FALMOUTH BANCORP INC
Form 10QSB
February 13, 2002

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-QSB

(Mark One)

[X] QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended December 31, 2001

OR

[ ] TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _________ to _________

Commission file number 01-13465

Falmouth Bancorp, Inc.
(Exact name of small business issuer as specified in its charter)

Delaware	04-3337685
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

20 Davis Straits, Falmouth, MA 02540
(Address of principal executive offices)
(508) 548-3500
(Issuer's telephone number including area code)
NA
(Former name, former address and former fiscal year, if changed since last Report)

Check whether issuer (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirement for the past 90 days.

Yes X No

State the number of shares outstanding of each of the issuer's classes of common equity as of the latest practicable date.

Class	Outstanding at December 31, 2001
Common Stock, Par Value $.01	915,607

Transitional small business disclosure format (check one):
Yes No X

FALMOUTH BANCORP, INC.
AND SUBSIDIARIES
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FORWARD LOOKING STATEMENTS

This report contains certain forward looking statements consisting of estimates with respect to the financial condition, results of operations and business of the Company and the Bank that are subject to various factors which could cause actual results to differ materially from these estimates. These factors include, but are not limited to: general and local economic conditions; changes in interest rates, deposit flows, demand for mortgages and other loans, real estate values, and competition; changes in accounting principles, policies, or guidelines; changes in legislation or regulation; and other economic, competitive, governmental, regulatory, and technological factors affecting our operations, pricing, products and services.

Any or all of our forward-looking statements in the report and in any other public statements we make may turn out to be wrong. They can be affected by inaccurate assumptions we might make or by known or unknown risks and uncertainties. Consequently, no forward-looking statement can be guaranteed.

We undertake no obligation to publicly update forward-looking statements, whether as a result of new information, future events or otherwise.

Part I. Item I. FALMOUTH BANCORP, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

December 31, 2001 and September 30, 2001

	December 31, 2001 (Unaudited)	September 30, 2001
ASSETS		
Cash, due from banks and interest bearing deposits	$ 1,879,971	$ 3,521,609
Federal funds sold	1,294,906	7,313,670
Total cash and cash equivalents	3,174,877	10,835,279
Investments in available-for-sale securities (at fair value)	12,103,749	9,381,853
Investments in held-to-maturity securities (fair values of $16,565,725 as of December 31, 2001 and $10,036,408 as of September 30, 2001)	16,507,733	9,948,877
Federal Home Loan Bank stock, at cost	878,000	878,000
Loans, net	110,532,664	112,554,093
Premises and equipment	1,852,886	1,897,697
Accrued interest receivable	797,338	830,421
Cooperative Central Bank Reserve Fund Deposit	395,395	395,395
Other assets	730,114	717,147
Total assets	$146,972,756	$147,438,762

LIABILITIES AND STOCKHOLDERS' EQUITY

Deposits:

Noninterest-bearing	$ 14,640,076	$ 16,147,253
Interest-bearing	107,414,013	106,028,583
Total deposits	122,054,089	122,175,836
Securities sold under agreements to repurchase	654,723	675,756
Federal Home Loan Bank advances	6,745,884	7,267,948
Other liabilities	450,682	354,534
Total liabilities	129,905,378	130,474,074
Minority preferred stockholders' equity in a subsidiary company of Falmouth Bank	54,000	54,000
Stockholders' equity:		
Preferred stock, par value $.01 per share, authorized 500,000 shares; none issued		
Common stock, par value $.01 per share, authorized 2,500,000 shares; issued 1,454,750 shares	14,547	14,547
Paid-in capital	13,944,608	13,901,279
Retained earnings	13,031,385	12,676,198
Unallocated Employee Stock Ownership Plan shares	(367,437)	(389,483)
Treasury stock (539,143 shares as of December 31, 2001; 516,743 shares as of September 30, 2001)	(9,235,225)	(8,749,737)
Unearned compensation	(137,429)	(137,429)
Accumulated other comprehensive loss	(237,071)	(404,687)
Total stockholders' equity	17,013,378	16,910,688
Total liabilities and stockholders' equity	$146,972,756	$147,438,762

The accompanying notes are integral part of these condensed consolidated financial statements.

