recorded in OCI. The gross OTTI would then be offset by the amount of non-credit-related OTTI, showing the net as the impact on earnings.

Management does not believe any individual unrealized loss in securities within the portfolio as of September 30, 2019 represents OTTI. At September 30, 2019, the Bank had the following securities, in a loss position for 12 months or more relative to their amortized historical cost, which were deemed to have no credit impairment, thus, the disclosed unrealized losses relate directly to changes in interest rates subsequent to the acquisition of the individual securities. The Company does not intend to sell these securities, nor is it more likely than not that the Company will be required to sell these securities prior to the recovery of the amortized cost.

- Four corporate securities, categorized as available-for-sale, with an aggregate amortized historical cost of $2.3 million and an aggregate market value of $2.3 million (unrealized aggregate loss of $12,000, or 0.53%). Each of these securities maintains a credit rating established by one or more NRSRO above the minimum level required to be considered investment grade and, therefore, no credit-related OTTI is deemed to be present.

- One privately-issued asset-backed securities, categorized as available-for-sale, with an amortized historical cost of $917,000 and an aggregate market value of $895,000 (unrealized loss of $22,000 or 2.44%). This security maintains a credit rating established by one or more NRSRO above the minimum level required to be considered as investment grade and therefore, no credit-related OTTI is deemed to be present.

- Four privately-issued collateralized mortgage obligation securities, categorized as available-for-sale, with an aggregate amortized historical cost of $3.5 million and an aggregate market value of $3.4 million (unrealized aggregate loss of $33,000, or 0.96%). These securities were not rated at the time of their issuance by any NRSRO but each security remains significantly collateralized through subordination. Therefore, no credit-related OTTI is deemed to be present.

- Two privately-issued collateralized mortgage obligation securities, categorized as held-to-maturity, with an aggregate amortized historical cost of $1.4 million and an aggregate market value of $1.3 million (aggregate unrealized loss of $5,000, or 0.39%). These securities were not rated at the time of their issuance by any NRSRO but each security remains significantly collateralized through subordination. Therefore, no credit-related OTTI is deemed to be present.

All other securities with market values less than their amortized historical costs for twelve or more months are issued by United States agencies or government sponsored enterprises and consist of mortgage-backed securities, collateralized mortgage obligations and direct agency financings. These positions in US government agency and government-sponsored enterprises are deemed to have no credit impairment, thus, the disclosed unrealized losses relate directly to changes in interest rates subsequent to the acquisition of the individual securities. The Company does not intend to sell these securities, nor is it more likely than not that the Company will be required to sell these securities prior to the recovery of the amortized cost.

In determining whether OTTI has occurred for equity securities, the Company considers the applicable factors described above and the length of time the equity security's fair value has been below the carrying amount. The Company had no equity investment securities that were impaired at September 30, 2019 or December 31, 2018.

Gross realized gains (losses) on sales of securities for the indicated periods are detailed below:

	For the three months ended September 30,		For the nine months ended September 30,	
(In thousands)	2019	2018	2019	2018
Realized gains on investments	$ 143	$ 76	$ 544	$ 236
Realized losses on investments	(22)	(136)	(312)	(425)
	$ 121	$ (60)	$ 232	$ (189)

As of September 30, 2019 and December 31, 2018, securities with a fair value of $104.1 million and $69.8 million, respectively, were pledged to collateralize certain municipal deposit relationships. As of the same dates, securities with a fair value of $22.2 million and $19.5 million were pledged against the Company's established borrowing arrangements.

Management has reviewed its loan and mortgage-backed securities portfolios and determined that, to the best of its knowledge, only minimal exposure exists to sub-prime or other high-risk residential mortgages. With limited exceptions in the Company's investment portfolio involving the most senior tranches of securitized bonds, the Company is not in the practice of investing in, or originating, these types of investments or loans.

Note 5: Pension and Postretirement Benefits

The Company has a noncontributory defined benefit pension plan covering most employees. The plan provides defined benefits based on years of service and final average salary. On May 14, 2012, the Company informed its employees of its decision to freeze participation and benefit accruals under the plan, primarily to reduce some of the volatility in earnings that can accompany the maintenance of a defined benefit plan. The plan was frozen on June 30, 2012. Compensation earned by employees up to June 30, 2012 is used for purposes of calculating benefits under the plan but there are no future benefit accruals after this date. Participants as of June 30, 2012 will continue to earn vesting credit with respect to their frozen accrued benefits as they continue to work. In addition, the Company provides certain health and life insurance benefits for a limited number of eligible retired employees. The healthcare plan is contributory with participants' contributions adjusted annually; the life insurance plan is noncontributory. Employees with less than 14 years of service as of January 1, 1995, are not eligible for the health and life insurance retirement benefits.

The composition of net periodic pension plan and postretirement plan costs for the indicated periods is as follows:

	Pension Benefits		Postretirement Benefits		Pension Benefits		Postretirement Benefits	
	For the three months ended September 30,				For the nine months ended September 30,			
(In thousands)	2019	2018	2019	2018	2019	2018	2019	2018
Service cost	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Interest cost	124	119	6	5	371	355	16	16
Expected return on plan assets	(234)	(260)	-	-	(701)	(778)	-	-
Amortization of prior service credits	-	-	(1)	(1)	-	-	(3)	(3)
Amortization of net losses	82	41	3	3	246	123	9	9
Net periodic benefit plan (benefit) cost	$ (28)	$ (100)	$ 8	$ 7	$ (84)	$ (300)	$ 22	$ 22

The Company will evaluate the need for further contributions to the defined benefit pension plan during 2019. The prepaid pension asset is recorded in other assets on the statement of condition as of September 30, 2019 and December 31, 2018.

Note 6: Loans

Major classifications of loans at the indicated dates are as follows:

(In thousands)	September 30, 2019	December 31, 2018
Residential mortgage loans:		
1-4 family first-lien residential mortgages	$ 241,817	$ 232,523
Construction	4,241	7,121
Total residential mortgage loans	246,058	239,644
Commercial loans:		
Real estate	235,364	212,314
Lines of credit	58,408	44,235
Other commercial and industrial	80,829	63,359
Tax exempt loans	8,183	9,320
Total commercial loans	382,784	329,228
Consumer loans:		
Home equity and junior liens	47,512	26,109
Other consumer	49,486	25,424
Total consumer loans	96,998	51,533
Total loans	725,840	620,405
Net deferred loan fees	60	(135)
Less allowance for loan losses	(8,330)	(7,306)
Loans receivable, net	$ 717,570	$ 612,964

Although the Bank may occasionally purchase or fund loan participation interests outside of its primary market areas, the Bank generally originates residential mortgage, commercial, and consumer loans largely to customers throughout Oswego and Onondaga counties. Although the Bank has a diversified loan portfolio, a substantial portion of its borrowers' abilities to honor their loan contracts is dependent upon the counties' employment and economic conditions.

The Bank acquired $15.6 million, $10.2 million, and $24.6 million of loans originated by an unrelated financial institution, located outside of the Bank's market area, in January 2017, April 2017, and March 2019, respectively. The acquired loan pools represented a 90% participating interest in a total of 2,283 loans secured by liens on automobiles with maturities ranging primarily from two to six years. These loans will be serviced through their respective maturities by the originating financial institution. At September 30, 2019 and December 31, 2018, there were 1,731 loans outstanding with a remaining outstanding carrying value of $30.0 million and 909 loans outstanding with a remaining outstanding carrying value of $13.3 million, respectively. Since the acquisition of these loan pools, a total of 25 loans had cumulative net charge-offs totaling $187,000 with $67,000 in net charge-offs for the nine months ended September 30, 2019.

The Bank acquired a $5.0 million pool of consumer loans and a $5.0 million pool of commercial and industrial loans originated by an unrelated financial institution, located outside of the Bank's market area, in June 2019. The acquired loan pools represent a 100% interest in a total of 86 unsecured consumer loans and 35 commercial and industrial loans. These loans have maturities ranging primarily from four to ten years. At September 30, 2019, there were 85 unsecured consumer loans outstanding with a remaining outstanding carrying value of $4.8 million and 35 commercial and industrial loans outstanding with a remaining outstanding carrying value of $4.9 million. No charge-offs have occurred since the acquisition of these loan pools.

The Bank acquired a $21.9 million pool of home equity lines of credit originated by an unrelated financial institution, located outside of the Bank's market area, in August 2019. The acquired loan pools represent a 100% interest in a total of 395 secured home equity lines of credit. These lines of credit have maturities ranging primarily from four to thirty years. These lines of credit will be serviced through their respective maturities by the originating financial institution. At

September 30, 2019, there were 383 secured home equity lines of credit outstanding with a remaining outstanding carrying value of $21.3 million. No charge-offs have occurred since the acquisition of these loan pools.

As of September 30, 2019 and December 31, 2018, residential mortgage loans with a carrying value of $136.6 million and $154.9 million, respectively, have been pledged by the Company to the Federal Home Loan Bank of New York ("FHLBNY") under a blanket collateral agreement to secure the Company's line of credit and term borrowings.

Loan Origination / Risk Management

The Company's lending policies and procedures are presented in Note 5 to the audited consolidated financial statements included in the 2018 Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 27, 2019 and have not changed. As part of the execution of the Company's overall balance sheet management strategies, the Bank will acquire participating interests in loans originated by unrelated third parties on a sporadic basis. The purchase of participations in loans that are originated by third parties only occurs after the completion of thorough pre-acquisition due diligence. Loans in which the Company acquires a participating interest are determined to meet, in all material respects, the Company's internal underwriting policies, including credit and collateral suitability thresholds, prior to acquisition. In addition, the financial condition of the originating financial institutions, which are generally retained as the ongoing loan servicing provider for participations acquired by the Bank, are analyzed prior to the acquisition of the participating interests and monitored on a regular basis thereafter for the life of those interests.

To develop and document a systematic methodology for determining the allowance for loan losses, the Company has divided the loan portfolio into three portfolio segments, each with different risk characteristics but with similar methodologies for assessing risk. Each portfolio segment is broken down into loan classes where appropriate. Loan classes contain unique measurement attributes, risk characteristics, and methods for monitoring and assessing risk that are necessary to develop the allowance for loan losses. Unique characteristics such as borrower type, loan type, collateral type, and risk characteristics define each class.

The following table illustrates the portfolio segments and classes for the Company's loan portfolio:

Portfolio Segment	Class
Residential Mortgage Loans	1-4 family first-lien residential mortgages
	Construction
Commercial Loans	Real estate
	Lines of credit
	Other commercial and industrial
	Tax exempt loans
Consumer Loans	Home equity and junior liens
	Other consumer

The following tables present the classes of the loan portfolio, not including net deferred loan costs, summarized by the aggregate pass rating and the classified ratings of special mention, substandard and doubtful within the Company's internal risk rating system as of the dates indicated:

	As of September 30, 2019				
(In thousands)	Pass	Special Mention	Substandard	Doubtful	Total
Residential mortgage loans:					
1-4 family first-lien residential mortgages	$ 238,192	$ 1,297	$ 1,069	$ 1,259	$ 241,817
Construction	4,241	-	-	-	4,241
Total residential mortgage loans	242,433	1,297	1,069	1,259	246,058
Commercial loans:					
Real estate	224,314	7,367	2,787	896	235,364
Lines of credit	56,687	1,339	382	-	58,408
Other commercial and industrial	75,863	3,867	1,050	49	80,829
Tax exempt loans	8,183	-	-	-	8,183
Total commercial loans	365,047	12,573	4,219	945	382,784
Consumer loans:					
Home equity and junior liens	46,840	129	234	309	47,512
Other consumer	49,146	206	134	-	49,486
Total consumer loans	95,986	335	368	309	96,998
Total loans	$ 703,466	$ 14,205	$ 5,656	$ 2,513	$ 725,840

	As of December 31, 2018				
(In thousands)	Pass	Special Mention	Substandard	Doubtful	Total
Residential mortgage loans:					
1-4 family first-lien residential mortgages	$ 228,563	$ 999	$ 1,190	$ 1,771	$ 232,523
Construction	7,121	-	-	-	7,121
Total residential mortgage loans	235,684	999	1,190	1,771	239,644
Commercial loans:					
Real estate	201,997	8,299	1,947	71	212,314
Lines of credit	42,489	1,491	233	22	44,235
Other commercial and industrial	59,344	3,268	612	135	63,359
Tax exempt loans	9,320	-	-	-	9,320
Total commercial loans	313,150	13,058	2,792	228	329,228
Consumer loans:					
Home equity and junior liens	25,706	144	173	86	26,109
Other consumer	25,294	95	35	-	25,424
Total consumer loans	51,000	239	208	86	51,533
Total loans	$ 599,834	$ 14,296	$ 4,190	$ 2,085	$ 620,405

Management has reviewed its loan portfolio and determined that, to the best of its knowledge, no material exposure exists to sub-prime or other high-risk residential mortgages. The Company is not in the practice of originating these types of loans.

Nonaccrual and Past Due Loans

Loans are placed on nonaccrual when the contractual payment of principal and interest has become 90 days past due or management has serious doubts about further collectability of principal or interest, even though the loan may be currently performing.

Loans are considered past due if the required principal and interest payments have not been received within thirty days of the payment due date.

An age analysis of past due loans, not including net deferred loan costs, segregated by portfolio segment and class of loans, as of September 30, 2019 and December 31, 2018, are detailed in the following tables:

	As of September 30, 2019					
(In thousands)	30-59 Days Past Due	60-89 Days Past Due	90 Days and Over	Total Past Due	Current	Total Loans Receivable
Residential mortgage loans:						
1-4 family first-lien residential mortgages	$ 1,591	$ 775	$ 777	$ 3,143	$ 238,674	$ 241,817
Construction	-	-	-	-	4,241	4,241
Total residential mortgage loans	1,591	775	777	3,143	242,915	246,058
Commercial loans:						
Real estate	16	151	2,845	3,012	232,352	235,364
Lines of credit	15	248	392	655	57,753	58,408
Other commercial and industrial	526	415	891	1,832	78,997	80,829
Tax exempt loans	-	-	-	-	8,183	8,183
Total commercial loans	557	814	4,128	5,499	377,285	382,784
Consumer loans:						
Home equity and junior liens	391	107	276	774	46,738	47,512
Other consumer	294	115	66	475	49,011	49,486
Total consumer loans	685	222	342	1,249	95,749	96,998
Total loans	$ 2,833	$ 1,811	$ 5,247	$ 9,891	$ 715,949	$ 725,840

	As of December 31, 2018					
(In thousands)	30-59 Days Past Due	60-89 Days Past Due	90 Days and Over	Total Past Due	Current	Total Loans Receivable
Residential mortgage loans:						
1-4 family first-lien residential mortgages	$ 1,507	$ 505	$ 1,176	$ 3,188	$ 229,335	$ 232,523
Construction	-	-	-	-	7,121	7,121
Total residential mortgage loans	1,507	505	1,176	3,188	236,456	239,644
Commercial loans:						
Real estate	4,261	364	323	4,948	207,366	212,314
Lines of credit	1,033	111	22	1,166	43,069	44,235
Other commercial and industrial	814	44	387	1,245	62,114	63,359
Tax exempt loans	-	-	-	-	9,320	9,320
Total commercial loans	6,108	519	732	7,359	321,869	329,228
Consumer loans:						
Home equity and junior liens	247	6	35	288	25,821	26,109
Other consumer	226	65	107	398	25,026	25,424
Total consumer loans	473	71	142	686	50,847	51,533
Total loans	$ 8,088	$ 1,095	$ 2,050	$ 11,233	$ 609,172	$ 620,405

Nonaccrual loans, segregated by class of loan, were as follows:

(In thousands)	September 30, 2019	December 31, 2018
Residential mortgage loans:		
1-4 family first-lien residential mortgages	$ 777	$ 1,176
	777	1,176
Commercial loans:		
Real estate	2,923	415
Lines of credit	392	28
Other commercial and industrial	891	387
	4,206	830
Consumer loans:		
Home equity and junior liens	276	35
Other consumer	66	107
	342	142
Total nonaccrual loans	$ 5,325	$ 2,148

The Company is required to disclose certain activities related to Troubled Debt Restructurings ("TDR") in accordance with accounting guidance. Certain loans have been modified in a TDR where economic concessions have been granted to a borrower who is experiencing, or expected to experience, financial difficulties. These economic concessions could include a reduction in the loan interest rate, extension of payment terms, reduction of principal amortization, or other actions that it would not otherwise consider for a new loan with similar risk characteristics.

