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FALMOUTH BANCORP INC
Form 10QSB
February 11, 2003

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-QSB

(Mark One)

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

For the quarterly period ended December 31, 2002

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
(State or other jurisdiction of
incorporation or organization)

04-3337685
(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 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, 2002 -----
Common Stock, Par Value \$.01	902,573

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

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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

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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.

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Part I. Item I. FALMOUTH BANCORP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

December 31, 2002 and September 30, 2002

	December 31, 2002	September 30, 2002
	-----	-----
	(Unaudited)	
ASSETS		

Cash, due from banks and interest bearing deposits	\$ 3,178,894	\$ 2,916,804
Federal funds sold	9,410,490	4,505,780
	-----	-----
Total cash and cash equivalents	12,589,384	7,422,584
Investments in available-for-sale securities (at fair value)	20,866,992	18,712,954
Investments in held-to-maturity securities (fair values of \$29,613,593 as of December 31, 2002 and \$28,034,474 as of September 30, 2002)	29,591,000	28,060,267
Federal Home Loan Bank stock, at cost	878,000	878,000
Loans, net	84,800,328	95,009,955
Premises and equipment	1,766,706	1,792,016
Accrued interest receivable	1,021,578	1,114,924
Cooperative Central Bank Reserve Fund Deposit	395,395	395,395
Other assets	1,297,584	1,134,907
	-----	-----
Total assets	\$153,206,967	\$154,521,002
	=====	=====
LIABILITIES AND STOCKHOLDERS' EQUITY		

Deposits:		
Noninterest-bearing	\$ 16,575,358	\$ 17,552,180
Interest-bearing	113,565,941	114,164,879
	-----	-----
Total deposits	130,141,299	131,717,059
Securities sold under agreements to repurchase	582,461	471,872
Federal Home Loan Bank advances	5,154,775	5,178,175
Other liabilities	408,695	761,663
	-----	-----
Total liabilities	136,287,230	138,128,769
	-----	-----

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Minority preferred stockholders' equity in a subsidiary company of Falmouth Bank	51,500	53,500
	-----	-----
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	14,036,729	13,981,543
Retained earnings	13,993,160	13,735,221
Unallocated Employee Stock Ownership Plan shares	(279,252)	(301,299)
Treasury stock (552,177 shares as of December 31, 2002; 553,971 shares as of September 30, 2002)	(9,776,127)	(9,807,890)
Unearned compensation	(477,088)	(477,088)
Accumulated other comprehensive loss	(643,732)	(806,301)
	-----	-----
Total stockholders' equity	16,868,237	16,338,733
	-----	-----
Total liabilities and stockholders' equity	\$153,206,967	\$154,521,002
	=====	=====

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, 2002 and 2001
(Unaudited)

	2002	2001
	----	----
Interest and dividend income:		
Interest and fees on loans	\$1,494,869	\$2,021,484
Interest and dividends on securities:		
Taxable	338,112	190,356
Dividends on marketable equity securities	20,447	24,733
Dividends on Cooperative Bank Investment and Liquidity Funds	-	551
Other interest	30,420	40,701
	-----	-----
Total interest and dividend income	1,883,848	2,277,825
	-----	-----
Interest expense:		
Interest on deposits	653,351	898,985
Interest on securities sold under agreement to repurchase	1,983	2,114
Interest on Federal Home Loan Bank advances	62,453	84,515
	-----	-----
Total interest expense	717,787	985,614
	-----	-----
Net interest and dividend income	1,166,061	1,292,211
Provision for loan losses	-	50,000
	-----	-----
Net interest and dividend income after provision for		

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loan losses	1,166,061	1,242,211
	-----	-----
Other income:		
Service charges on deposit accounts	50,365	48,956
Securities gains (losses), net	(76,587)	17,062
Net gains on sales of loans	325,311	186,417
Loan servicing fees	29,192	9,072
Other income	87,800	79,406
	-----	-----
Total other income	416,081	340,913
	-----	-----
Other expense:		
Salaries and employee benefits	487,679	430,099
Occupancy expense	40,981	41,540
Equipment expense	44,824	49,040
Data processing expense	88,705	94,764
Directors' fees	18,610	13,000
Legal and professional fees	56,320	47,447
Other expenses	247,055	174,366
	-----	-----
Total other expenses	984,174	850,256
	-----	-----
Income before income taxes	597,968	732,868
Income taxes	222,850	266,200
	-----	-----
Net income	\$ 375,118	\$ 466,668
	=====	=====
Comprehensive income	\$ 537,687	\$ 634,284
	=====	=====
Earnings per common share	\$ 0.43	\$ 0.52
	=====	=====
Earnings per common share, assuming dilution	\$ 0.41	\$ 0.50
	=====	=====