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FALMOUTH BANCORP, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

Three Months Ended December 31, 2001 and 2000

(Unaudited)

	2001	2000
Interest and dividend income:		
Interest and fees on loans	$2,021,484	$2,059,439
Interest and dividends on securities:		
Taxable	190,356	245,674
Dividends on marketable equity securities	24,733	30,745
Dividends on Cooperative Bank Investment		

and Liquidity Funds	551	7,745
Other interest	40,701	52,558
Total interest and dividend income	2,277,825	2,396,161
Interest expense:		
Interest on deposits	898,985	1,061,582
Interest on securities sold under agreement to repurchase	2,114	13,172
Interest on Federal Home Loan Bank advances	84,515	51,384
Total interest expense	985,614	1,126,138
Net interest and dividend income	1,292,211	1,270,023
Provision for loan losses	50,000	85,000
Net interest and dividend income after provision for loan losses	1,242,211	1,185,023
Other income:		
Service charges on deposit accounts	48,956	37,895
Securities gains, net	17,062	75,724
Gains on mortgages sold, net	186,417	17,862
Other income	88,478	76,043
Total other income	340,913	207,524
Other expense:		
Salaries and employee benefits	430,099	437,262
Occupancy expense	41,540	47,042
Equipment expense	49,040	44,132
Data processing expense	94,764	71,505
Directors' fees	13,000	14,900
Legal and professional fees	47,447	70,602
Other expenses	174,366	175,356
Total other expenses	850,256	860,799
Income before income taxes	732,868	531,748
Income taxes	266,200	188,563
Net income	$ 466,668	$ 343,185
Comprehensive income	$ 167,616	$ 209,735
Earnings per common share	$ 0.52	$ 0.35
Earnings per common share, assuming dilution	$ 0.50	$ 0.35

The accompanying notes are integral part of these condensed consolidated financial statements.

FALMOUTH BANCORP, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

Three Months Ended December 31, 2001

(Unaudited)

	Common Stock	Paid-In Capital	Retained Earnings	Unallocated Employee Stock Ownership Plan Shares	Treasury Stock	Unea Compen
Balance, September 30, 2001	$14,547	$13,901,279	$12,676,198	$(389,483)	$(8,749,737)	$(13
Employee Stock Ownership Plan		22,546				
ESOP shares released				22,046		
Recognition and retention plan		27,060				
Purchase of treasury stock					(546,760)	
Exercise of stock options and related tax benefit		(6,277)			61,272	
Dividends declared ($.12 per share)			(111,481)			
Comprehensive income:						
Net income			466,668			
Net change in unrealized holding gain on available-for-sale securities						
Comprehensive income						
Balance, December 31, 2001	$14,547	$13,944,608	$13,031,385	$(367,437)	$(9,235,225)	$(13

Three Months Ended December 31, 2000

(Unaudited)

	Common Stock	Paid-In Capital	Retained Earnings	Unallocated Employee Stock Ownership Plan Shares	Treasury Stock	Unea Compen
Balance, September 30, 2000	$14,547	$13,901,452	$11,669,877	$(477,668)	$(6,850,722)	$(29
Employee Stock Ownership Plan		8,236				
ESOP shares released				22,046		
Recognition and retention plan		27,357				
Purchase of treasury stock					(180,532)	
Exercise of stock options and						

related tax benefit		(1,756)			9,781	
Dividends declared ($.09 per share)			(92,424)			
Comprehensive income:						
Net income			343,185			
Net change in unrealized holding gain on available-for-sale securities						
Comprehensive income						
Balance, December 31, 2000	$14,547	$13,935,289	$11,920,638	$(455,622)	$(7,021,473)	$(29

The accompanying notes are integral part of these condensed consolidated financial statements.