The Company is required to disclose new TDRs for each reporting period for which an income statement is being presented. The pre-modification outstanding recorded investment is the principal loan balance less the provision for loan losses before the loan was modified as a TDR. The post-modification outstanding recorded investment is the principal balance less the provision for loan losses after the loan was modified as a TDR. Additional provision for loan losses is the change in the allowance for loan losses between the pre-modification outstanding recorded investment and post-modification outstanding recorded investment.

The Company had no loans that were modified as TDRs for the three months ended September 30, 2019.

The table below details one loan that was modified as a TDR for the nine months ended September 30, 2019.

	For the nine months ended September 30, 2019			
(In thousands)	Number of loans	Pre-modification outstanding recorded investment	Post-modification outstanding recorded investment	Additional provision for loan losses
Residential real estate loans	1	$ 205	$ 250	$ -

The TDR evaluated for impairment, for the nine months ended September 30, 2019, has been classified as a TDR due to economic concessions granted, which consisted of additional funds advanced without associated increases in collateral and an extended maturity date that will result in a delay in payment from the original contractual maturity.

The Company had no loans that were modified as TDRs for the three months ended September 30, 2018.

The table below details one loan that was modified as a TDR for the nine months ended September 30, 2018.

	For the nine months ended September 30, 2018			
(In thousands)	Number of loans	Pre-modification outstanding recorded investment	Post-modification outstanding recorded investment	Additional provision for loan losses
Other commercial and industrial loans	1	$ 300	$ 300	$ -

The TDR evaluated for impairment, for the nine months ended September 30, 2018, has been classified as a TDR due to economic concessions granted, which included an extended maturity date that will result in a delay in payment from the original contractual maturity.

The Company is required to disclose loans that have been modified as TDRs within the previous 12 months in which there was payment default after the restructuring. The Company defines payment default as any loans 90 days past due on contractual payments.

The Company had no loans that were modified as TDRs during the twelve months prior to September 30, 2019, which had subsequently defaulted during the nine months ended September 30, 2019.

The Company had no loans that were modified as TDRs during the twelve months prior to September 30, 2018, which had subsequently defaulted during the nine months ended September 30, 2018.

When the Company modifies a loan within a portfolio segment that is individually evaluated for impairment, a potential impairment is analyzed either based on the present value of the expected future cash flows discounted at the interest rate of the original loan terms or the fair value of the collateral less costs to sell. If it is determined that the value of the loan is less than its recorded investment, then impairment is recognized as a component of the provision for loan losses, an associated increase to the allowance for loan losses or as a charge-off to the allowance for loan losses in the current period.

Impaired Loans

The following table summarizes impaired loan information by portfolio class at the indicated dates:

	September 30, 2019			December 31, 2018		
(In thousands)	Recorded Investment	Unpaid Principal Balance	Related Allowance	Recorded Investment	Unpaid Principal Balance	Related Allowance
With no related allowance recorded:						
1-4 family first-lien residential mortgages	$ 1,029	$ 1,029	$ -	$ 1,221	$ 1,226	$ -
Commercial real estate	4,244	4,313	-	2,387	2,448	-
Commercial lines of credit	238	238	-	228	228	-
Other commercial and industrial	584	592	-	451	452	-
Home equity and junior liens	41	41	-	-	-	-
Other consumer	56	56	-	-	-	-
With an allowance recorded:						
1-4 family first-lien residential mortgages	587	587	98	606	606	108
Commercial real estate	451	451	77	486	486	100
Commercial lines of credit	110	110	110	28	28	28
Other commercial and industrial	531	531	339	373	373	255
Home equity and junior liens	179	179	152	207	207	140
Other consumer	37	37	3	-	-	-
Total:						
1-4 family first-lien residential mortgages	1,616	1,616	98	1,827	1,832	108
Commercial real estate	4,695	4,764	77	2,873	2,934	100
Commercial lines of credit	348	348	110	256	256	28
Other commercial and industrial	1,115	1,123	339	824	825	255
Home equity and junior liens	220	220	152	207	207	140
Other consumer	93	93	3	-	-	-
Totals	$ 8,087	$ 8,164	$ 779	$ 5,987	$ 6,054	$ 631

The following table presents the average recorded investment in impaired loans for the periods indicated:

(In thousands)	For the three months ended September 30, 2019	For the three months ended September 30, 2018	For the nine months ended September 30, 2019	For the nine months ended September 30, 2018
1-4 family first-lien residential mortgages	$ 1,625	$ 1,840	$ 1,625	$ 1,846
Commercial real estate	4,578	4,497	3,723	4,976
Commercial lines of credit	359	186	323	365
Other commercial and industrial	1,131	947	1,035	1,001
Home equity and junior liens	234	207	220	228
Other consumer	95	-	73	-
Total	$ 8,022	$ 7,677	$ 6,999	$ 8,416

The following table presents the cash basis interest income recognized on impaired loans for the periods indicated:

(In thousands)	For the three months ended September 30, 2019	For the three months ended September 30, 2018	For the nine months ended September 30, 2019	For the nine months ended September 30, 2018
1-4 family first-lien residential mortgages	$ 19	$ 16	$ 54	$ 48
Commercial real estate	73	62	158	128
Commercial lines of credit	2	4	20	25
Other commercial and industrial	12	5	50	24
Home equity and junior liens	2	3	8	9
Other consumer	2	-	5	-
Total	$ 110	$ 90	$ 295	$ 234

Note 7: Allowance for Loan Losses

Summarized in the tables below are changes in the allowance for loan losses for the indicated periods and information pertaining to the allocation of the allowance for loan losses, balances of the allowance for loan losses, loans receivable based on individual, and collective impairment evaluation by loan portfolio class. An allocation of a portion of the allowance to a given portfolio class does not limit the Company's ability to absorb losses in another portfolio class.

	For the three months ended September 30, 2019				
(In thousands)	1-4 family first-lien residential mortgage	Residential construction mortgage	Commercial real estate	Commercial lines of credit	Other commercial and industrial
Allowance for loan losses:					
Beginning Balance	$ 724	$ -	$ 3,452	$ 1,145	$ 1,702
Charge-offs	-	-	-	(5)	(4)
Recoveries	-	-	-	-	1
Provisions (credits)	(77)	-	388	(84)	89
Ending balance	$ 647	$ -	$ 3,840	$ 1,056	$ 1,788
Ending balance: related to loans individually evaluated for impairment	$ 98	$ -	$ 77	$ 110	$ 339
Ending balance: related to loans collectively evaluated for impairment	$ 549	$ -	$ 3,763	$ 946	$ 1,449
Loans receivables:					
Ending balance	$ 241,817	$ 4,241	$ 235,364	$ 58,408	$ 80,829
Ending balance: individually evaluated for impairment	$ 1,616	$ -	$ 4,695	$ 348	$ 1,115
Ending balance: collectively evaluated for impairment	$ 240,201	$ 4,241	$ 230,669	$ 58,060	$ 79,714

	Tax exempt	Home equity and junior liens	Other Consumer	Unallocated	Total
Allowance for loan losses:					
Beginning Balance	$ 1	$ 386	$ 415	$ -	$ 7,825
Charge-offs	-	(7)	(107)	-	(123)
Recoveries	-	-	27	-	28
Provisions	-	95	93	96	600
Ending balance	$ 1	$ 474	$ 428	$ 96	$ 8,330
Ending balance: related to loans individually evaluated for impairment	$ -	$ 152	$ 3	$ -	$ 779
Ending balance: related to loans collectively evaluated for impairment	$ 1	$ 322	$ 425	$ 96	$ 7,551
Loans receivables:					
Ending balance	$ 8,183	$ 47,512	$ 49,486		$ 725,840
Ending balance: individually evaluated for impairment	$ -	$ 220	$ 93		$ 8,087
Ending balance: collectively evaluated for impairment	$ 8,183	$ 47,292	$ 49,393		$ 717,753

(In thousands)	1-4 family first-lien residential mortgage	Residential construction mortgage	Commercial real estate	Commercial lines of credit	Other commercial and industrial
	For the nine months ended September 30, 2019				
Allowance for loan losses:					
Beginning Balance	$ 766	$ -	$ 3,578	$ 730	$ 1,285
Charge-offs	(11)	-	-	(136)	(6)
Recoveries	1	-	-	-	1
Provisions (credits)	(109)	-	262	462	508
Ending balance	$ 647	$ -	$ 3,840	$ 1,056	$ 1,788

	Tax exempt	Home equity and junior liens	Other consumer	Unallocated	Total
Allowance for loan losses:					
Beginning Balance	$ 1	$ 409	$ 385	$ 152	$ 7,306
Charge-offs	-	(7)	(214)	-	(374)
Recoveries	-	-	42	-	44
Provisions (credits)	-	72	215	(56)	1,354
Ending balance	$ 1	$ 474	$ 428	$ 96	$ 8,330

(In thousands)	For the three months ended September 30, 2018 1-4 family first-lien residential mortgage	Residential construction mortgage	Commercial real estate	Commercial lines of credit	Other commercial and industrial
Allowance for loan losses:					
Beginning Balance	$ 722	$ -	$ 4,141	$ 731	$ 1,271
Charge-offs	(27)	-	(31)	(12)	(1)
Recoveries	1	-	-	-	-
Provisions (credits)	65	-	(170)	66	(82)
Ending balance	$ 761	$ -	$ 3,940	$ 785	$ 1,188
Ending balance: related to loans individually evaluated for impairment	$ 109	$ -	$ 593	$ 46	$ 276
Ending balance: related to loans collectively evaluated for impairment	$ 652	$ -	$ 3,347	$ 739	$ 912
Loans receivables:					
Ending balance	$ 231,830	$ 3,888	$ 213,303	$ 48,496	$ 60,984
Ending balance: individually evaluated for impairment	$ 1,835	$ -	$ 4,463	$ 162	$ 856
Ending balance: collectively evaluated for impairment	$ 229,995	$ 3,888	$ 208,840	$ 48,334	$ 60,128

	Tax exempt	Home equity and junior liens	Other Consumer	Unallocated	Total
Allowance for loan losses:					
Beginning Balance	$ 1	$ 434	$ 291	$ 14	$ 7,605
Charge-offs	-	-	(33)	-	(104)
Recoveries	-	5	6	-	12
Provisions (credits)	-	(18)	166	264	291
Ending balance	$ 1	$ 421	$ 430	$ 278	$ 7,804
Ending balance: related to loans individually evaluated for impairment	$ -	$ 140	$ -	$ -	$ 1,164
Ending balance: related to loans collectively evaluated for impairment	$ 1	$ 281	$ 430	$ 278	$ 6,640
Loans receivables:					
Ending balance	$ 10,163	$ 25,985	$ 26,410		$ 621,059
Ending balance: individually evaluated for impairment	$ -	$ 206	$ -		$ 7,522
Ending balance: collectively evaluated for impairment	$ 10,163	$ 25,779	$ 26,410		$ 613,537

(In thousands)	1-4 family first-lien residential mortgage	Residential construction mortgage	Commercial real estate	Commercial lines of credit	Other commercial and industrial
	For the nine months ended September 30, 2018				
Allowance for loan losses:					
Beginning Balance	$ 865	$ -	$ 3,589	$ 735	$ 1,214
Charge-offs	(219)	-	(31)	(62)	(172)
Recoveries	21	-	-	66	-
Provisions (credits)	94	-	382	46	146
Ending balance	$ 761	$ -	$ 3,940	$ 785	$ 1,188

	Tax exempt	Home equity and junior liens	Other consumer	Unallocated	Total
Allowance for loan losses:					
Beginning Balance	$ 1	$ 514	$ 208	$ -	$ 7,126
Charge-offs	-	(17)	(144)	-	(645)
Recoveries	-	6	29	-	122
Provisions (credits)	-	(82)	337	278	1,201
Ending balance	$ 1	$ 421	$ 430	$ 278	$ 7,804

The Company’s methodology for determining its allowance for loan losses includes an analysis of qualitative factors that are added to the historical loss rates in arriving at the total allowance for loan losses needed for this general pool of loans. The qualitative factors include:

- Changes in national and local economic trends;
- The rate of growth in the portfolio;
- Trends of delinquencies and nonaccrual balances;
- Changes in loan policy; and
- Changes in lending management experience and related staffing.

Each factor is assigned a value to reflect improving, stable or declining conditions based on management’s best judgment using relevant information available at the time of the evaluation. These qualitative factors, applied to each product class, make the evaluation inherently subjective, as it requires material estimates that may be susceptible to significant revision as more information becomes available. Adjustments to the factors are supported through documentation of changes in conditions in a narrative accompanying the allowance for loan losses analysis and calculation.

The allocation of the allowance for loan losses summarized on the basis of the Company's calculation methodology was as follows:

	September 30, 2019				
(In thousands)	1-4 family first-lien residential mortgage	Residential construction mortgage	Commercial real estate	Commercial lines of credit	Other commercial and industrial
Specifically reserved	$ 98	$ -	$ 77	$ 110	$ 339
Historical loss rate	36	-	93	37	29
Qualitative factors	513	-	3,670	909	1,420
Total	$ 647	$ -	$ 3,840	$ 1,056	$ 1,788

	Tax exempt	Home equity and junior liens	Other consumer	Unallocated	Total
Specifically reserved	$ -	$ 152	$ 3	$ -	$ 779
Historical loss rate	-	4	155	-	354
Qualitative factors	1	318	270	-	7,101
Other	-	-	-	96	96
Total	$ 1	$ 474	$ 428	$ 96	$ 8,330

	September 30, 2018				
(In thousands)	1-4 family first-lien residential mortgage	Residential construction mortgage	Commercial real estate	Commercial lines of credit	Other commercial and industrial
Specifically reserved	$ 109	$ -	$ 593	$ 46	$ 276
Historical loss rate	114	-	87	18	24
Qualitative factors	538	-	3,260	721	888
Total	$ 761	$ -	$ 3,940	$ 785	$ 1,188

	Tax exempt	Home equity and junior liens	Other consumer	Unallocated	Total
Specifically reserved	$ -	$ 140	$ -	$ -	$ 1,164
Historical loss rate	-	21	218	-	482
Qualitative factors	1	260	212	-	5,880
Other	-	-	-	278	278
Total	$ 1	$ 421	$ 430	$ 278	$ 7,804

Note 8: Foreclosed Real Estate

The Company is required to disclose the carrying amount of foreclosed residential real estate properties held as a result of obtaining physical possession of the property at each reporting period.

(Dollars in thousands)	Number of properties	September 30, 2019	Number of properties	December 31, 2018
Foreclosed residential real estate	1	$ 60	2	$ 73

At September 30, 2019 and December 31, 2018, the Company reported $302,000 and $951,000, respectively, in residential real estate loans in the process of foreclosure.

Note 9: Guarantees

The Company does not issue any guarantees that would require liability recognition or disclosure, other than its standby letters of credit. Generally, all letters of credit, when issued have expiration dates within one year. The credit risks 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 $2.2 million of standby letters of credit as of September 30, 2019. 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 fair value of standby letters of credit was not significant to the Company's consolidated financial statements.

Note 10: Fair Value Measurements

Accounting guidance related to fair value measurements and disclosures specifies a hierarchy of valuation techniques based on whether the inputs to those valuation techniques are observable or unobservable. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Company's market assumptions. These two types of inputs have created the following fair value hierarchy:

Level 1 – Quoted prices (unadjusted) for identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.

Level 2 – Quoted prices for similar assets and liabilities in active markets; quoted prices for identical or similar assets or liabilities in markets that are not active; and model-derived valuations in which all significant inputs and significant value drivers are observable in active markets.

Level 3 – Model-derived valuations in which one or more significant inputs or significant value drivers are unobservable.

An asset's or liability's level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement.

In determining fair value, the Company utilizes valuation techniques that maximize the use of observable inputs, minimize the use of unobservable inputs, to the extent possible, and considers counterparty credit risk in its assessment of fair value.

The Company used the following methods and significant assumptions to estimate fair value:

Investment securities: The fair values of available-for-sale and marketable equity securities are obtained from an independent third party and are based on quoted prices on nationally recognized securities exchanges where available (Level 1). If quoted prices are not available, fair values are measured by utilizing matrix pricing, which is a mathematical technique used widely in the industry to value debt securities without relying exclusively on quoted prices for specific securities but rather by relying on the securities' relationship to other benchmark quoted securities (Level 2). Management made no adjustment to the fair value quotes that were received from the independent third party pricing service. Level 3 securities are assets whose fair value cannot be determined by using observable measures, such as market prices or pricing models. Level 3 assets are typically very illiquid, and fair values can only be calculated using estimates or risk-adjusted value ranges. Management applies known factors, such as currently applicable discount rates, to the valuation of those investments in order to determine fair value at the reporting date.