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 CHANGES IN STOCKHOLDERS' EQUITY

Three Months Ended December 31, 2002
(Unaudited)

Common Stock	Paid-In Capital	Retained Earnings	Unallocated Employee Stock Ownership Plan Shares	Treasury Stock	Un Comp
-----	-----	-----	-----	-----	-----

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Balance, September 30, 2002	\$14,547	\$13,981,543	\$13,735,221	\$(301,299)	\$(9,807,890)	\$(4,117,417)
Employee Stock Ownership Plan		32,720				
ESOP shares released				22,047		
Recognition and retention plan		26,618				
Exercise of stock options and related tax benefit		(4,152)			31,763	
Dividends declared (\$.13 per share)			(117,179)			
Comprehensive income:						
Net income			375,118			
Net change in unrealized holding gain on available-for-sale securities						
Comprehensive income						
Balance, December 31, 2002	\$14,547	\$14,036,729	\$13,993,160	\$(279,252)	\$(9,776,127)	\$(4,117,417)

Three Months Ended December 31, 2001
(Unaudited)

	Common Stock	Paid-In Capital	Retained Earnings	Unallocated Employee Stock Ownership Plan Shares	Treasury Stock	Unallocated
	-----	-----	-----	-----	-----	-----
Balance, September 30, 2001	\$14,547	\$13,901,279	\$12,676,198	\$(389,483)	\$(8,749,737)	\$(4,117,417)
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)	\$(4,117,417)

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

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For the Three Months Ended December 31, 2002 and 2001

	2002 ----- (Unaudited)	2001 ----- (Unaudited)
Cash flows from operating activities		
Net income	\$ 375,118	\$ 466,668
Adjustments to reconcile net income to net cash provided by operating activities:		
Realized (gains) losses on available-for-sale investment securities, net	76,587	(17,062)
Amortization of investment securities, net	297,975	107,117
Provision for loan loss	-	50,000
Change in deferred loan costs net of origination fees	(50,735)	(4,652)
Net gains on sales of loans	(325,311)	(186,417)
Depreciation and amortization	42,641	56,682
Loss on disposal of equipment	-	1,071
Decrease in accrued interest receivable	93,346	33,083
Decrease in prepaid expenses	23,072	9,696
Increase in other assets	(163,732)	(171,567)
Recognition and retention plan (RRP)	26,618	27,060
Increase (decrease) in accrued expenses	7,331	(6,381)
Increase (decrease) in taxes payable	(105,765)	255,196
Increase (decrease) in accrued interest payable	(28)	390
Decrease in other liabilities	(360,271)	(90,409)
	-----	-----
Net cash provided by (used in) operating activities	(63,154)	530,475
	-----	-----
Cash flows from investing activities		
Purchases of available-for-sale securities	(6,687,065)	(3,086,751)
Proceeds from sales of available-for-sale securities	93,941	60,868
Proceeds from maturities of available-for-sale securities	4,531,090	503,805
Purchases of held-to-maturity securities	(11,317,034)	(8,101,183)
Proceeds from maturities of held-to-maturity securities	9,566,052	1,506,326
Loan originations and principal collections, net	(11,499,798)	(6,229,612)
Proceeds from sales of loans	22,085,471	8,392,110
Capital expenditures	(17,331)	(12,942)
	-----	-----
Net cash provided by (used in) investing activities	6,755,326	(6,967,379)
	-----	-----
Cash flows from financing activities:		
Net increase in demand deposits, NOW and savings accounts	627,582	1,775,972
Net decrease in time deposits	(2,203,342)	(1,897,719)
Net increase (decrease) in securities sold under agreements to repurchase	110,589	(21,033)
Repayments of Federal Home Loan Bank long-term advances	(23,400)	(522,064)
Redemption of preferred shares relative to minority interests	(2,000)	-
Proceeds from exercise of stock options	27,611	54,995
Employee Stock Ownership Plan	32,720	22,546
Unallocated ESOP shares released	22,047	22,046
Dividends paid	(117,179)	(111,481)
Purchase of treasury stock	-	(546,760)
	-----	-----
Net cash used in financing activities	(1,525,372)	(1,223,498)
	-----	-----
Increase (decrease) in cash and cash equivalents	5,166,800	(7,660,402)

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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, 2002 and 2001
(continued)

Cash and cash equivalents at beginning of period	7,422,584	10,835,279
	-----	-----
Cash and cash equivalents at end or period	\$ 12,589,384	\$ 3,174,877
	=====	=====
Supplemental disclosures		
Interest paid	\$ 717,815	\$ 985,224
Income taxes paid	328,615	11,004

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

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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, 2002. The results of operations for the three-month period ended December 31, 2002 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 2002 Annual Report contained on Form 10-KSB.