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FALMOUTH BANCORP, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

For the Three Months Ended December 31, 2001 and 2000

	2001 (Unaudited)	2000 (Unaudited)
Cash flows from operating activities		
Net income	$ 466,668	$ 343,185
Adjustments to reconcile net income to net cash provided by operating activities:		
Gains on sales of investment securities, net	(17,062)	(75,724)
(Amortization) accretion of investment securities, net	107,117	(4,861)
Provision for loan loss	50,000	85,000
Change in unearned income	(4,652)	(10,496)
Net gains on sales of loans	(186,417)	(17,862)
Depreciation and amortization	56,682	43,984
Loss on disposal of equipment	1,071	-
Amortization of mortgage servicing rights	3,890	-
Increase in mortgage servicing rights	(174,493)	-
(Increase) decrease in accrued interest receivable	33,083	(1,669)
(Increase) decrease in prepaid expenses	9,696	(16,269)
(Increase) decrease in other assets	(964)	1,364
Recognition and retention plan (RRP)	27,060	27,357
Decrease in accrued expenses	(6,381)	(91,508)
Increase in taxes payable	255,196	129,643
Increase in accrued interest payable	390	-
Decrease in other liabilities	(90,409)	(16,884)
Net cash provided by operating activities	530,475	395,260

Cash flows from investing activities		
Purchases of available-for-sale securities	(3,086,751)	(1,106,107)
Proceeds from sales of available-for-sale securities	60,868	155,623
Proceeds from maturities of available-for-sale securities	503,805	525,597
Purchases of held-to-maturity securities	(8,101,183)	(983,176)
Proceeds from maturities of held-to-maturity securities	1,506,326	3,400,247
Net increase in loans	(6,229,612)	(3,942,300)
Proceeds from sales of loans	8,392,110	2,445,422
Capital expenditures	(12,942)	(27,451)
Net cash (used in) provided by investing activities	(6,967,379)	467,855
Cash flows from financing activities:		
Net increase (decrease) in demand deposits, NOW and savings accounts	1,775,972	(4,514,089)
Net increase (decrease) in time deposits	(1,897,719)	1,621,157
Net decrease in securities sold under agreements to repurchase	(21,033)	(332,669)
Proceeds from Federal Home Loan Bank long-term advances	-	2,000,000
Repayments of Federal Home Loan Bank long-term advances	(522,064)	(20,659)
Net change in Federal Home Loan Bank short-term advances	-	943,000
Proceeds from exercise of stock options	54,995	8,025
Dividends paid	(111,481)	(92,424)
Employee Stock Ownership Plan	22,546	8,236
Unallocated ESOP shares released	22,046	22,046
Purchase of treasury stock	(546,760)	(180,532)
Net cash used in financing activities	(1,223,498)	(537,909)
Increase (decrease) in cash and cash equivalents	(7,660,402)	325,206
Cash and cash equivalents at beginning of period	10,835,279	6,830,473
Cash and cash equivalents at end or period	$ 3,174,877	$ 7,155,679
Supplemental disclosures		
Interest paid	$ 985,614	$ 1,126,138
Income taxes paid	4,508	57,920

The accompanying notes are integral part of these condensed consolidated financial statements.

FALMOUTH BANCORP, INC.

AND SUBSIDIARIES

Notes to Unaudited Condensed Consolidated Financial Statements

Note 1 - Basis of Presentation

The condensed consolidated financial statements of Falmouth Bancorp, Inc. (the "Company") and its subsidiaries presented herein are unaudited and should be read in conjunction with the consolidated financial statements of the Company for the year ended September 30, 2001. The results of operations for the three-month period ended December 31, 2001 are not necessarily indicative of the results to be expected for the full year. All material intercompany balances and transactions have been eliminated in consolidation. In the opinion of management, the condensed consolidated financial statements reflect all adjustments (consisting solely of normal recurring adjustments) necessary for a fair presentation of results for the interim periods. The year-end condensed balance sheet was derived from audited financial statements, but does not include all disclosures required by accounting principles generally accepted in the USA (GAAP).

Note 2 - Accounting Policies

The accounting and reporting policies of the Company conform to GAAP and prevailing practices within the banking industry. The interim financial information should be read in conjunction with the Company's 2001 Annual Report contained on Form 10-KSB.