The Company holds two corporate investment securities with an aggregate amortized historical cost of $4.8 million and an aggregate fair market value of $5.0 million as of September 30, 2019. These securities have valuations that are determined using published net asset values (NAV) derived by analyses of the securities' underlying assets. These securities are comprised primarily of broadly-diversified real estate and adjustable-rate senior secured business loans and are traded in secondary markets on an infrequent basis. While these securities are redeemable at least annually through tender offers made by their respective issuers, the liquidation value of the securities may be below their stated NAVs and also subject to restrictions as to the amount of securities that can be redeemed at any single scheduled redemption. The

Company anticipates that these securities will be redeemed by their respective issuers on indeterminate future dates as a consequence of the ultimate liquidation strategies employed by the management of these investments.

Interest rate swap derivative: The fair value of the interest rate swap derivative is calculated based on a discounted cash flow model. All future floating cash flows are projected and both floating and fixed cash flows are discounted to the valuation date. The curve utilized for discounting and projecting is built by obtaining publicly available third party market quotes for various swap maturity terms.

Impaired loans: Impaired loans are those loans in which the Company has measured impairment based on the fair value of the loan's collateral or the discounted value of expected future cash flows. Fair value is generally determined based upon market value evaluations by third parties of the properties and/or estimates by management of working capital collateral or discounted cash flows based upon expected proceeds. These appraisals may include up to three approaches to value: the sales comparison approach, the income approach (for income-producing property), and the cost approach. Management modifies the appraised values, if needed, to take into account recent developments in the market or other factors, such as, changes in absorption rates or market conditions from the time of valuation and anticipated sales values considering management's plans for disposition. Such modifications to the appraised values could result in lower valuations of such collateral. Estimated costs to sell are based on current amounts of disposal costs for similar assets. These measurements are classified as Level 3 within the valuation hierarchy. Impaired loans are subject to nonrecurring fair value adjustment upon initial recognition or subsequent impairment. A portion of the allowance for loan losses is allocated to impaired loans if the value of such loans is deemed to be less than the unpaid balance.

Foreclosed real estate: Fair values for foreclosed real estate are initially recorded based on market value evaluations by third parties, less costs to sell ("initial cost basis"). Any write-downs required when the related loan receivable is exchanged for the underlying real estate collateral at the time of transfer to foreclosed real estate are charged to the allowance for loan losses. Values are derived from appraisals, similar to impaired loans, of underlying collateral or discounted cash flow analysis. Subsequent to foreclosure, valuations are updated periodically and assets are marked to current fair value, not to exceed the initial cost basis. In the determination of fair value subsequent to foreclosure, management also considers other factors or recent developments, such as, changes in absorption rates and market conditions from the time of valuation and anticipated sales values considering management's plans for disposition. Either change could result in adjustment to lower the property value estimates indicated in the appraisals. These measurements are classified as Level 3 within the fair value hierarchy.

The following tables summarize assets measured at fair value on a recurring basis as of the indicated dates, segregated by the level of valuation inputs within the hierarchy utilized to measure fair value:

	September 30, 2019			
(In thousands)	Level 1	Level 2	Level 3	Total Fair Value
Available-for-Sale Portfolio				
Debt investment securities:				
US Treasury, agencies and GSEs	$ -	$ 6,986	$ -	$ 6,986
State and political subdivisions	-	4,807	-	4,807
Corporate	-	7,621	-	7,621
Asset backed securities	-	14,378	-	14,378
Residential mortgage-backed - US agency	-	20,994	-	20,994
Collateralized mortgage obligations - US agency	-	41,725	-	41,725
Collateralized mortgage obligations - Private label	-	18,241	-	18,241
Total		114,752		114,752
Corporate measured at NAV	-	-	-	5,044
Total available-for-sale securities	$ -	$ 114,752	$ -	$ 119,796
Marketable equity securities	$ -	$ 514	$ -	$ 514
Interest rate swap derivative	$ -	$ (115)	$ -	$ (115)

(In thousands)	December 31, 2018 Level 1	Level 2	Level 3	Total Fair Value
Available-for-Sale Portfolio				
Debt investment securities:				
US Treasury, agencies and GSEs	$ -	$ 17,031	$ -	$ 17,031
State and political subdivisions	-	23,065	-	23,065
Corporate	-	12,141	-	12,141
Asset backed securities	-	18,119	-	18,119
Residential mortgage-backed - US agency	-	31,666	-	31,666
Collateralized mortgage obligations - US agency	-	46,441	-	46,441
Collateralized mortgage obligations - Private label	-	23,936	-	23,936
Total		172,399		172,399
Corporate measured at NAV	-	-	-	5,059
Total available-for-sale securities	$ -	$ 172,399	$ -	$ 177,458
Marketable equity securities	$ -	$ 453	$ -	$ 453

Pathfinder Bank had the following assets measured at fair value on a nonrecurring basis as of September 30, 2019 and December 31, 2018:

(In thousands)	September 30, 2019 Level 1	Level 2	Level 3	Total Fair Value
Impaired loans	$ -	$ -	$ 3,055	$ 3,055
Foreclosed real estate	$ -	$ -	$ 60	$ 60

(In thousands)	December 31, 2018 Level 1	Level 2	Level 3	Total Fair Value
Impaired loans	$ -	$ -	$ 1,098	$ 1,098
Foreclosed real estate	$ -	$ -	$ 1,173	$ 1,173

The following table presents additional quantitative information about assets measured at fair value on a nonrecurring basis and for which Level 3 inputs were used to determine fair value at the indicated dates.

	Quantitative Information about Level 3 Fair Value Measurements Valuation Techniques	Unobservable Input	Range (Weighted Avg.)
At September 30, 2019			
Impaired loans	Appraisal of collateral	Appraisal Adjustments	5% - 20% (9%)
	(Sales Approach)	Costs to Sell	7% - 13% (10%)
	Discounted Cash Flow		
Foreclosed real estate	Appraisal of collateral	Appraisal Adjustments	15% - 15% (15%)
	(Sales Approach)	Costs to Sell	6% - 9% (8%)

	Quantitative Information about Level 3 Fair Value Measurements		
	Valuation Techniques	Unobservable Input	Range (Weighted Avg.)
At December 31, 2018			
Impaired loans	Appraisal of collateral	Appraisal Adjustments	5% - 15% (6%)
	(Sales Approach)	Costs to Sell	5% - 13% (11%)
	Discounted Cash Flow		
Foreclosed real estate	Appraisal of collateral	Appraisal Adjustments	15% - 15% (15%)
	(Sales Approach)	Costs to Sell	6% - 8% (7%)

There have been no transfers of assets into or out of any fair value measurement during the three and nine months ended September 30, 2019.

Required disclosures include fair value information of financial instruments, whether or not recognized in the consolidated statement of condition, for which it is practicable to estimate that value. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. In that regard, the derived fair value estimates cannot be substantiated by comparison to independent markets and, in many cases, could not be realized in immediate settlement of the instrument.

The Company has various processes and controls in place to ensure that fair value is reasonably estimated. The Company performs due diligence procedures over third-party pricing service providers in order to support their use in the valuation process.

While the Company believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date.

Management uses its best judgment in estimating the fair value of the Company's financial instruments; however, there are inherent weaknesses in any estimation technique. Therefore, for substantially all financial instruments, the fair value estimates herein are not necessarily indicative of the amounts the Company could have realized in a sales transaction on the dates indicated. The estimated fair value amounts have been measured as of their respective period-ends, and have not been re-evaluated or updated for purposes of these financial statements subsequent to those respective dates. As such, the estimated fair values of these financial instruments subsequent to the respective reporting dates may be different than the amounts reported at each period-end.

FASB ASC Topic 820 for Fair Value Measurements and Disclosures, the financial assets and liabilities were valued at a price that represents the Company's exit price or the price at which these instruments would be sold or transferred.

The following information should not be interpreted as an estimate of the fair value of the entire Company since a fair value calculation is only provided for a limited portion of the Company's assets and liabilities. Due to a wide range of valuation techniques and the degree of subjectivity used in making the estimates, comparisons between the Company's disclosures and those of other companies may not be meaningful. The Company, in estimating its fair value disclosures for financial instruments, used the following methods and assumptions:

Cash and cash equivalents – The carrying amounts of these assets approximate their fair value and are classified as Level 1.

Investment securities – The fair values of available-for-sale, held-to-maturity and marketable equity securities are obtained from an independent third party and are based on quoted prices on nationally recognized exchange where available (Level 1). If quoted prices are not available, fair values are measured by utilizing matrix pricing, which is a mathematical technique used widely in the industry to value debt securities without relying exclusively on quoted prices for specific securities, but rather by relying on the securities' relationship to other benchmark quoted securities (Level 2). Management made no adjustment to the fair value quotes that were received from the independent third party pricing service. Level 3 securities are assets whose fair value cannot be determined by using observable measures, such as market prices or pricing models. Level 3 assets are typically very illiquid, and fair values can only be calculated using estimates or risk-adjusted value ranges. Management applies known factors, such as currently applicable discount rates, to the valuation of those investments in order to determine fair value at the reporting date.

The Company holds two corporate investment securities with an aggregate amortized historical cost of $4.8 million and an aggregate fair market value of $5.0 million as of September 30, 2019. These securities have valuations that are determined using published NAV derived by analyses of the securities' underlying assets. These securities are comprised primarily of broadly-diversified real estate and adjustable-rate senior secured business loans and are traded in secondary markets on an infrequent basis. While these securities are redeemable at least annually through tender offers made by their respective issuers, the liquidation value of the securities may be below their stated NAVs and also subject to restrictions as to the amount of securities that can be redeemed at any single scheduled redemption. The Company anticipates that these securities will be redeemed by their respective issuers on indeterminate future dates as a consequence of the ultimate liquidation strategies employed by the management of these investments.

Federal Home Loan Bank stock – The carrying amount of these assets approximates their fair value and are classified as Level 2.

Net loans – For variable-rate loans that re-price frequently, fair value is based on carrying amounts. The fair value of other loans (for example, fixed-rate commercial real estate loans, mortgage loans, and commercial and industrial loans) is estimated using discounted cash flow analysis, based on interest rates currently being offered in the market for loans with similar terms to borrowers of similar credit quality. Loan value estimates include judgments based on expected prepayment rates. The measurement of the fair value of loans, including impaired loans, is classified within Level 3 of the fair value hierarchy.

Accrued interest receivable and payable – The carrying amount of these assets approximates their fair value and are classified as Level 1.

Deposits – The fair values disclosed for demand deposits (e.g., interest-bearing and noninterest-bearing checking, passbook savings and certain types of money management accounts) are, by definition, equal to the amount payable on demand at the reporting date (i.e., their carrying amounts) and are classified within Level 1 of the fair value hierarchy. Fair values for fixed-rate certificates of deposit are estimated using a discounted cash flow calculation that applies interest rates currently being offered in the market on certificates of deposits to a schedule of aggregated expected monthly maturities on time deposits. Measurements of the fair value of time deposits are classified within Level 2 of the fair value hierarchy.

Borrowings – Fixed/variable term "bullet" structures are valued using a replacement cost of funds approach. These borrowings are discounted to the FHLBNY advance curve. Option structured borrowings' fair values are determined by the FHLB for borrowings that include a call or conversion option. If market pricing is not available from this source, current market indications from the FHLBNY are obtained and the borrowings are discounted to the FHLBNY advance curve less an appropriate spread to adjust for the option. These measurements are classified as Level 2 within the fair value hierarchy.

Subordinated loans – The Company secures quotes from its pricing service based on a discounted cash flow methodology or utilizes observations of recent highly-similar transactions which result in a Level 2 classification.

Interest rate swap derivative – The fair value of the interest rate swap derivative is obtained from a third party pricing agent and is calculated based on a discounted cash flow model. All future floating cash flows are projected and both floating and fixed cash flows are discounted to the valuation date. The curve utilized for discounting and projecting is built by obtaining publicly available third party market quotes for various swap maturity terms, and therefore is classified within Level 2 of the fair value hierarchy.

The carrying amounts and fair values of the Company's financial instruments as of the indicated dates are presented in the following table:

		September 30, 2019		December 31, 2018	
(In thousands)	Fair Value Hierarchy	Carrying Amounts	Estimated Fair Values	Carrying Amounts	Estimated Fair Values
Financial assets:					
Cash and cash equivalents	1	$ 39,773	$ 39,773	$ 26,316	$ 26,316
Investment securities - available-for-sale	2	114,752	114,752	172,399	172,399
Investment securities - available-for-sale	NAV	5,044	5,044	5,059	5,059
Investment securities - marketable equity	2	514	514	453	453
Investment securities - held-to-maturity	2	114,349	116,187	53,908	53,769
Federal Home Loan Bank stock	2	4,210	4,210	5,937	5,937
Net loans	3	717,570	717,687	612,964	601,789
Accrued interest receivable	1	3,313	3,313	3,068	3,068
Financial liabilities:					
Demand Deposits, Savings, NOW and MMDA	1	$ 467,391	$ 467,391	$ 450,267	$ 450,267
Time Deposits	2	392,218	393,320	276,793	275,727
Borrowings	2	79,252	79,742	118,534	118,379
Subordinated loans	2	15,119	14,766	15,094	14,485
Accrued interest payable	1	468	468	304	304
Interest rate swap derivative	2	115	115	-	-

Note 11: Interest Rate Derivatives

The Company is exposed to certain risks from both its business operations and economic conditions. The Company principally manages its exposures to a wide variety of business and operational risks through the management of its core business activities. As part of the Company's overall risk management processes, the Company manages its economic risks, including interest rate, liquidity and credit risk, primarily by managing the amount, sources and duration of certain balance sheet assets and liabilities. In the normal course of business, the Company also uses derivative financial instruments as an additional risk management tool. Financial derivatives are recorded at fair value as other assets.

The accounting for changes in the fair value of a derivative depends on whether it has been designated and qualifies as part of a hedging relationship. There are two primary types of interest rate derivatives that may be employed by the Company:

- *Fair Value Hedge* - As a result of interest rate fluctuations, fixed-rate assets and liabilities will appreciate or depreciate in fair value. When effectively hedged, this appreciation or depreciation will generally be offset by fluctuations in the fair value of derivative instruments that are linked to the hedged assets and liabilities. This strategy is referred to as a fair value hedge. For a fair value hedge, changes in the fair value of the derivative instrument and changes in the fair value of the hedged asset or liability are recognized currently in earnings.

- *Cash Flow Hedge* - Cash flows related to floating rate assets and liabilities will fluctuate with changes in the underlying rate index. When effectively hedged, the increases or decreases in cash flows related to the floating-rate asset or liability will generally be offset by changes in cash flows of the derivative instrumnets designated as a hedge. This strategy is referred to as a cash flow hedge. For a cash flow hedge, changes in the fair value of the derivative instrument, to the extent that it is effective, are recorded in other comprehensive income and subsequently reclassified to earnings as the hedged transaction impacts net income. Any ineffective portion of a cash flow hedge is recognized currently in earnings.

Among the array of interest rate derivative transactions potentially available to the Company are interest rate swaps. The Company uses interest rate swaps as part of its interest rate risk management strategy. Interest rate swaps, designated as fair value hedges, involve the receipt of variable amounts from a counterparty in exchange for the Company making fixed payments over the life of the agreements without the exchange of the underlying notional amount. The gain or loss on the derivative as well as the offsetting gain of loss on the hedged item attributable to the hedged risk are recognized in earnings. The Company entered into a pay-fixed/receive variable interest rate swap with a notional amount of $9.2 million in April 2019, which was designated as a fair value hedge associated with specific pools within the Company's fixed-rate consumer loan portfolio.

As of September 30, 2019, the following amounts were recorded on the balance sheet related to the cumulative basis adjustments for fair value hedges:

(In thousands)	Carrying Amount of the Hedged Assets at September 30, 2019	Cumulative Amount of Fair Value Hedging Adjustment Included in The Carrying Amount of the Hedged Assets at September 30, 2019
Line item on the balance sheet in which the hedged item is included:		
Loans receivable (1)	$ 20,952	$ 92

(1) These amounts include the amortized cost basis of the closed portfolio used to designate the hedging relationship in which the hedged item is the remaining amortized cost of the last layer expected to be remaining at the end of the hedging relationship. At September 30, 2019, the amortized cost of the basis of the closed portfolio used in the hedging relationship was $21.0 million, the cumulative basis adjustment associated with the hedging relationship was $92,000, and the amount of the designated hedged item was $9.2 million.