Management is required to make estimates and assumptions that affect amounts reported in the consolidated financial statements. Actual results could differ significantly from those estimates.

Note 3 - Impact of New Accounting Standards

In June 1998, the FASB issued SFAS No. 133 "Accounting for Derivative Instruments and Hedging Activities". Statement No. 133, as amended by SFAS No. 138, establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts and for hedging activities. The Statement is effective for all fiscal quarters of fiscal years beginning after June 15, 2000. The adoption of SFAS No. 133, did not have a material effect on the Company's consolidated financial statements.

FASB has issued SFAS No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities. This replaces SFAS No, 125, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities, and rescinds SFAS Statement No. 127, "Deferral of the Effective Date of Certain Provisions of FASB Statement No. 125." SFAS No. 140 provides accounting and reporting standards for transfers and servicing of financial assets and extinguishments of liabilities. This statement provides consistent standards for distinguishing transfers of financial assets that are sales from transfers that are secured borrowings. This statement is effective for transfers and servicing of

financial assets and extinguishments of liabilities occurring after March 31, 2001; however, the disclosure provisions are effective for fiscal years ending after December 15, 2000. The effect of this statement did not have a material impact on the Company's financial position or result of operations.

Statement of Financial Accounting Standards No. 141 improves the consistency of the accounting and reporting for business combinations by requiring that all business combinations be accounted for under a single method - the purchase method. Use of the pooling-of-interests method is no longer permitted. Statement No. 141 requires that the purchase method be used for business combinations initiated after June 30, 2001. Management does not anticipate any impact on the consolidated financial statements upon adoption of this statement.

Statement of Financial Accounting Standards No. 142 requires that goodwill no longer be amortized to earnings, but instead be reviewed for impairment. The amortization of goodwill ceases upon adoption of the Statement, which for most companies, will be January 1, 2002. Management does not anticipate any impact on the consolidated financial statements upon adoption of this statement.

Note 4 - Earnings per Share

EPS for the three months ended December 31, 2001 and 2000 have been calculated according to the guidelines of Statement 128. ESOP shares are only considered outstanding for earnings per share calculations when they are committed to be released.

Reconciliation of the numerators and the denominators in the calculation of basic and diluted per share comparisons for net income are as follows:

	Income (Numerator)	Shares (Denominator)	Per Sh Amoun
Three Months Ended December 31, 2001			
Basic EPS			
Net income and income available to common stockholders	$466,668	892,175	$0.5
Effect of dilutive securities options and warrants		40,628	
Diluted EPS			
Income available to common stockholders	$466,668	932,803	$0.5
Three Months Ended December 31, 2000			
Basic EPS			
Net income and income available to common stockholders	$343,185	982,778	$0.3
Effect of dilutive securities options and warrants		5,630	
Diluted EPS			
Income available to common stockholders	$343,185	988,408	$0.3

Note 5 - Dividends

On November 21, 2001, the Board of Directors of the Company declared a quarterly cash dividend of $0.12 per share of common stock, which was paid to stockholders of record on December 17, 2001.

Note 6 - Recent Developments

During the quarter ended December 31, 2001 the Company repurchased 26,000 shares of its common stock. The Company released 3,600 shares due to exercised employee stock options. At December 31, 2001, the Company had 539,143 treasury shares.

Effective September 28, 2001, Falmouth Bank dissolved a subsidiary, The Falmouth Securities Corporation, a Massachusetts securities corporation.

Part I. Item 2. Management's Discussion and Analysis of Financial Condition and Operating Results

General

Falmouth Bancorp, Inc. (the "Company" or "Bancorp"), a Delaware corporation, is the holding company for Falmouth Co-operative Bank, a Massachusetts chartered stock co-operative bank, which is doing business as Falmouth Bank (the "Bank" or "Falmouth"). At December 31, 2001, there were 915,607 shares outstanding. The Company's stock trades on the American Stock Exchange under the symbol "FCB."

The Company's sole business activity is ownership of the Bank. The Company also makes investments in long and short-term marketable securities and other liquid investments. The business of the Bank consists of attracting deposits from the general public and local businesses and using these funds to originate primarily residential and commercial real estate loans located in Falmouth, Massachusetts and surrounding areas and to invest in United States Government and Agency securities. To a lesser extent, the Bank engages in various forms of consumer and home equity lending. The Bank's business strategy is to operate as a profitable community bank dedicated to financing home ownership, small business, and consumer needs in its market area and to provide personal, high quality service to its customers. The Bank has one subsidiary, Falmouth Capital Corporation, a real estate investment trust.

Comparison of Financial Condition at December 31, 2001 and September 30, 2001.

The Company's total assets decreased by $466,000 or 0.3% for the three months ended December 31, 2001, from $147.4 million at September 30, 2001 to $147.0 million at December 31, 2001. Total deposits decreased $122,000 or 0.1%, from $122.2 million at September 30, 2001 to $122.1 million at December 31, 2001. This decrease was due, in part to withdrawals from retail checking, commercial checking, and certificate of deposit accounts during the period. Total net loans were $110.5 million or 90.5% of total deposits at December 31, 2001, as compared to $112.6 million or 92.1% of total deposits at September 30, 2001, representing a decrease of $2.0 million for the quarter. This decrease is due, in part, to the Bank's decision to sell $7.3 million of 1-4 family loans on the secondary market coupled with an increase in loan principal repayments due to refinancing activity caused by a decline in interest rates during the period. Investment securities were $29.5 million or 20.1% of total assets at December 31, 2001, as compared to $20.2 million or 13.7% of total assets at September 30, 2001. Investment securities increased $9.3 million or 46.0% due, in part, to cash flow provided by the Bank's decision to sell a significant portion of its current loan production.

Borrowed funds from the Federal Home Loan Bank of Boston decreased from $7.3 million at September 30, 2001 to $6.8 million at December 31, 2001. The decrease of $522,000 was the result of the repayment of maturing debt along with normal amortization of long term borrowings.

Securities sold under an agreement to repurchase (sweep accounts for commercial depositors) decreased from $676,000 at September 30, 2001 to $655,000 at December 31, 2001. The decrease was attributed to the increased seasonal liquidity needs of selected commercial deposit accounts at December 31, 2001.

Stockholders' equity was $17.0 million at December 31, 2001, and $16.9 million at September 30, 2001. The components of stockholders' equity changed as a result of an increase in retained earnings of $355,000 and a decrease in the unrealized accumulated comprehensive loss in securities of $168,000, which was offset, in part, by an increase in treasury shares purchased of $485,000 under the Company's stock repurchase programs. The ratio of stockholders' equity to total assets was 11.6% at December 31, 2001, and the book value per share of common stock was $18.58, compared to 11.5% and $18.01, respectively, at September 30, 2001.

The ratio of the allowance for loan losses to total loans was .89% at December 31, 2001. Management believes the allowance will be adequate based upon, among other things, past loss experience, prevailing economic conditions, and the level of credit risk in the loan portfolio. However, the Bank may periodically provide additional provisions as deemed necessary to maintain a sufficient allowance for the loan loss to total loan ratio. The Bank plans to continue to set aside additional general reserves as well as specific reserves for commercial loans and large residential mortgages.

Net Income. The Company's net income for the three months ended December 31, 2001 was $467,000 as compared to $343,000 on December 31, 2000. The increase in net income of $123,000 was primarily due to an increase in other income of $133,000, an increase of $57,000 in net interest and dividend after provision for loan losses, a decrease in other expenses of $11,000 offset by an increase in income taxes of $78,000. The annualized return on average assets (ROA) for the three months ended December 31, 2001 was 1.26%, an increase of 22 basis points, as compared to 1.04% for the same period of the prior year. The increase of $123,000 included $116,000 in after tax income from the adoption of SFAS No. 122 and SFAS No. 125 "Mortgage Servicing Assets and Mortgage Servicing Rights."