At September 30, 2019, the fair value of the derivative resulted in a net liability position of $115,000 under the agreement, recorded by the Company in other liabilities. The Company had no derivative agreements in place at December 31, 2018.

The Company manages its potential credit exposure on interest rate swap transactions by entering into a bilateral credit support agreements with each counterparty. These agreements require collateralization of credit exposures beyond specified minimum threshold amounts. The Company's agreement with its interest rate swap counterparty contains a provision whereby if either party defaults on any of its indebtedness, then that party could also be declared in default on its derivative obligations. The agreement with the Company's derivative counterparty also includes certain other provisions that if not met, could result in the Company or the counterparty being declared in default. If either the Company or the counterparty were to be declared in default, the other party to the agreement can terminate the derivative position and require settlement of all obligations as specifically outlined within the terms of the agreement.

Note 12: Accumulated Other Comprehensive Income (Loss)

Changes in the components of accumulated other comprehensive income (loss) ("AOCI"), net of tax, for the periods indicated are summarized in the table below.

	For the three months ended September 30, 2019			
(In thousands)	Retirement Plans	Unrealized Gains and Losses on Available-for-Sale Securities	Unrealized Loss on Securities Transferred to Held-to-Maturity	Total
Beginning balance	$ (3,021)	$ 43	$ (46)	$ (3,024)
Other comprehensive income before reclassifications	-	282	5	287
Amounts reclassified from AOCI	67	(96)	-	(29)
Ending balance	$ (2,954)	$ 229	$ (41)	$ (2,766)

	For the three months ended September 30, 2018			
(In thousands)	Retirement Plans	Unrealized Gains and Losses on Available-for-Sale Securities	Unrealized Loss on Securities Transferred to Held-to-Maturity	Total
Beginning balance	$ (2,156)	$ (3,248)	$ (67)	$ (5,471)
Other comprehensive income before reclassifications	-	(456)	4	(452)
Amounts reclassified from AOCI	31	44	-	75
Ending balance	$ (2,125)	$ (3,660)	$ (63)	$ (5,848)

	For the nine months ended September 30, 2019			
(In thousands)	Retirement Plans	Unrealized Gains and Losses on Available-for-Sale Securities	Unrealized Loss on Securities Transferred to Held-to-Maturity	Total
Beginning balance	$ (3,152)	$ (2,832)	$ (58)	$ (6,042)
Other comprehensive income before reclassifications	-	3,244	17	3,261
Amounts reclassified from AOCI	198	(183)	-	15
Ending balance	$ (2,954)	$ 229	$ (41)	$ (2,766)

	For the nine months ended September 30, 2018			
(In thousands)	Retirement Plans	Unrealized Gains and Losses on Available-for-Sale Securities	Securities reclassified from AFS to HTM	Total
Beginning balance	$ (2,220)	$ (1,558)	$ (430)	$ (4,208)
Other comprehensive income before reclassifications	-	(2,305)	124	(2,181)
Amounts reclassified from AOCI	95	140	-	235
Cumulative effect of change in measurement of equity securities (1)	-	(53)	-	(53)
Cumulative effect of change in investment securities transfer (2)	-	116	243	359
Ending balance	$ (2,125)	$ (3,660)	$ (63)	$ (5,848)

(1) Cumulative effect of unrealized gain on marketable equity securities based on the adoption of ASU 2016-01 – Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Liabilities.

(2) Cumulative effect of unrealized gains on the transfer of 52 investment securities from held-to-maturity classification to available-for-sale classification based on the adoption of ASU 2017-12: Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities.

The following table presents the amounts reclassified out of each component of AOCI for the indicated period:

(In thousands)	Amount Reclassified from AOCI (1) (Unaudited) For the three months ended			Amount Reclassified from AOCI (1) (Unaudited) For the nine months ended	
Details about AOCI (1) components	September 30, 2019	September 30, 2018	Affected Line Item in the Statement of Income	September 30, 2019	September 30, 2018
Retirement plan items					
Retirement plan net losses recognized in plan expenses (2)	$ (84)	$ (43)	Salaries and employee benefits	$ (252)	$ (129)
Tax effect	17	12	Provision for income taxes	54	34
	$ (67)	$ (31)	Net Income	$ (198)	$ (95)
Available-for-sale securities					
Realized gain (loss) on sale of securities	$ 121	$ (60)	Net gains (losses) on sales and redemptions of investment securities	$ 232	$ (189)
Tax effect	(25)	16	Provision for income taxes	(49)	49
	$ 96	$ (44)	Net Income	$ 183	$ (140)

(1) Amounts in parentheses indicates debits in net income.

(2) These items are included in net periodic pension cost. See Note 5 for additional information.

Note 13: Noninterest Income

The Company has included the following table regarding the Company's noninterest income for the periods presented.

(In thousands)	For the three months ended September 30, 2019	2018	For the nine months ended September 30, 2019	2018
Service fees				
Insufficient funds fees	$ 347	$ 218	$ 827	$ 618
Deposit related fees	28	49	133	148
ATM fees	24	24	69	72
Total service fees	399	291	1,029	838
Fee Income				
Insurance commissions	168	172	620	632
Investment services revenue	58	70	203	218
ATM fees surcharge	68	71	173	178
Banking house rents collected	32	34	100	100
Total fee income	326	347	1,096	1,128
Card income				
Debit card interchange fees	166	141	497	432
Merchant card fees	21	21	58	54
Total card income	187	162	555	486
Mortgage fee income and realized gain on sale of loans and foreclosed real estate				
Loan servicing fees	57	25	144	108
Net gains on sales of loans and foreclosed real estate	38	8	43	24
Total mortgage fee income and realized gain on sale of loans and foreclosed real estate	95	33	187	132
Total	1,007	833	2,867	2,584
Earnings and gain on bank owned life insurance	133	138	355	319
Net gains (losses) on sales and redemptions of investment securities	121	(60)	232	(189)
Gains on marketable equity securities	4	-	61	26
Other miscellaneous income	21	29	83	119
Total noninterest income	$ 1,286	$ 940	$ 3,598	$ 2,859

The following is a discussion of key revenues within the scope of the new revenue guidance:

- *Service fees* – Revenue is earned through insufficient funds fees, customer initiated activities or passage of time for deposit related fees, and ATM service fees. Transaction-based fees are recognized at the time the transaction is executed, which is the same time the Company's performance obligation is satisfied. Account maintenance fees are earned over the course of the month as the monthly maintenance performance obligation to the customer is satisfied.
- *Fee income* – Revenue is earned through commissions on insurance and securities sales, ATM surcharge fees, and banking house rents collected. The Company earns investment advisory fee income by providing investment management services to customers under investment management contracts. As the direction of investment management accounts is provided over time, the performance obligation to investment management customers is satisfied over time, and therefore, revenue is recognized over time.
- *Card income* – Card income consists of interchange fees from consumer debit card networks and other related services. Interchange rates are set by the card networks. Interchange fees are based on purchase volumes and other factors and are recognized as transactions occur.
- *Mortgage fee income and realized gain on sale of loans and foreclosed real estate* – Revenue from mortgage fee income and realized gain on sale of loans and foreclosed real estate is earned through the origination of residential

and commercial mortgage loans, sales of one-to-four family residential mortgage loans, sales of government guarantees portions of SBA loans, and sales of foreclosed real estate, and is earned as the transaction occurs.

Note 14: Leases

The Company has operating and finance leases for certain banking offices and land under noncancelable agreements. Our leases have remaining lease terms that vary from less than one year up to 31 years, some of which include options to extend the leases for various renewal periods. All options to renew are included in the current lease term when we believe it is reasonably certain that the renewal options will be exercised.

The Company elected to adopt the transition relief under Topic 842, Leases, using the modified retrospective transition method. The periods presented prior to January 1, 2019 continue to be in accordance with ASC 840.

The components of the lease expense are as follows:

(In thousands)	For the three months ended September 30, 2019	For the nine months ended September 30, 2019
Operating lease cost	$ 61	$ 180
Finance lease cost	20	32

(In thousands)	For the three months ended September 30, 2019	For the nine months ended September 30, 2019
Cash paid for amount included in the measurement of lease liabilities:		
Operating cash flows from operating leases	$ 55	$ 159
Operating cash flows from finance leases	20	32
Financing cash flows from finance leases	17	28

Supplemental balance sheet information related to leases was as follows:

(In thousands, except lease term and discount rate)	September 30, 2019
Operating Leases:	
Operating lease right-of-use assets	$ 2,422
Operating lease liabilities	$ 2,681
Finance Leases:	
Financial Liability	$ 576
Weighted Average Remaining Lease Term:	
Operating Leases	19.71 years
Finance Leases	29.67 years
Weighted Average Discount Rate:	
Operating Leases	3.71%
Finance Leases	13.75%

Maturities of lease liabilities were as follows:

Years Ending September 30,		
(In thousands)		
2020	$	117
2021		104
2022		97
2023		107
2024		116
Thereafter		2,716
Total minimum lease payments	$	3,257

The Company owns certain properties that it leases to unaffiliated third parties at market rates. Lease rental income was $32,000 and $34,000 for the three months ended September 30, 2019 and 2018, respectively. Lease rental income was $100,000 for both the nine months ended September 30, 2019 and 2018. All lease agreements, in which the Company is the lessor, are accounted for as operating leases. The Company has no unamortized initial direct costs related to the establishment of these lease agreements at January 1, 2019.

Note 15: Subsequent Events

On November 7, 2019, the Bank acquired $25.1 million of loans originated by an unrelated financial technology company, located outside of the Bank's market area. The acquired loan pool represents a 55.9% participating interest in a total of 2,787 unsecured consumer loans with maturities ranging primarily from three to five years. These loans will be serviced through their respective maturities by the originating financial technology company.

The Company's management routinely evaluates the overall characteristics of its loan portfolio. Such evaluations may include analyses of certain loans for potential sales to unaffiliated third parties. Loan sales may be made in response to a variety of factors such as changes in market conditions or changes in the level of certain loan-type concentrations. Such sales, if executed, would typically be made in order to improve certain characteristics within the overall loan portfolio, viewed individually or in combination, related to factors such as cash flow, liquidity, duration or potential interest rate risk. As of the date of the issuance of this filing, the Company was in the process of evaluating the sale of certain conforming 30-year loans that have been held in portfolio for the past two-to-five years. The sale of loans of this type would typically reduce the overall duration of the loan portfolio and would, therefore, generally reduce the Company's exposure to the effects of rising interest rates. As of the date of this filing, no decision has been made to sell the loans currently being evaluated. The amount of any potential sale, the expected gain or loss on such a sale, or the potential effects on future earnings of such a sale has not been determined.

Item 2 - Management's Discussion and Analysis of Financial Condition and Results of Operations (Unaudited)

General

The Company is a Maryland corporation headquartered in Oswego, New York. The Company is 100% owned by public shareholders. The primary business of the Company is its investment in Pathfinder Bank (the "Bank"), a New York State chartered commercial bank, which is 100% owned by the Company. The Bank has two wholly owned operating subsidiaries, Pathfinder Risk Management Company, Inc. ("PRMC") and Whispering Oaks Development Corp. All significant inter-company accounts and activity have been eliminated in consolidation. Although the Company owns, through its subsidiary PRMC, 51% of the membership interest in FitzGibbons Agency, LLC ("Agency"), the Company is required to consolidate 100% of FitzGibbons within the consolidated financial statements. The 49% of which the Company does not own is accounted for separately as a noncontrolling interest within the consolidated financial statements. At September 30, 2019, the Company and subsidiaries had total consolidated assets of $1.1 billion, total consolidated liabilities of $966.9 million and shareholders' equity of $89.0 million plus noncontrolling interest of $229,000, which represents the 49% of FitzGibbons not owned by the Company.

The following discussion reviews the Company's financial condition at September 30, 2019 and the results of operations for the three and nine month periods ended September 30, 2019 and 2018. Operating results for the three and nine months ended September 30, 2019 are not necessarily indicative of the results that may be expected for the year ending December 31, 2019 or any other period.

The following material under the heading "Management's Discussion and Analysis of Financial Condition and Results of Operations" is written with the presumption that the users of the interim financial statements have read, or have access to, the Company's latest audited financial statements and notes thereto, together with Management's Discussion and Analysis of Financial Condition and Results of Operations included in the 2018 Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 27, 2019 (“the consolidated annual financial statements”) as of December 31, 2018 and 2017 and for the two years then ended. Therefore, only material changes in financial condition and results of operations are discussed in the remainder of Item 2.

Statement Regarding Forward-Looking Statements

This report contains forward-looking statements that are based on assumptions and may describe future plans, strategies and expectations of the Company. These forward-looking statements are generally identified by use of the words “believe,” “expect,” “intend,” “anticipate,” “estimate,” “project” or similar expressions. The Company’s ability to predict results or the actual effect of future plans or strategies is inherently uncertain. Factors which could have a material adverse effect on the operations of the Company and its subsidiaries include, but are not limited to:

- Credit quality and the effect of credit quality on the adequacy of our allowance for loan losses;
- Deterioration in financial markets that may result in impairment charges relating to our securities portfolio;
- Competition in our primary market areas;
- Changes in interest rates and national or regional economic conditions;
- Changes in monetary and fiscal policies of the U.S. Government, including policies of the U.S. Treasury and the Federal Reserve Board;
- Significant government regulations, legislation and potential changes thereto;
- A reduction in our ability to generate or originate revenue-producing assets as a result of compliance with heightened capital standards;
- Increased cost of operations due to greater regulatory oversight, supervision and examination of banks and bank holding companies, and higher deposit insurance premiums;
- Cyberattacks, computer viruses and other technological threats that may breach the security of our websites or other systems;
- Technological changes that may be more difficult or expensive than expected;
- Limitations on our ability to expand consumer product and service offerings due to anticipated stricter consumer protection laws and regulations; and
- Other risks described herein and in the other reports and statements we file with the SEC.

These risks and uncertainties should be considered in evaluating forward-looking statements and undue reliance should not be placed on such statements. Except as required by applicable law or regulation, the Company does not undertake, and specifically disclaims any obligation, to release publicly the result of any revisions that may be made to any forward-looking statements to reflect events or circumstances after the date of the statements or to reflect the occurrence of anticipated or unanticipated events.

Application of Critical Accounting Policies

The Company's consolidated annual financial statements are prepared in accordance with accounting principles generally accepted in the United States and follow practices within the banking industry. Application of these principles requires management to make estimates, assumptions, and judgments that affect the amounts reported in the consolidated annual 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 accounting 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 unaffiliated 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 annual audited 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 annual 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 allowance for loan losses, deferred income taxes, pension obligations, the evaluation of investment securities for other than temporary impairment, the estimation of fair values for accounting and disclosure purposes, and the evaluation of goodwill for impairment to be the accounting areas that require the most subjective and complex judgments. These areas 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 on 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.

Our Allowance for Loan and Lease Losses policy establishes criteria for selecting loans to be measured for impairment based on the following:

Residential and Consumer Loans:

- All loans rated substandard or worse, on nonaccrual, and above our total related credit (“TRC”) threshold balance of $300,000.
- All Troubled Debt Restructured Loans

Commercial Lines and Loans, Commercial Real Estate and Tax-exempt loans:

- All loans rated substandard or worse, on nonaccrual, and above our TRC threshold balance of $100,000.
- All Troubled Debt Restructured Loans

Impairment is measured by determining the present value of expected future cash flows or, for collateral-dependent loans, the fair value of the collateral adjusted for market conditions and selling expenses as compared to the loan carrying value. For all other loans and leases, the Company uses the general allocation methodology that establishes an allowance to estimate the probable incurred loss for each risk-rating category.

Deferred income tax assets and liabilities are determined using the liability method. Under this method, the net deferred tax asset or liability is recognized for the future tax consequences. This is attributable to the differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases as well as net operating and capital loss carry forwards. Deferred tax assets and liabilities are measured using enacted tax rates applied to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income tax expense in the period that includes the enactment date. If current available evidence about the future raises doubt about the likelihood of a deferred tax asset being realized, a valuation allowance is established. The judgment about the level of future taxable income, including that which is considered capital, is inherently subjective and is reviewed on a continual basis as regulatory and business factors change. In the quarter ended March 31, 2019, the Company established, through a charge to earnings, a valuation allowance in the amount of $136,000 in order to reserve against deferred tax assets related to New York State income taxes. Effective in January 2018, the Company adopted a modification methodology, made available following changes to the New York State tax code, effecting how the Company's state income tax liability is computed. Under this adopted methodology, it is unlikely that the Company will pay income taxes to New York in future periods and it is therefore probable that the Company's deferred tax assets related to New York State income taxes are unlikely to further reduce the Company's state income tax rate in the future. Accordingly, a valuation allowance against the value of those deferred tax assets was established to reduce the net deferred tax asset related to New York income taxes to $-0-. At September 30, 2019, the Company had a valuation allowance of $77,000 established against the future projected benefits of deferred tax assets related to New York State income tax obligations. There were no valuation allowances against deferred tax assets at December 31, 2018. The Company's effective tax rate typically differs from the 21% federal statutory tax rate due primarily to tax-exempt income from specific types of investment securities and loans, bank owned life insurance, and, to a much lesser degree, the utilization of low income housing tax credits. These factors, which typically lower the effective tax rate for the Company, were offset by the establishment of the valuation allowance described above resulting in an effective tax rate of 23.7% for the nine months ended September 30, 2019.

We maintain a noncontributory defined benefit pension plan covering most employees. The plan provides defined benefits based on years of service and final average salary. On May 14, 2012, we informed our employees of our decision to freeze participation and benefit accruals under the plan, primarily to reduce some of the volatility in earnings that can accompany the maintenance of a defined benefit plan. Pension and post-retirement benefit plan liabilities and expenses are based upon actuarial assumptions of future events; including fair value of plan assets, interest rates, and the length of time the Company will have to provide those benefits. The assumptions used by management are discussed in Note 14 to the consolidated annual financial statements.

The Company carries all of its available-for-sale investments at fair value with any unrealized gains or losses reported, net of tax, as an adjustment to shareholders' equity and included in accumulated other comprehensive income (loss), except for the credit-related portion of debt securities impairment losses and OTTI of equity securities which are charged to earnings. The Company's ability to fully realize the value of its investments in various securities, including corporate debt securities, is dependent on the underlying creditworthiness of the issuing organization. In evaluating the debt securities (both available-for-sale and held-to-maturity) portfolio for other-than-temporary impairment losses, management considers (1) if we intend to sell the security; (2) if it is "more likely than not" we will be required to sell the security before recovery of its amortized cost basis; or (3) if the present value of expected cash flows is not sufficient to recover the entire amortized cost basis. When the fair value of a held-to-maturity or available-for-sale security is less than its amortized cost basis, an assessment is made as to whether OTTI is present. The Company considers numerous factors when determining whether a potential OTTI exists and the period over which the debt security is expected to recover. The principal factors considered are (1) the length of time and the extent to which the fair value has been less than the amortized cost basis, (2) the financial condition of the issue and (guarantor, if any) and adverse conditions specifically related to the security, industry or geographic area, (3) failure of the issuer of the security to make scheduled interest or principal payments, (4) any changes to the rating of the security by a NRSRO, and (5) the presence of credit enhancements, if any, including the guarantee of the federal government or any of its agencies.

The estimation of fair value is significant to several of our assets; including loans, available-for-sale and marketable equity investment securities, intangible assets, foreclosed real estate, and the value of loan collateral when valuing impaired loans. These are all recorded at either fair value, or the lower of cost or fair value. Fair values are determined based on third party sources, when available. Furthermore, accounting principles generally accepted in the United States require disclosure of the fair value of financial instruments as a part of the notes to the annual audited consolidated financial statements. Fair values on our available-for-sale securities may be influenced by a number of factors; including market interest rates, prepayment speeds, discount rates, and the shape of yield curves.

Fair values for securities available-for-sale are obtained from unaffiliated third party pricing services. Where available, fair values are based on quoted prices on a nationally recognized securities exchange. If quoted prices are not available, fair values are measured using quoted market prices for similar benchmark securities. Management made no adjustments to the fair value quotes that were provided by the pricing sources. Fair values for marketable equity securities are based on quoted prices on a nationally recognized securities exchange for similar benchmark securities. The fair values of foreclosed real estate and the underlying collateral value of impaired loans are typically determined based on evaluations by third parties, less estimated costs to sell. When necessary, appraisals are updated to reflect changes in market conditions.

Management performs an annual evaluation of our goodwill for possible impairment at each of our reporting units. Based on the results of the December 31, 2018 evaluation, management has determined that the carrying value of goodwill was not impaired as of that date. The evaluation approach is described in Note 10 of the consolidated annual financial statements. Further information on the estimation of fair values can be found in Note 22 to the consolidated annual financial statements.

Recent Events

On September 23, 2019, the Company announced that its Board of Directors had declared a cash dividend of $0.06 per common and preferred share, payable to shareholders of record as of October 18, 2019 on November 8, 2019.

Overview and Results of Operations

The following represents the significant highlights of the Company's operating results between the third quarter of 2019 and the third quarter of 2018.

- Total net income increased $310,000, or 31.5%, to $1.3 million.
- Basic and diluted earnings per share both decreased $0.01 to $0.22.
- Return on average assets increased by seven basis points to 0.51% as the increase in the Company's net income slightly outpaced the increase in average assets.
- Net interest income, after provision for loan losses, increased $500,000, or 8.2%, to $6.6 million. Excluding the provision, net interest income increased $809,000, or 12.7%, to $7.2 million. This increase in net interest income was primarily due to the increase in average balances of interest earning assets, accompanied by an increase in the average yield earned on interest-earning assets.
- Net interest margin decreased by one basis point to 3.01%, primarily as a result of a $112.0 million increase in the average balance of time deposits, coupled with a 58 basis point increase in the average rate paid on time deposits. The increases in the average rates paid on time deposits reflected the competitive environment for such deposits within the Company's marketplace as well as a general increase in short-term interest rates nationally.
- The effective income tax rate increased 6.3% to 19.9% for the three months ended September 30, 2019 as compared to 13.6% for the same three month period in 2018. The increase was primarily related to the tax benefit recognized related to the cashless exercise of incentive stock options in the prior year quarter.

The following represents significant highlights of the Company's operating results between the first nine months of 2019 and the first nine months of 2018.

- Net income decreased $518,000, or 17.7%, to $2.4 million.
- Basic and diluted earnings per share were both $0.47 per share and decreased $0.24 per share and $0.22 per share, respectively.
- Return on average assets decreased 11 basis points to 0.33% between the year-over-year nine month periods as net income (the numerator of the ratio) decreased by $518,000, or 17.7%, resulting in a seven basis point decrease in the return on average assets between the year-over-year nine month periods. Further, average assets (the denominator of the ratio) grew $95.8 million, or 10.8%, resulting in a four basis point decrease in the return on average assets between the year-over-year nine month periods.
- Net interest income, after provision for loan losses, increased by $1.0 million, or 5.8%, to $19.1 million. This increase in earnings was primarily due to the increase in average balances of interest earning assets, accompanied by an increase in the average yield earned on interest-earning assets.
- Net interest margin decreased by nine basis points to 2.94%, primarily as a result of a $117.5 million increase in the average balance of time deposits, coupled with a 76 basis point increase in the average rate paid on time deposits. The increases in the average rates paid on time deposits reflected the competitive environment for such deposits within the Company's marketplace as well as a general increase in short-term interest rates nationally.
- The effective income tax rate increased 9.1% to 23.7% for the nine months ended September 30, 2019 as compared to 14.6% for the same nine month period in 2018. This increase was primarily related to the nonrecurring establishment, through a charge to earnings, of a $136,000 valuation allowance to reserve against deferred tax assets related to New York State income taxes. Excluding the nonrecurring charge, the increase in

income tax expense and the effective tax rate in the first nine months of 2019, as compared to the previous period, was primarily attributable to the recognition of tax benefits of $115,000 in the first nine months of 2018 that resulted from the cashless exercise of incentive stock options by certain executives of the Company.

The following reflects the significant changes in financial condition between the periods of December 31, 2018 and September 30, 2019. In addition, the following reflects significant changes in asset quality metrics between September 30, 2018 and September 30, 2019.

- Total assets increased $123.0 million, or 13.2% to $1.1 billion at September 30, 2019, as compared to December 31, 2018, primarily due to increases in loans, cash and cash equivalents, and investment securities. These increases were funded largely by increases in deposits, including brokered deposits, as well as the cash flow from the sale and maturity of investment securities.
- Asset quality metrics remained stable in comparison to recent reporting periods. The Company's consistent asset quality metrics are reflective of its disciplined risk management process, along with the relative economic stability of its Central New York State market area. The annualized net loan charge-offs to average loans ratio was 0.07% for the third quarter of 2019, compared to 0.12% for the third quarter of 2018, and 0.22% for the fourth quarter of 2018. Nonperforming loans to total loans decreased two basis points to 0.73% at September 30, 2019, compared to 0.75% at September 30, 2018. Nonperforming loans to total loans increased 38 basis points to 0.73% at September 30, 2019, compared to 0.35% at December 31, 2018. Correspondingly, the ratio of the allowance for loan losses to nonperforming loans at September 30, 2019 was 156.43%, as compared to 167.72% at September 30, 2018, and 340.13% at December 31, 2018.

The Company had net income of $1.3 million for the three months ended September 30, 2019 compared to net income of $985,000 for the three months ended September 30, 2018. The $310,000 increase in net income was due primarily to a $1.9 million increase in interest and dividend income and a $346,000 increase in noninterest income. The increase in net income was partially offset by a $1.1 million increase in interest expense, a $370,000 increase in noninterest expenses, and a $309,000 increase in the provisions for loans losses.

Net interest income before the provision for loan losses increased $809,000, or 12.7%, to $7.2 million for the three months ended September 30, 2019 as compared to $6.4 million for the same three month period in 2018. The increase was primarily the result of the increase in average interest-earning asset balances due to increases in average loans and average taxable investment securities. The positive effects of increased average interest-earning assets for the three months ended September 30, 2019, as compared to the same three month period in 2018, were also enhanced by an increase in the average yield of interest-earning assets of 31 basis points to 4.47% for the three months ended September 30, 2019 from 4.16% for the same three month period of the previous year. These positive factors on net interest income were partially offset by an increase in the average balance of interest-bearing liabilities of $91.5 million, or 12.6%, and an increase of 39 basis points on the average interest rate paid on those liabilities.

The $346,000, or 36.8%, increase in noninterest income in the quarter ended September 30, 2019, as compared to the same quarterly period in 2018, was primarily the result of a $181,000 net increase in the net gains on the sales and redemptions of investment securities, from a loss of $60,000 for the three months ended September 30, 2018 to a net gain of $121,000 for the same quarter in 2019. The investment securities sales were part of the Company's portfolio optimization and liquidity management strategies. It is the intention of management to reinvest the proceeds of these investment securities sales into potentially higher yielding interest-earning assets in future periods. Further contributing to the increase in noninterest income was a $108,000 increase on service charges on deposit accounts and a $32,000 increase in loan servicing fees. All other noninterest income categories increased by an aggregate $25,000, or 3.7% in the quarter ended September 30, 2019 as compared to the prior year quarter.

The $370,000, or 6.3%, increase in noninterest expense in the quarter ended September 30, 2019, as compared to the same quarterly period in 2018, was primarily a result of a $98,000 increase in building and occupancy costs, a $95,000 increase in data processing charges, an $84,000 increase in salaries and employee benefits expense, and an $80,000 increase in advertising expense. The increase in building and occupancy costs and data processing charges were partially due to expenses related to our new banking location in Onondaga County. These increases are consistent with branch and operational growth. The increase in salaries and employee benefits expense reflected an increase in staffing levels intended to meet increased loan demand and to better serve customers and potential customers as the Bank's operations continue to expand primarily into Onondaga County, New York. Advertising expense increased primarily as the result of increases in the level of brand awareness advertising expenditures primarily focused on the Onondaga County market. All other noninterest expense categories increased $13,000, or 1.1%, in aggregate during the quarter ended September 30, 2019, as compared to the same three month period in 2018.

In comparing the year-over-year third quarter periods, the return on average assets increased seven basis points to 0.51% due to the effects of the increase in net income (the numerator in the ratio), partially offset by the increase in average assets (the denominator in the ratio). Average assets increased due to increases in average loans and average taxable investment securities of $93.4 million and $40.2 million, respectively, in the third quarter of 2019 as compared to the same quarter of 2018. Average interest-bearing deposits increased $89.9 million in the third quarter of 2019, as compared with the same quarter in 2018. The increase in deposits was the result of organic growth within our existing marketplace coupled with targeted promotions for our time deposit products.

The Company had net income of $2.4 million for the nine months ended September 30, 2019 compared to net income of $2.9 million for the nine months ended September 30, 2018. The $518,000 decrease in net income was due primarily to a $3.8 million increase in interest expense, a $2.0 million increase in noninterest expense, a $245,000 increase in income tax expense, and a $153,000 increase in the provision for loan losses. The increase expenses were partially offset by an increase of $5.0 million in interest and dividend income and a $739,000 increase in noninterest income.

Net interest income before the provision for loan losses increased $1.2 million, or 6.2%, to $20.5 million for the nine months ended September 30, 2019 as compared to the same nine month period in the previous year. The increase was a result of the increase in average balances on loans and taxable investment securities and an increase in the average yield earned on those balances, partially offset by an increase in the average balance and average cost of interest-bearing liabilities between the year-over-year nine month periods.

The $739,000, or 25.8%, increase in noninterest income in the nine months ended September 30, 2019, as compared to the same nine month period in 2018, was primarily the result of a net increase of $421,000 in the net gains on the sales and redemptions of investment securities from a loss of $189,000 for the nine months ended September 30, 2018 to a net gain of $232,000 for the same nine month period in 2019. The investment securities sales were part of the Company's portfolio optimization and liquidity management strategies. It is the intention of management to reinvest the proceeds of these investment securities sales into potentially higher yielding interest-earning assets in future periods. Also contributing to the increase in noninterest income was service charges on deposit accounts, debit interchange fees, earnings and gain on bank owned life insurance, and loan servicing fees, which increased $191,000, $65,000, $36,000, and $36,000, respectively. All other noninterest income categories decreased by $10,000, or 0.7%, in the nine months ended September 30, 2019 as compared to the prior year period.

The $2.0 million, or 11.6%, increase in noninterest expense was due primarily to an increase of $998,000, or 10.6%, in salary and employee benefits expense that reflected, in part, approximately $170,000 in one-time employee severance payments and $217,000 in reduced accrued earnings from the Company's defined benefit pension plan (due primarily to market value declines in the Company's pension assets at December 31, 2018). The remainder of the year-over-year increase in salary and employee benefits expense of $611,000 was primarily due to increases in staffing levels intended to meet increased loan demand and to better serve customers and potential customers as the Bank's operations continue to expand into Onondaga County. In addition, data processing costs, building and occupancy costs, and foreclosed real estate expenses increased $345,000, $297,000, and $231,000, respectively. The increase in data processing and building and occupancy costs were partially due to expenses related to our new banking location in Onondaga County. Foreclosed real estate expenses increased due to expenses related to the final disposition of a single foreclosed commercial property. All other noninterest expense categories increased $163,000, or 3.3%, in aggregate for the nine month period ended September 30, 2019, as compared to the same nine month period in 2018.

Return on average assets decreased 11 basis points to 0.33% between the year-over-year nine month periods as net income (the numerator of the ratio) decreased by $518,000, or 17.7%, resulting in a seven basis point decrease in the return on average assets between the year-over-year nine month periods. Further, average assets (the denominator of the ratio) grew $95.8 million, or 10.8%, resulting in a four basis point decrease in the return on average assets between the year-over-year nine month periods.

For the three months ended September 30, 2019, we recorded $600,000 in provision for loan losses as compared to $291,000 in the same prior year three month period. This $309,000 increase in the provision for the three month period is reflective of continued significant growth in the Bank’s commercial and consumer lending portfolios, as well as changes to both quantitative and environmental factors deemed appropriate for the Bank’s loan portfolio. Average loan balances increased $93.4 million, or 15.2%, in the third quarter of 2019 as compared with the same quarter of 2018.

For the first nine months of 2019, we recorded $1.4 million in provision for loan losses as compared to $1.2 million in the same prior year nine month period. This $153,000 increase in the provision for loan losses was reflective of continued significant growth in the Bank’s commercial and consumer lending portfolios. Average loan balances increased $64.5 million, or 10.7%, from September 30, 2019 as compared with the same prior year period.