Interest and Dividend Income. Total interest and dividend income for the three months ended December 31, 2001 was $2.3 million, a decrease of $118,000, as compared to $2.4 million for the three month period ended December 31, 2000. The decrease was attributable to a decrease in interest and fees on loans of $38,000, and a decrease in dividends on securities and other interest of $80,000.

Interest Expense. Total interest expense for the three months ended December 31, 2001 was $986,000 as compared to $1.1 million for the same period of the prior year, a decrease of $141,000. The decrease in interest expense is primarily due to declining short term interest rates offset by an $11.3 million growth in interest bearing deposits for the twelve months ended December 31, 2001.

Net Interest and Dividend Income. Net interest and dividend income for the three-month period ended December 31, 2001 was $1.292 million as compared to $1.270 million for the three months ended December 31, 2000. During the most recent period, there was a $22,000 increase resulting from a $118,000 decrease in interest and dividend income, offset by a $140,000 decrease in interest expense. The net interest margin for the three months ended December 31, 2001 was 3.70%, a decrease of 31 basis points, as compared to 4.01% for the three months ended December 31, 2000. The decrease in net interest margin was primarily the result of a decrease in interest income.

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Provision for Loan Losses. The Bank added $50,000 to its allowance for loan losses during the quarter ended December 31, 2001, as compared to $85,000 for the quarter ended December 31, 2000. This decrease was the result of managements desire to sell a substantial amount of its newly originated loans on the secondary market, thus reducing the amount of growth in loans as compared to the same period of the previous year. Management believes that, although the provision is deemed adequate based on its delinquency and loan loss record, additional provisions may be added from time to time as the loan portfolio expands by loan type and volume, including expansion in the commercial loan portfolio. The Bank reviews the general and specific reserves allocated to each loan type, both on and off the balance sheet. This review procedure allows management to look at the growth and risk of each loan type. If necessary, additional reserves can be allocated where loss exposure appears to have risen. Where commercial loans traditionally have a greater degree of loss exposure, the amount of the allowance may be greater than that of traditional 1-4 family mortgage loan of the same amount. If losses appear eminent within a loan type or in general, allowances could be increased. General allowances are generally increased as the total loan portfolio increases. Net loans decreased $2.0 million for the three months ended December 31, 2001, primarily due to 1-4 family loan sales. This decrease aided in improving the Bank's allowance for loan loss to .89 % of total loans at December 31, 2002. The Bank's Asset/Liability Committee routinely reviews the risk weighting applied to each type of loan. There have been no changes during the period ended December 31, 2001. As of December 31, 2001, the Bank had three non-performing installment loans with combined principal balances of $5,000.

Other Income. Other income for the three months ended December 31, 2001 was $341,000, as compared to $208,000 for the three months ended December 31, 2000. The $133,000 increase was primarily the result of an increase in service charge income of $11,000, an increase in net gains on the sale of mortgages of $169,000 and an increase in other income of $12,000. This was offset, in part, by a decrease in net gains realized from the sale of investment securities of $59,000. Gains on mortgages sold of $186,000 for the three months ended December 31, 2001 was primarily due to the adoption of SFAS No. 122 and SFAS No. 125 "Mortgage Servicing Assets and Mortgage Servicing Rights." Mortgage servicing assets are to be amortized over the expected life of the asset. The expense is not expected to have a significant impact on net income. To the extent that loans serviced for others increase or decrease, the valuation of the mortgage servicing asset will be adjusted accordingly. Large changes over short periods of time in the valuation of the asset could have a significant impact on net earnings. Management does not anticipate large short term changes in the valuation, but expects decreases due to loan pay-offs to be offset by increases in sales of newly originated loans. Management believes that changes in the valuation of the mortgage servicing asset will be gradual and impact on net income will not be significant.