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 loans, interest-earning deposits, and investment securities, exceeds the interest paid on deposits and other interest-bearing liabilities. Changes in net interest income and net interest margin result from the interaction between the volume and composition of interest-earning assets, interest-bearing liabilities, related yields, and associated funding costs.

The following tables set forth information concerning average interest-earning assets and interest-bearing liabilities and the average yields and rates thereon for the periods indicated. Interest income and resultant yield information in the tables has not been adjusted for tax equivalency. Averages are computed on the daily average balance for each month in the period divided by the number of days in the period. Yields and amounts earned include loan fees. Nonaccrual loans have been included in interest-earning assets for purposes of these calculations.

	For the three months ended September 30,					
	2019			2018		
(Dollars in thousands)	Average Balance	Interest	Average Yield / Cost	Average Balance	Interest	Average Yield / Cost
Interest-earning assets:						
Loans	$ 707,250	$ 8,817	4.99%	$ 613,889	$ 7,213	4.70%
Taxable investment securities	235,095	1,833	3.12%	194,925	1,409	2.89%
Tax-exempt investment securities	1,710	11	2.57%	23,568	143	2.43%
Fed funds sold and interest-earning deposits	17,039	72	1.69%	16,921	65	1.54%
Total interest-earning assets	961,094	10,733	4.47%	849,303	8,830	4.16%
Noninterest-earning assets:						
Other assets	68,095			59,232		
Allowance for loan losses	(7,980)			(7,721)		
Net unrealized losses on available-for-sale securities	(9)			(4,273)		
Total assets	$ 1,021,200			$ 896,541		
Interest-bearing liabilities:						
NOW accounts	$ 66,189	$ 34	0.21%	$ 67,203	$ 30	0.18%
Money management accounts	13,538	5	0.15%	13,117	5	0.15%
MMDA accounts	197,309	521	1.06%	218,866	583	1.07%
Savings and club accounts	83,696	25	0.12%	83,620	21	0.10%
Time deposits	367,271	2,260	2.46%	255,267	1,200	1.88%
Subordinated loans	15,114	216	5.72%	15,079	216	5.73%
Borrowings	73,350	467	2.55%	71,807	379	2.11%
Total interest-bearing liabilities	816,467	3,528	1.73%	724,959	2,434	1.34%
Noninterest-bearing liabilities:						
Demand deposits	103,698			100,932		
Other liabilities	11,762			6,570		
Total liabilities	931,927			832,461		
Shareholders' equity	89,273			64,080		
Total liabilities & shareholders' equity	$ 1,021,200			$ 896,541		
Net interest income		$ 7,205			$ 6,396	
Net interest rate spread			2.74%			2.82%
Net interest margin			3.00%			3.01%
Ratio of average interest-earning assets to average interest-bearing liabilities			117.71%			117.15%

(Dollars in thousands)	2019 Average Balance	2019 Interest	2019 Average Yield / Cost	2018 Average Balance	2018 Interest	2018 Average Yield / Cost
	For the nine months ended September 30,					
Interest-earning assets:						
Loans	$ 669,457	$ 24,614	4.90%	$ 604,987	$ 20,949	4.62%
Taxable investment securities	229,455	5,438	3.16%	194,133	3,837	2.64%
Tax-exempt investment securities	9,793	170	2.31%	31,521	608	2.57%
Fed funds sold and interest-earning deposits	19,924	288	1.93%	15,345	161	1.40%
Total interest-earning assets	928,629	30,510	4.38%	845,986	25,555	4.03%
Noninterest-earning assets:						
Other assets	67,237			56,033		
Allowance for loan losses	(7,545)			(7,458)		
Net unrealized (losses) on available for sale securities	(1,640)			(3,666)		
Total assets	$ 986,681			$ 890,895		
Interest-bearing liabilities:						
NOW accounts	$ 67,984	$ 90	0.18%	$ 67,741	$ 83	0.16%
Money management accounts	13,725	15	0.15%	13,865	16	0.15%
MMDA accounts	186,434	1,350	0.97%	241,363	1,654	0.91%
Savings and club accounts	84,423	75	0.12%	83,806	64	0.10%
Time deposits	352,827	6,400	2.42%	235,347	2,933	1.66%
Subordinated loans	15,103	650	5.74%	15,071	629	5.56%
Borrowings	77,228	1,472	2.54%	68,608	920	1.79%
Total interest-bearing liabilities	797,724	10,052	1.68%	725,801	6,299	1.16%
Noninterest-bearing liabilities:						
Demand deposits	102,228			95,542		
Other liabilities	10,135			6,166		
Total liabilities	910,087			827,509		
Shareholders' equity	76,594			63,386		
Total liabilities & shareholders' equity	$ 986,681			$ 890,895		
Net interest income		$ 20,458			$ 19,256	
Net interest rate spread			2.70%			2.87%
Net interest margin			2.94%			3.03%
Ratio of average interest-earning assets to average interest-bearing liabilities			116.41%			116.56%

As indicated in the above tables, net interest income, before provision for loan losses, increased $809,000, or 12.7%, to $7.2 million for the three months ended September 30, 2019 as compared to $6.4 million for the same prior year period. This increase was due principally to the $111.8 million, or 13.2%, increase in the average balance of interest-earning assets, and an increase of 31 basis points on the average yield earned on those assets. These positive factors on net interest income were partially offset by an increase in the average balance of interest-bearing liabilities of $91.5 million, or 12.6%, and an increase of 39 basis points on the average interest rate paid on those liabilities. In total, net interest margin decreased one basis point to 3.00% due largely to the increase in rates paid on average interest-bearing liabilities, as noted above. The following analysis should also be viewed in conjunction with the table below which reports the changes in net interest income attributable to rate and volume.

Interest and dividend income increased $1.9 million, or 21.6%, to $10.7 million for the three months ended September 30, 2019 compared to $8.8 million for the same three month period in 2018. The increase in interest and dividend income was due principally to the increase in average interest-earning assets (primarily loans and taxable investment securities), which increased between the year-over-year third quarter periods by $133.5 million, or 16.5%. The increase in the average balance of loans reflected the Company's continued success in its expansion within the greater Syracuse, New York market. Further supporting the quarter-over-quarter increase in interest income, the average yield on the loans and taxable investment portfolio improved 29 basis points to 4.99% and 23 basis points to 3.12%, respectively. This increase in the average yield on loans was the result of new loan production being added to the loan portfolio at rates slightly higher than the average yields of the previously existing portfolio. The increase in the average yield on taxable investment securities was the result of an increase in book yields on adjustable-rate securities and the purchase of new securities, often with longer durations or more credit risk exposure, at rates higher than the average yields of securities within the previously-existing portfolio whose balances continue to be reduced by amortization and maturities.

Interest expense for the three months ended September 30, 2019 increased $1.1 million, or 45.0%, to $3.5 million when compared to the same prior year period. Deposit interest expense increased $1.0 million, or 54.7%, to $2.8 million due to an $89.9 million increase in the average balance of interest-bearing deposits accompanied by a 41 basis point increase in the average annualized rate paid on these deposits to 1.56% for the three months ended September 30, 2019, as compared with the same three month period in 2018. This increase in the average rate was primarily due to a 58 basis point increase in the average rate paid on time deposits, during the three months ended September 30, 2019 as compared to the same three month period in 2018. The increase in the average rate paid on time deposits reflected the competitive environment for such deposits within the Company's marketplace. Further contributing to the increase in interest expense was an $88,000 increase in borrowings expense, which increased due to a $1.5 million increase in the average balance of borrowings.

For the nine month period ended September 30, 2019, net interest income, before the provision for loan losses, increased $1.2 million, or 6.2%, to $20.5 million compared to $19.3 million for the nine months ended September 30, 2018. This increase was due principally to the $82.6 million, or 9.8%, increase in the average balance of interest-earning assets, and an increase of 35 basis points on the average yield earned on those assets. These positive factors on net interest income were partially offset by an increase in the average balance of interest-bearing liabilities of $71.9 million, or 9.9%, and an increase of 52 basis points on the average interest rate paid on those liabilities. Interest and dividend income increased $5.0 million, or 19.4%, to $30.5 million for the nine months ended September 30, 2019 from $25.6 million for the same nine month period in 2018. The increase in interest and dividend income was due principally to the increase in average balances of loan and taxable investment securities, which increased 10.7% and 18.2%, respectively, between the year-over-year nine month periods. The increase in the average balance of loans reflected the Company's continued success in its expansion within the greater Syracuse market. These increases were also positively affected by the increase in the average yield on loans and taxable investment securities of 28 basis points to 4.90% and 52 basis points to 3.16%, respectively. This increase in the average yield on loans was the result of new loan production being added to the loan portfolio at rates slightly higher than the average rates of the previously existing portfolio. The increase in the average yield on taxable investment securities was the result of an increase in book yields on adjustable-rate securities and the purchase of new securities, often with longer durations or more credit risk exposure, at rates higher than the average rates of securities within the previously-existing portfolio whose balances continue to be reduced by amortization, maturities and sales.

Interest expense for the nine months ended September 30, 2019 increased $3.8 million, or 59.6%, to $10.1 million as compared to $6.3 million for the nine months ended September 30, 2018. The increase in interest expense was due principally to the increase in average interest-bearing liabilities of $71.9 million, along with a 52 basis point increase in the average rate paid on these liabilities to 1.68%. Deposit expense increased $3.2 million, or 66.9%. The average balance of interest-bearing deposits, which included brokered deposits, increased $63.3 million between the year-over-year nine month periods. Deposit interest expense increased 51 basis points to 1.50% for the nine months ended September 30, 2019 as compared with the same nine month period in 2018. This increase was primarily due to a 76 basis point increase in the average rate paid on time deposits, during the nine months ended September 30, 2019 as compared to the same time period in 2018. The increase in rates paid on those deposits reflected the competitive environment for such deposits within the Company's marketplace. Further contributing to the increase in interest expense was a $552,000 increase in borrowings expense, which increased due to an $8.6 million increase in the average balance of borrowings.

Rate/Volume Analysis

Net interest income can also be analyzed in terms of the impact of changing interest rates on interest-earning assets and interest-bearing liabilities and changes in the volume or amount of these assets and liabilities. The following table represents the extent to which changes in interest rates and changes in the volume of interest-earning assets and interest-bearing liabilities have affected the Company's interest income and interest expense during the periods indicated. Information is provided in each category with respect to: (i) changes attributable to changes in volume (change in volume multiplied by prior rate); (ii) changes attributable to changes in rate (changes in rate multiplied by prior volume); and (iii) total increase or decrease. Changes attributable to both rate and volume have been allocated ratably.

	Three months ended September 30, 2019 vs. 2018 Increase/(Decrease) Due to			Nine months ended September 30, 2019 vs. 2018 Increase/(Decrease) Due to		
(In thousands)	**Volume**	**Rate**	**Total Increase (Decrease)**	**Volume**	**Rate**	**Total Increase (Decrease)**
Interest Income:						
Loans	$ 1,145	$ 459	$ 1,604	$ 2,320	$ 1,345	$ 3,665
Taxable investment securities	307	117	424	765	836	1,601
Tax-exempt investment securities	(189)	57	(132)	(382)	(56)	(438)
Interest-earning deposits	-	7	7	56	71	127
Total interest income	1,263	640	1,903	2,759	2,196	4,955
Interest Expense:						
NOW accounts	(3)	7	4	-	7	7
Money management accounts	1	(1)	-	-	(1)	(1)
MMDA accounts	(57)	(5)	(62)	(444)	140	(304)
Savings and club accounts	-	4	4	-	11	11
Time deposits	622	438	1,060	1,813	1,654	3,467
Subordinated loans	2	(2)	-	1	20	21
Borrowings	8	80	88	127	425	552
Total interest expense	573	521	1,094	1,497	2,256	3,753
Net change in net interest income	$ 690	$ 119	$ 809	$ 1,262	$ (60)	$ 1,202

Provision for Loan Losses

We establish a provision for loan losses, which is charged to operations, at a level management believes is appropriate to absorb probable incurred credit losses in the loan portfolio. In evaluating the level of the allowance for loan losses, management considers historical loss experience, the types of loans and the amount of loans in the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral, and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available or as future events change. The provision for loan losses represents management's estimate of the amount necessary to maintain the allowance for loan losses at an adequate level.

Management extensively reviews recent trends in historical losses, qualitative factors and specific reserve needs on loans individually evaluated for impairment in its determination of the adequacy of the allowance for loan losses. We recorded $600,000 in provision for loan losses for the three month period ended September 30, 2019, as compared to $291,000 for the three month period ended September 30, 2018. The $309,000 increase in the provision for the three month period is reflective of continued significant growth in the Bank's commercial and consumer lending portfolios, as well as changes to both quantitative and environmental factors deemed appropriate for the Bank's loan portfolio. Average loan balances increased $93.4 million, or 15.2%, in the third quarter of 2019 as compared with the same quarter of 2018.

For the first nine months of 2019, we recorded $1.4 million in provision for loan losses as compared to $1.2 million in the same prior year nine month period. The $153,000 increase in the provision for loan losses was reflective of continued significant growth in the Bank's commercial and consumer lending portfolio. Average loan balances increased $64.5 million, or 10.7%, in the first nine months of 2019 as compared with the same prior year period.

The Company measures delinquency based on the amount of past due loans as a percentage of total loans. The ratio of delinquent loans to total loans decreased to 1.36% at September 30, 2019 as compared to 1.81% at December 31, 2018. Delinquent loans (numerator) decreased $1.3 million while total loan balances (denominator) increased $105.4 million at September 30, 2019, as compared to December 31, 2018. The decrease in past due loans was primarily driven by a decrease of $5.3 million in loans delinquent 30-59 days. This was partially offset by an increase of $3.2 million in loans delinquent more than 90 days and a $716,000 increase in loans delinquent 60-89 days. The decrease in loans 30-59 days past due at September 30, 2019 as compared to December 31, 2018 was primarily due to eight commercial real estate loans totaling $4.2 million and six commercial lines of credit totaling $1.0 million, which were no longer 30-59 days delinquent at September 30, 2019. The increase in loans delinquent 90 days or more at September 30, 2019 as compared to December 31, 2018 was primarily due to the addition of seven commercial real estate loans totaling $2.5 million and six other commercial and industrial loans totaling $590,000. The increase in loans 60-89 days past due at September 30, 2019 as compared to December 31, 2018 was primarily due to the addition of four other commercial and industrial loans totaling $384,000 and a $270,000 increase in residential loans 60-89 days past due.

At September 30, 2019, there were $9.8 million in loans past due including $2.8 million in loans 30-59 days past due, $1.8 million in loans 60-89 days past due and $5.2 million in loans 90 or more days past due. At December 31, 2018, there were $11.2 million in loans past due, including $8.1 million in loans 30-59 days past due, $1.1 million in loans 60-89 days past due and $2.0 million in loans 90 or more days past due.

Noninterest Income

The Company's noninterest income is primarily comprised of fees on deposit account balances and transactions, loan servicing, commissions, including insurance agency commissions, and net gains on sales of 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,				Nine months ended September 30,			
(Dollars in thousands)	2019	2018	Change		2019	2018	Change	
Service charges on deposit accounts	$ 399	$ 291	$ 108	37.1%	$ 1,029	$ 838	$ 191	22.8%
Earnings and gain on bank owned life insurance	133	138	(5)	-3.6%	355	319	36	11.3%
Loan servicing fees	57	25	32	128.0%	144	108	36	33.3%
Debit card interchange fees	166	141	25	17.7%	497	432	65	15.0%
Insurance agency revenue	170	174	(4)	-2.3%	631	639	(8)	-1.3%
Other charges, commissions and fees	198	223	(25)	-11.2%	606	662	(56)	-8.5%
Noninterest income before gains (losses)	1,123	992	131	13.2%	3,262	2,998	264	8.8%
Net gains (losses) on sales and redemptions of investment securities	121	(60)	181	301.7%	232	(189)	421	222.8%
Gains on marketable equity securities	4	-	4	-	61	26	35	134.6%
Net gains on sales of loans and foreclosed real estate	38	8	30	375.0%	43	24	19	79.2%
Total noninterest income	$ 1,286	$ 940	$ 346	36.8%	$ 3,598	$ 2,859	$ 739	25.8%

The $346,000 or 36.8%, increase in noninterest income in the quarter ended September 30, 2019, as compared to the same quarterly period in 2018, was partially due to the net increase of $181,000 in the net gains on the sales and redemptions of investment securities from a loss of $60,000 for the three months ended September 30, 2018 to a net gain of $121,000 for the same quarter in 2019. The investment securities sales were part of the Company's portfolio optimization and liquidity management strategies. It is the intention of management to reinvest the proceeds of these investment securities sales into potentially higher yielding interest-earning assets in future periods.

Excluding the effects of the quarter over quarter increase in gains on the sale of investment securities, all other noninterest income categories increased in aggregate by $165,000, or 16.5% to $1.2 million in the quarter ended September 30, 2019 as compared with $1.0 million in the same quarter of 2018. This $165,000 quarter over quarter increase in noninterest income, excluding the effects of gains on the sales and redemptions of investment securities, was due primarily to increases of $108,000 in service charges on deposit accounts and $32,000 in loan servicing fees. All other noninterest income categories increased by $25,000, or 3.7% in the quarter ended September 30, 2019 as compared to the prior year quarter.

The $739,000, or 25.8%, increase in noninterest income in the nine months ended September 30, 2019, as compared to the same nine month period in 2018, was primarily the result of a net increase of $421,000 in the net gains on the sales and redemptions of investment securities from a loss of $189,000 for the nine months ended September 30, 2018 to a net gain of $232,000 for the same nine month period in 2019. The investment securities sales were part of the Company's portfolio optimization and liquidity management strategies. It is the intention of management to reinvest the proceeds of these investment securities sales into potentially higher yielding interest-earning assets in future periods.

Excluding the effects of the period over period increase in gains on the sale of investment securities, all other noninterest income categories increased in aggregate by $318,000, or 10.4%, to $3.4 million in the nine months ended September 30, 2019 as compared with $3.0 million in the same nine month period of 2018. This $318,000 period over period increase in noninterest income, excluding the effects of gains on the sales and redemptions of investment securities, was due primarily to increases in service charges on deposit accounts, debit interchange fees, earnings and gain on bank owned life insurance, and loan servicing fees, which increased $191,000, $65,000, $36,000, and $36,000, respectively. All other noninterest income categories decreased by $10,000, or 0.7%, in the nine months ended September 30, 2019 as compared to the prior year period.

Noninterest Expense

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

	Three months ended September 30,				Nine months ended September 30,			
(Dollars in thousands)	2019	2018	Change		2019	2018	Change	
Salaries and employee benefits	$ 3,275	$ 3,191	$ 84	2.6%	$ 10,379	$ 9,381	$ 998	10.6%
Building and occupancy	699	601	98	16.3%	1,986	1,689	297	17.6%
Data processing	587	492	95	19.3%	1,749	1,404	345	24.6%
Professional and other services	352	359	(7)	-1.9%	1,068	1,095	(27)	-2.5%
Advertising	238	158	80	50.6%	719	626	93	14.9%
FDIC assessments	130	152	(22)	-14.5%	371	407	(36)	-8.8%
Audits and exams	104	104	-	0.0%	304	314	(10)	-3.2%
Insurance agency expense	190	190	-	0.0%	618	679	(61)	-9.0%
Community service activities	110	142	(32)	-22.5%	392	370	22	5.9%
Foreclosed real estate expenses	28	19	9	47.4%	324	93	231	248.4%
Other expenses	569	504	65	12.9%	1,622	1,440	182	12.6%
Total noninterest expenses	$ 6,282	$ 5,912	$ 370	6.3%	$ 19,532	$ 17,498	$ 2,034	11.6%

The $370,000, or 6.3%, increase in noninterest expense between the year-over-year third quarter periods was principally due to increases in building and occupancy costs, data processing costs, salaries and employee benefits expense, and advertising expenses. The detail of the components of the overall increase in noninterest expense is as follows:

- The increase in building and occupancy costs was primarily due to $30,000 in additional depreciation expense related to recently completed building modernization and refurbishment projects, a $21,000 increase in property taxes, a $16,000 increase in utilities and communications, a $10,000 increase in building and land lease expense, and a $10,000 increase in building and machine maintenance. These increases are consistent with branch and operational growth.
- The $95,000 increase in data processing costs was primarily due to $67,000 in additional depreciation related to recently completed projects and a $32,000 increase in internet banking services. These increases are consistent with branch and operational growth.
- The $84,000 increase in salaries and employee benefits expense in the third quarter of 2019, as compared to the same three month period in 2018, was primarily due to increases of $142,000 in salary expense and increases of $117,000 in employee benefits expense, including employee payroll tax expenses. Offsetting these increases was an $186,000 decrease in commission expense. Commission expense decreased primarily due to additional

accruals in the second quarter of 2018 that related to the timing of commissions payments, primarily to the senior management team of the Agency under a revised compensation formula established at the end of 2017. Salaries expense increased primarily as the result of additional staff members supporting current and planned asset growth and risk management activities as well as increased customer service and other operating costs reflecting the ramp-up period for our two new banking locations in Oneida and Onondaga counties. The year-over-year increases in employee benefit expenses were consistent with the salary increases discussed above.
- Advertising expense increased $80,000 primarily as the result of increases in the level of brand awareness advertising expenditures primarily focused on the Onondaga County market.
- All other noninterest expense categories increased $13,000, or 1.1%, in aggregate during the quarter ended September 30, 2019, as compared to the same three month period in 2018.

The $2.0 million, or 11.6%, increase in noninterest expenses between the nine month period ended September 30, 2019 and the same nine month period in the prior year was principally due to an increase in salaries and employee benefits expense, data processing expense, building and occupancy costs, and foreclosed real estate expense. The detail of the components of the overall increase in noninterest expense is as follows:

- The $998,000 increase in salaries and employee benefits expense in the first nine months of 2019, as compared to the same nine month period in 2018, was primarily due to increases of $906,000 in salary expense and increases of $554,000 in employee benefits expense, including employee payroll tax expenses. Offsetting these increases was a $466,000 decrease in commission expenses. Commission expense decreased primarily due to additional accruals in the prior year in the second quarter of 2018 that related to the timing of commissions payments, primarily to the senior management team of the Agency under a revised compensation formula established at the end of 2017. Salaries expense increased primarily as the result of additional staff members supporting current and planned asset growth and risk management activities as well as increased customer service and other operating costs reflecting the ramp-up period for our two new banking locations in Oneida and Onondaga counties. The year-over-year increases in employee benefit expenses were consistent with the salary increases discussed above.
- The $345,000 increase in data processing costs was primarily due to $195,000 in additional depreciation related to recently completed projects, a $78,000 increase in processing fees paid by the Bank that were based on increased levels of customer activity primarily transacted through its electronic delivery channels, a $29,000 increase in maintenance costs, and a $27,000 increase in supplies. These increases are consistent with branch and operational growth.
- The increase in building and occupancy costs was primarily due to $70,000 in additional depreciation expense related to recently completed building modernization and refurbishment projects, a $58,000 increase in utilities and communications, a $42,000 increase in property taxes, a $36,000 increase in building and machine maintenance, and a $29,000 increase in building and land lease expense. These increases are consistent with branch and operational growth.
- Foreclosed real estate expenses increased $231,000 as a result of property taxes paid on a foreclosed property. This foreclosed property was sold in February 2019 and is no longer in foreclosed real estate at September 30, 2019.
- All other noninterest expense categories increased $163,000, or 3.3%, in aggregate for the nine month period ended September 30, 2019, as compared to the same nine month period in 2018.

At September 30, 2019, the Bank serviced 193 residential mortgage loans in the aggregate amount of $11.5 million that have been sold on a non-recourse basis to FNMA. FNMA is the only unrelated third-party that has acquired loans originated by the Bank. On an infrequent basis, loans previously sold to FNMA that subsequently default may be found to have underwriting defects that place the loans out of compliance with the representations and warranties made by the Bank. This can occur at any time while the loan is outstanding. In such cases, the Bank is required to repurchase the defaulted loans from FNMA. Repurchase losses sustained by the Bank include all costs incurred by FNMA as part of the foreclosure process, including items such as delinquent property taxes and legal fees. Management continues to monitor the underwriting standards applied to all residential mortgage loan originations and subsequent sales through its quality control processes and considers these occurrences and their related expenses to be isolated instances.

Income Tax Expense

Income tax expense increased $167,000 to $324,000, with an effective tax rate of 19.9%, for the quarter ended September 30, 2019, as compared to $157,000, with an effective tax rate of 13.6%, for the same three-month period in 2018. The increase in income tax expense in the current quarter, as compared to the same quarter in 2018, was primarily due to the $476,000 increase in pretax income. Further contributing to the increase in income tax expense in the current quarter, as compared to the same quarter in 2018, was the recognition of tax benefits of $41,000 in the third quarter of 2018 that resulted from the cashless exercise of incentive stock options by certain executives of the Company. There were no tax benefits derived from the exercise of these options in the third quarter of 2019.

Income tax expense increased $245,000 to $750,000, with an effective tax rate of 23.7% for the nine months ended September 30, 2019 as compared to $505,000, with an effective tax rate of 14.6% for the same nine month period in 2018. In the first quarter of 2019, the Company established, through a charge to earnings, a valuation allowance in the amount of $136,000, increasing the Company's effective tax rate by 4.3%, in order to establish a reserve against deferred tax assets related to New York State income taxes. Effective in January 2018, the Company adopted a modification methodology, made available following changes to the New York State tax code, effecting how the Company's state income tax liability is computed. Under this adopted methodology, it is unlikely that the Company will pay income taxes to New York in future periods and it is therefore probable that the Company's deferred tax assets related to New York State income taxes are unlikely to further reduce the Company's State tax rate in the future. Accordingly, a valuation allowance against the recorded value of those deferred tax assets was established in order to reduce the net deferred tax asset related to New York income taxes to $-0- at September 30, 2019. There were no valuation allowances against deferred tax assets at December 31, 2018.

The Company's effective tax rate differs from the statutory federal tax rate of 21% due primarily to tax-exempt income from specific types of investment securities and loans, bank owned life insurance, and, to a much lesser degree, the utilization of low income housing credits. In addition, the tax effects of certain incentive stock option activity may also reduce the Company's effective tax rate on a sporadic basis. During the nine months ended September 30, 2019 these effects reduced the Company's effective tax rate by 0.6%. Excluding the nonrecurring charge related to the deferred tax asset valuation allowance, income tax expense in the first nine months of 2019 would have been $109,000 more than the prior period, and the effective tax rate would have been 19.4%. Excluding the nonrecurring charge, the increase in income tax expense and the effective tax rate in the first nine months of 2019, as compared to the previous period, was primarily attributable to the recognition of tax benefits of $115,000 in the first nine months of 2018 that resulted from the cashless exercise of incentive stock options by certain executives of the Company.

Earnings per Share

Basic and diluted earnings per share were $0.22 per share for the third quarter of 2019, as compared to $0.23 per basic and diluted share for the same quarter of 2018.

Basic and diluted earnings per share were $0.47 for the nine month period ended September 30, 2019, as compared to $0.71 and $0.69, respectively, for the same prior year period. The decrease in earnings per share between these two periods was due to the decrease in net income between these two time periods. Further information on earnings per share can be found in Note 3 of this Form 10-Q.

Changes in Financial Condition

Assets

Total assets increased $123.0 million, or 13.2%, to $1.1 billion at September 30, 2019 as compared to $933.1 million at December 31, 2018. This increase was due primarily to increases in loans, cash and cash equivalents, and in investment securities.

Total loans receivable increased $104.6 million, or 17.1%, to $717.6 million at September 30, 2019 from $613.0 million at December 31, 2018. Commercial loans, consumer loans, and residential loans recorded increases between these two dates, with increases of $53.6 million, $45.5 million, and $6.4 million, respectively.

Investment securities increased $2.8 million, or 1.2%, to $234.9 million at September 30, 2019, as compared to $232.0 million at December 31, 2018 and is consistent with the Company's portfolio optimization and liquidity management strategies.

Cash and cash equivalents increased $13.5 million, or 51.1%, to $39.8 million at September 30, 2019, as compared to $26.3 million at December 31, 2018. The $13.5 million increase in cash and cash equivalents was primarily due to a strategic increase in short-term liquidity in anticipation of continued high levels of demand for loan fundings during the fourth quarter of 2019. The Bank considers its statutorily required cash reserve balances held at the Federal Reserve Bank to be restricted cash. Total restricted cash was -$0- and $4.0 million at September 30, 2019 and December 31, 2018, respectively.

Liabilities

Total liabilities increased $98.3 million, or 11.3%, to $966.9 million at September 30, 2019 compared to $868.7 million at December 31, 2018. Deposits increased $132.5 million, or 18.2%, to $859.6 million at September 30, 2019, compared to $727.1 million at December 31, 2018. This increase was the result of an increase in retail deposits of $40.6 million, primarily due to increases in time deposits. This increase was further enhanced by the seasonally-normal strong deposit inflows related to the Bank's municipal depositor relationships, which increased $34.4 million. The increase in these customer deposits during the nine months ended September 30, 2019 was partially offset by a decrease in business deposits of $8.5 million. Brokered deposits increased $66.1 million primarily as a result of additional brokered time deposits the Bank took on in March 2019 and September 2019. In March 2019, the Bank took on additional brokered time deposits through an unrelated financial institution in the amount of $24.0 million, of which $8.0 million matured. In September 2019, the Bank took on an additional $10.0 million of brokered time deposits from the same unrelated financial institution. The Bank utilizes the Certificates of Deposit Account Registry Service ("CDARS") provided by Promontory Interfinancial Network and other deposits acquired through unaffiliated financial institutions as forms of brokered deposits. At September 30, 2019, deposits obtained through the use of these services increased $39.1 million to $80.5 million as compared to $41.4 million at December 31, 2018. Borrowed funds balances from the FHLB-NY decreased $39.3 million, or 33.1%, to $79.3 million at September 30, 2019 from $118.5 million at December 31, 2018 as the borrowing needs of the Bank decreased due to the growth in deposits.

Shareholders' Equity

The Company's shareholders' equity, exclusive of the noncontrolling interest, increased $24.7 million, or 38.5%, to $89.0 million at September 30, 2019 from $64.2 million at December 31, 2018. This increase was principally due to the $20.1 million increase in additional paid in capital, a $3.3 million increase in comprehensive income, a $1.2 million increase in retained earnings, and a $135,000 increase in ESOP shares earned. Additional paid in capital increased as a result of the proceeds received from the Private Placement of common and preferred shares that took place in May 2019. Comprehensive income increased primarily as the result of the appreciation in the fair market value of our available-for-sale investment securities during the nine months ended September 30, 2019. The slight increase in retained earnings resulted from $2.4 million in net income recorded in the first nine months of 2019. Partially offsetting the increase in retained earnings was $805,000 in cash dividends declared on our common stock, $139,000 in cash dividends declared on our preferred stock, and $15,000 in cash dividends declared on our issued warrant. In addition, retained earnings was further reduced by a $239,000 one-time adjustment, at January 1, 2019, related to the cumulative effect of the capitalization of the operating lease right-of-use-assets based on the adoption of *ASU 2016-02 - Leases (Topic 842).*

Capital

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 banking operations. This strong capital position serves to support growth and expansion activities while at the same time exceeding regulatory standards. At September 30, 2019, the Bank 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 8%, Tier 1 common equity exceeding 6.5%, and a total risk-based capital ratio exceeding 10%.

In addition to establishing the minimum regulatory capital requirements, the regulations limit capital distributions and certain discretionary bonus payments to management if the institution does not hold a "capital conservation buffer" consisting of 2.5% of common equity Tier 1 capital to risk-weighted assets above the amount necessary to meet its minimum risk-based capital requirements. The buffer is separate from the capital ratios required under the Prompt Corrective Actions ("PCA") standards. In order to avoid these restrictions, the capital conservation buffer effectively increases the minimum levels of the following capital to risk-weighted assets ratios: (1) Core Capital, (2) Total Capital and (3) Common Equity. The capital conservation buffer requirement is now fully implemented at 2.5% of risk-weighted assets as of January 1, 2019. At September 30, 2019, the Bank exceeded all regulatory required minimum capital ratios, including the capital buffer requirements.