Operating Expenses. Operating expenses for the three months ended December 31, 2001 were $850,000 compared to $861,000 for the three months ended December 31, 2000. The $11,000 decrease was primarily due to the combination of a decrease in salaries and employee benefits of $7,000, a decrease in occupancy expense of $6,000, a decrease in directors' fees of $2,000, a decrease in legal and professional costs of $23,000 and a decrease in other expenses of $1,000, combined with an increase in data processing expense of $23,000 and an increase in equipment expense of $5,000. The annualized ratio of operating expenses to average total assets for the three months ended December 31, 2001 was 2.29%, as compared to 2.57% for the three month period ended December 31, 2000, a decrease of 28 basis points. The operating efficiency ratio improved from 67.48% for the three months period ended December 31, 2000 to 55.69% for the three months period ended December 31, 2001. The decrease in legal and professional cost was due to the absence of third party consultants utilized during the same period of the previous year. Data processing expense increased, in part, due to the increased annual operating costs of Internet Banking and bill paying which were introduced in August 2001.

Liquidity and Capital Resources

The Bank's primary sources of funds consist of deposits, repayment and prepayment of loans and mortgaged-backed securities, maturities of investments and interest-bearing deposits, and funds provided from operations. While scheduled repayments of loans and mortgage-backed securities and maturities of investment securities are predictable sources of funds, deposit flows and loan prepayments are greatly influenced by the general level of interest rates, economic conditions and competition. The Bank uses its liquidity resources principally to fund existing and future loan commitments, to fund net deposit outflows, to invest in other interest-earning assets, to maintain liquidity, and to meet operating expenses.

The Bank is required to maintain adequate levels of liquid assets. This guideline, which may be varied depending upon economic conditions and deposit flows, is based upon a percentage of deposits and short-term borrowings. The Bank has historically maintained a level of liquid assets in excess of regulatory requirements. The Bank's liquidity ratio at December 31, 2001 was 25.0%.

A major portion of the Bank's liquidity consists of short-term securities obligations. The level of these assets is dependent on the Bank's operating, investing, lending and financing activities during any given period. At December 31, 2001, regulatory liquidity totaled $31.8 million. The primary investing activities of the Bank include origination of loans and the purchase of investment securities.

Liquidity management is both a daily and long-term function of management. If the Bank requires funds beyond its ability to generate them internally, the Bank believes that it could borrow additional funds from the FHLB of Boston. At December 31, 2001, the Bank had outstanding advances from the FHLB of Boston in the amount of $6.8 million in short and long-term borrowings. As these advances mature, they will be repaid or re-written as longer term matched borrowings which will assist the match of rate sensitive assets to rate sensitive liabilities.

At December 31, 2001, the Bank had $5.1 million in outstanding residential and commercial commitments to originate loans, as well as $19.9 million in unadvanced loan commitments. If the Bank anticipates that it may not have sufficient funds available to meet its current loan commitments it may commence further matched borrowing from the Federal Home Loan Bank of

Boston. Certificates of deposit that are scheduled to mature in one year or less totaled $43.6 million at December 31, 2001. Based on historical experience, management believes that a significant portion of such deposits will remain with the Bank.

At December 31, 2001 the Bank exceeded all of its regulatory capital requirements.

OTHER INFORMATION

Part II.

Item 1. Legal Proceedings
None

Item 2. Changes in Securities and Use of Proceeds
None

Item 3. Defaults upon Senior Securities
None

Item 4. Submission of Matters to a Vote of Security Holders
None

Item 5. Other Information
None

Item 6. Exhibits and Reports on Form 8-K
None

Falmouth Bancorp, Inc. is a publicly owned bank holding company and the parent corporation of Falmouth Bank, a Massachusetts chartered stock co-operative bank offering traditional products and services. The Bank conducts business through its main office located at 20 Davis Straits, Falmouth, Massachusetts 02540, and its two branch locations in North and East Falmouth. The telephone number is (508) 548-3500.

SIGNATURES

In accordance with the requirements of the Exchange Act, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

FALMOUTH BANCORP, INC.
(Registrant)

Date: February 13, 2002 By: /s/ Santo P. Pasqualucci

Santo P. Pasqualucci
President and Chief Executive Officer

Date: February 13, 2002

By: /s/ George E. Young, III

George E. Young, III
Senior Vice President and
Chief Financial Officer

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