On May 24, 2018, The Economic Growth, Regulatory Relief and Consumer Protection Act of 2018 (the "EGRRCPA") was enacted, which repeals or modifies certain provisions of the Dodd-Frank Act and eases regulations on all but the largest banks. The EGRRCPA's provisions include, among other things: (i) exempting banks with less than $10 billion in assets from the ability-to-repay requirements for certain qualified residential mortgage loans held in portfolio; (ii) not requiring appraisals for certain transactions valued at less than $400,000 in rural areas; (iii) exempting banks that originate fewer than 500 open-end and 500 closed-end mortgages from HMDA's expanded data disclosures; (iv) clarifying that, subject to various conditions, reciprocal deposits of another depository institution obtained using a deposit broker through a deposit placement network for purposes of obtaining maximum deposit insurance would not be considered brokered deposits subject to the FDIC's brokered-deposit regulations; (v) raising eligibility for the 18-month exam cycle from $1 billion to banks with $3 billion in assets; and (vi) simplifying capital calculations by requiring regulators to establish for institutions under $10 billion in assets a community bank leverage ratio (tier 1 capital to average consolidated assets) at a percentage not less than 8% and not greater than 10% that such institutions may elect to replace the general applicable risk-based capital requirements for determining well-capitalized status. The federal banking agencies have set the community bank leverage ratio at 9.0%. The new rule is effective on January 1, 2020. In addition, the law required the Federal Reserve Board to raise the asset threshold under its Small Bank Holding Company Policy Statement from $1 billion to $3 billion for bank or savings and loan holding companies that are exempt from consolidated capital requirements, provided that such companies meet certain other conditions such as not engaging in significant nonbanking activities.

Pathfinder Bank's capital amounts and ratios as of the indicated dates are presented in the following tables:

	Actual		Minimum For Capital Adequacy Purposes		Minimum To Be "Well-Capitalized" Under Prompt Corrective Provisions		Minimum For Capital Adequacy with Buffer	
(Dollars in thousands)	Amount	Ratio	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of September 30, 2019:								
Total Core Capital (to Risk-Weighted Assets)	$ 87,031	12.10%	$ 57,559	8.00%	$ 71,948	10.00%	$ 75,546	10.50%
Tier 1 Capital (to Risk-Weighted Assets)	$ 78,701	10.94%	$ 43,169	6.00%	$ 57,559	8.00%	$ 61,156	8.50%
Tier 1 Common Equity (to Risk-Weighted Assets)	$ 78,701	10.94%	$ 32,377	4.50%	$ 46,766	6.50%	$ 50,364	7.00%
Tier 1 Capital (to Assets)	$ 78,701	7.78%	$ 40,484	4.00%	$ 50,605	5.00%	$ 50,605	5.00%
As of December 31, 2018:								
Total Core Capital (to Risk-Weighted Assets)	$ 83,177	13.69%	$ 48,593	8.00%	$ 60,741	10.00%	$ 63,778	10.50%
Tier 1 Capital (to Risk-Weighted Assets)	$ 75,871	12.49%	$ 36,445	6.00%	$ 48,593	8.00%	$ 51,630	8.50%
Tier 1 Common Equity (to Risk-Weighted Assets)	$ 75,871	12.49%	$ 27,334	4.50%	$ 39,482	6.50%	$ 42,519	7.00%
Tier 1 Capital (to Assets)	$ 75,871	8.31%	$ 36,522	4.00%	$ 45,652	5.00%	$ 45,652	5.00%

Non-GAAP Financial Measures

Regulation G, a rule adopted by the Securities and Exchange Commission (SEC), applies to certain SEC filings, including earnings releases, made by registered companies that contain “non-GAAP financial measures.” GAAP is generally accepted accounting principles in the United States of America. Under Regulation G, companies making public disclosures containing non-GAAP financial measures must also disclose, along with each non-GAAP financial measure, certain additional information, including a reconciliation of the non-GAAP financial measure to the closest comparable GAAP financial measure (if a comparable GAAP measure exists) and a statement of the Company’s reasons for utilizing the non-GAAP financial measure as part of its financial disclosures. The SEC has exempted from the definition of “non-GAAP financial measures” certain commonly used financial measures that are not based on GAAP. When these exempted measures are included in public disclosures, supplemental information is not required. Financial institutions like the Company and its subsidiary bank are subject to an array of bank regulatory capital measures that are financial in nature but are not based on GAAP. The Company follows industry practice in disclosing its financial condition under these various regulatory capital measures, including period-end regulatory capital ratios for its subsidiary bank, in its periodic reports filed with the SEC. The Company provides, below, an explanation of the calculations, as supplemental information, for non-GAAP measures included in the consolidated annual financial statements. In addition, the Company provides a reconciliation of its subsidiary bank’s disclosed regulatory capital measures, below.

(Dollars in thousands)		September 30, 2019			December 31, 2018	
Regulatory Capital Ratios (Bank Only)						
Total capital (to risk-weighted assets)						
Total equity (GAAP)	$	86,156		$	86,614	
Goodwill		(4,536)			(4,536)	
Intangible assets		(153)			(165)	
Addback: Accumulated other comprehensive income		(2,766)			(6,042)	
Total Tier 1 Capital	$	78,701		$	75,871	
Allowance for loan and lease losses		8,330			7,306	
Total Tier 2 Capital	$	8,330		$	7,306	
Total Tier 1 plus Tier 2 Capital (numerator)	$	87,031		$	83,177	
Risk-weighted assets (denominator)		719,483			607,414	
Total core capital to risk-weighted assets		12.10	%		13.69	%
Tier 1 capital (to risk-weighted assets)						
Total Tier 1 capital (numerator)	$	78,701		$	75,871	
Risk-weighted assets (denominator)		719,483			607,414	
Total capital to risk-weighted assets		10.94	%		12.49	%
Tier 1 capital (to adjusted assets)						
Total Tier 1 capital (numerator)	$	78,701		$	75,871	
Total average assets		1,016,794			917,740	
Goodwill		(4,536)			(4,536)	
Intangible assets		(153)			(165)	
Adjusted assets (denominator)	$	1,012,105		$	913,039	
Total capital to adjusted assets		7.78	%		8.31	%
Tier 1 Common Equity (to risk-weighted assets)						
Total Tier 1 capital (numerator)	$	78,701		$	75,871	
Risk-weighted assets (denominator)		719,483			607,414	
Total Tier 1 Common Equity to risk-weighted assets		10.94	%		12.49	%

Loan and Asset Quality and Allowance for Loan Losses

The following table represents information concerning the aggregate amount of non-performing assets at the indicated dates:

(Dollars In thousands)	September 30, 2019	December 31, 2018	September 30, 2018
Nonaccrual loans:			
Commercial and commercial real estate loans	$ 4,206	$ 830	$ 2,565
Consumer	342	142	255
Residential mortgage loans	777	1,176	1,858
Total nonaccrual loans	5,325	2,148	4,678
Total nonperforming loans	5,325	2,148	4,678
Foreclosed real estate	148	1,173	268
Total nonperforming assets	$ 5,473	$ 3,321	$ 4,946
Accruing troubled debt restructurings	$ 2,540	$ 2,574	$ 2,711
Nonperforming loans to total loans	0.73%	0.35%	0.75%
Nonperforming assets to total assets	0.52%	0.36%	0.54%

Nonperforming assets include nonaccrual loans, nonaccrual troubled debt restructurings ("TDR"), and foreclosed real estate ("FRE"). The Company generally places a loan on nonaccrual status and ceases accruing interest when loan payment performance is deemed unsatisfactory and the loan is past due 90 days or more. There are no loans that are past due 90 days or more and still accruing interest. Loans are considered modified in a TDR when, due to a borrower's financial difficulties, the Company makes a concession(s) to the borrower that it would not otherwise consider. These modifications may include, among others, an extension of the term of the loan, and granting a period when interest-only payments can be made, with the principal payments made over the remaining term of the loan or at maturity. TDRs are included in the above table within the categories of nonaccrual loans or accruing TDRs. There was one nonaccruing TDR loan, with an aggregate carrying value of $74,000 included among the nonaccrual loans detailed in the table above at September 30, 2019.

As indicated in the table above, nonperforming assets at September 30, 2019 were $5.5 million and were $2.2 million higher than the $3.3 million reported at December 31, 2018, due primarily to an increase of $3.4 million in nonperforming commercial and commercial real estate loans and a $200,000 increase in nonperforming consumer loans, partially offset by decreases of $1.0 million in FRE and $399,000 in nonperforming residential real estate loans.

As indicated in the nonperforming asset table above, FRE balances decreased $1.0 million to $148,000 at September 30, 2019 from $1.2 million at December 31, 2018, following six sales from the portfolio and three additions to the portfolio during the nine month period ended September 30, 2019. More information regarding foreclosed real estate can be found in Note 8 of this Form 10-Q.

Fair values for commercial FRE are initially recorded based on market value evaluations by third parties, less costs to sell ("initial cost basis"). On a prospective basis, residential FRE assets will be initially recorded at the lower of the net amount of loan receivable or the real estate's fair value less costs to sell. Any write-downs required when the related loan receivable is exchanged for the underlying real estate collateral at the time of transfer to FRE are charged to the allowance for loan losses. Values are derived from appraisals, similar to impaired loans, of underlying collateral or discounted cash flow analysis. Subsequent to foreclosure, valuations are updated periodically and assets are marked to current fair value, not to exceed the initial cost basis for the FRE property.

The allowance for loan losses represents management's estimate of the probable losses inherent in the loan portfolio as of the date of the statement of condition. The allowance for loan losses was $8.3 million and $7.3 million at September 30, 2019 and December 31, 2018, respectively. The ratio of the allowance for loan losses to total loans decreased three basis points to 1.15% at September 30, 2019 from 1.18% at December 31, 2018. Management performs a quarterly evaluation of the allowance for loan losses based on quantitative and qualitative factors and has determined that the current level of the allowance for loan losses is adequate to absorb the losses in the loan portfolio as of September 30, 2019.

The Company considers a loan impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal and interest when due according to the contractual terms of the loan. The measurement of impaired loans is generally based upon the fair value of the collateral, with a portion of the impaired loans measured based upon the present value of future cash flows discounted at the historical effective interest rate. A specific reserve is established for an impaired loan if its carrying value exceeds its estimated fair value. The estimated fair values of the majority of the Company's impaired loans are measured based on the estimated fair value of the loan's collateral. For loans secured by real estate, estimated fair values are determined primarily through third-party appraisals or broker price opinions. When a loan is determined to be impaired, the Bank will reevaluate the collateral which secures the loan. For real estate, the Company will obtain a new appraisal or broker's opinion whichever is considered to provide the most accurate value in the event of sale. An evaluation of equipment held as collateral will be obtained from a firm able to provide such an evaluation. Collateral will be inspected not less than annually for all impaired loans and will be reevaluated not less than every two years. Appraised values and broker opinion values are discounted due to the market's perception of a reduced price of Bank-owned property and the Bank's desire to sell the property more quickly to arrive at the estimated selling price of the collateral, which is considered to be the estimated fair value. The discounts also include estimated costs to sell the property.

At September 30, 2019 and December 31, 2018, the Company had $8.1 million and $6.0 million in loans, respectively, which were deemed to be impaired, having established specific reserves of $779,000 and $631,000, respectively, on these loans. The increase in impaired loans between these two dates was primarily driven by increases of $1.8 million, $291,000, and $93,000, in impaired commercial real estate, other commercial and industrial loans, and other consumer loans. The $148,000 increase in specific reserves for impaired loans at September 30, 2019, as compared to December 31, 2018 was primarily due to an $84,000 increase in specific reserves for other commercial and industrial loans and an $82,000 increase in specific reserve for commercial lines of credit.

Management has identified potential credit problems which may result in the borrowers not being able to comply with the current loan repayment terms and which may result in those loans being included in future impaired loan reporting. Potential problem loans totaled $14.3 million as of September 30, 2019, a decrease of $297,000, or 2.0%, as compared to $14.6 million at December 31, 2018. These loans have been internally classified as special mention, substandard, or doubtful, yet are not currently considered impaired.

Appraisals are obtained at the time a real estate secured loan is originated. For commercial real estate held as collateral, the property is inspected every two years.

In the normal course of business, the Bank has infrequently sold residential mortgage loans and participation interests in commercial loans. As is typical in the industry, the Bank makes certain representations and warranties to the buyer. The Bank maintains a quality control program for closed loans and considers the risks and uncertainties associated with potential repurchase requirements to be minimal.

Liquidity

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

The Company's liquidity has been enhanced by its ability to borrow from the Federal Home Loan Bank of New York (“FHLBNY”), 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, 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 and/or losses on the sale of securities or loans.

Through the first nine months of 2019, as indicated in the consolidated statement of cash flows, the Company reported net cash flows from operating activities of $6.6 million and net cash outflows of $105.8 million related to investing activities. The net cash outflows from investing activities primarily was due to a net $106.7 million increase in loan balances, partially offset by a $845,000 decrease in all other investing activities in aggregate. The Company reported net cash flows from financing activities of $112.7 million generated principally by increased deposit balances of $66.5 million, increased brokered deposits balances of $66.0 million, and by net proceeds from the Private Placement offering totaling $19.6 million. This was partially offset by an aggregate decrease in net cash of $39.4 million from all other financing sources, including dividends paid to common and preferred shareholders of $885,000.

The Company has a number of existing credit facilities available to it. At September 30, 2019, total credit available to the Company under the existing lines of credit was approximately $173.9 million at FHLBNY, the Federal Reserve Bank, and two other correspondent banks. As of September 30, 2019, the Company had $79.3 million of the available lines of credit utilized, including encumbrances supporting outstanding letters of credit, described above, on its existing lines of credit with $94.6 million available.

The Asset Liability Management Committee of the Company is responsible for implementing the policies and guidelines for the maintenance of prudent levels of liquidity. As of September 30, 2019, management reported to the Board of Directors that the Company is in compliance with its liquidity policy guidelines.

Off-Balance Sheet Arrangements

The Company is also 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 standby letters of credit. At September 30, 2019, the Company had $132.0 million in outstanding commitments to extend credit and standby letters of credit.

Item 3 – Quantitative and Qualitative Disclosures About Market Risk

A smaller reporting company is not required to provide the information relating to this item.

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

At September 30, 2019, the Company is not currently a named party in a legal proceeding, the outcome of which would have a material and adverse effect on the financial condition or results of operations of the Company.

Item 1A – Risk Factors

A smaller reporting company is not required to provide the information relating to this item.

Item 2 – Unregistered Sales of Equity Securities and Use of Proceeds

Period	Total Number of Shares Purchased (1)	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares That May Yet Be Purchased Under the Plans or Programs
July 1, 2019 through July 31, 2019	-	$ -	-	74,292
August 1, 2019 through August 31, 2019	-	$ -	-	74,292
September 1, 2019 through September 30, 2019	-	$ -	-	74,292

(1) On August 29, 2016, our Board of Directors authorized the repurchase of up to 217,692 shares of our common stock, or 5% of the Company’s shares outstanding as of that date.

Item 3 – Defaults Upon Senior Securities

None

Item 4 – Mine Safety Disclosures

Not applicable

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	Section 1350 Certification of the Chief Executive Officer and Chief Financial Officer
101	Interactive data files pursuant to Rule 405 of Regulation S-T formatted in Extensible Business Reporting Language (XBRL): (i) the Consolidated Statements of Condition, (ii) the Consolidated Statements of Income (iii) the Consolidated Statements of Comprehensive Income, (iv) the Consolidated Statements of Changes in Shareholders’ Equity, (v) Consolidated Statements of Cash Flows, and (vi) the Notes to the Consolidated Financial Statements tagged as blocks of text.

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 12, 2019	/s/ Thomas W. Schneider Thomas W. Schneider President and Chief Executive Officer
November 12, 2019	/s/ Walter F. Rusnak Walter F. Rusnak 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 this 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)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) 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) Designed such internal control over financial reporting, or caused such internal control over financial reporting, to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

    (c) 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

    (d) 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 12, 2019

/s/ Thomas W. Schneider
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, Walter F. Rusnak, certify that:

1. I have reviewed this 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)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) 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. Designed such internal control over financial reporting, or caused such internal control over financial reporting, to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
    c. 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
    d. 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 12, 2019

/s/ Walter F. Rusnak
Walter F. Rusnak
Senior Vice President, Chief Financial Officer

EXHIBIT 32 Section 1350 Certification of the Chief Executive Officer and Chief Financial Officer

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

In connection with the Quarterly Report of Pathfinder Bancorp, Inc. (the “Company”) on Form 10-Q for the period ended September 30, 2019 as filed with the Securities and Exchange Commission (the “Report”), the undersigned hereby certify, pursuant to 18 U.S.C. §1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Sections 13(a) or 15(d) 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 as of and for the period covered by the Report.

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 12, 2019	/s/ Thomas W. Schneider Thomas W. Schneider President and Chief Executive Officer
November 12, 2019	/s/ Walter F. Rusnak Walter F. Rusnak Senior Vice President, Chief Financial Officer