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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

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, Business Combinations, 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. The adoption of SFAS No. 141 had no immediate effect on the Company's consolidated financial statements since it had no pending business combinations as of June 30, 2001

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or as of the date of the issuance of these consolidated financial statements. If the Company consummates business combinations in the future, any such combinations that would have been accounted for by the pooling-of-interests method under Opinion 16, will be accounted for under the purchase method and the difference in accounting could have a substantial impact on the Company's consolidated financial statements.

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. All of the provisions of SFAS No. 142 were effective for the Company beginning with its fiscal year ending September 30, 2003. The adoption of SFAS No. 142 did not have an impact on the Company's consolidated financial statements.

In August 2001, the FASB issued SFAS No. 144 "Accounting for Impairment or Disposal of Long Lived Assets." The provisions of SFAS No. 144 are required to be adopted starting with fiscal years beginning after December 15, 2001. The adoption of this Statement did not have a material impact on the Company's consolidated financial statements.

In June 2002, the FASB issued SFAS No. 146 "Accounting for Costs Associated with Exit or Disposal Activities." This statement requires that a liability for a cost associated with an exit or disposal activity be recognized and measured initially at fair value only when the liability is incurred. SFAS No. 146 is effective for exit or disposal activities that

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are initiated after December 31, 2002. Management does not anticipate that this Statement will have any material impact on the Company's consolidated financial statements.

In October 2002, the FASB issued SFAS No. 147 "Acquisitions of Certain Financial Institutions", an Amendment of SFAS Nos. 72 and 144 and FASB Interpretation No. 9 SFAS No. 72 "Accounting for Certain Acquisitions of Banking or Thrift Institutions" and FASB interpretation No. 9 "Applying APB Opinions No. 16 and 17 When a Savings and Loan Association Is Acquired in a Business Combination Accounted for by the Purchase Method" that provided interpretive guidance on the application of the purchase method to acquisitions of financial institutions. SFAS No. 147 was effective October 1, 2002. There was no impact on the Company's consolidated financial statements on adoption of this Statement.

Note 4 - Earnings per Share

Earnings per share (EPS) for the three months ended December 31, 2002 and 2001 have been calculated according to the guidelines of SFAS Statement 128. ESOP shares are only considered outstanding for EPS calculations when they are committed to be released.

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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 Share Amount
	-----	-----	-----
Three Months Ended December 31, 2002			
Basic EPS			

Net income and income available to common stockholders	\$375,118	870,641	\$0.43
Effect of dilutive securities options and warrants		47,923	
	-----	-----	
Diluted EPS			

Income available to common stockholders	\$375,118	918,564	\$0.41
	=====	=====	
THREE MONTHS ENDED DECEMBER 31, 2001			
Basic EPS			

Net income and income available to common stockholders	\$466,668	892,175	\$0.52
Effect of dilutive securities options and warrants		40,628	
	-----	-----	
Diluted EPS			

Income available to common stockholders	\$466,668	932,803	\$0.50
	=====	=====	

Note 5 - Dividends

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On November 20, 2002, the Board of Directors of the Company declared a quarterly cash dividend of \$0.13 per share of common stock, which was paid on December 18, 2002 to stockholders of record at the close of business on December 4, 2002.

Note 6 - Recent Developments

During the quarter ended December 31, 2002, the Company released 1,794 shares due to exercised employee stock options. At December 31, 2002, the Company had 552,177 treasury shares.

Note 7 - Contingency

Falmouth Capital Corporation ("FCC"), a subsidiary of the Bank, was established in December 1999 as a Massachusetts-chartered real estate investment trust (the "REIT"). The Bank received dividends from FCC.

The Bank, and several other financial institutions operating in the Commonwealth of Massachusetts with similar real estate investment trust subsidiaries, have recently received Notices of Intent to Assess additional state excise taxes from the Massachusetts Department of Revenue (the "DOR"), challenging the dividends received deduction claimed by the Bank and other institutions. The Bank received a Notice of Intent to assess a tax in the amount of \$470,972 and intends to vigorously appeal this Notice. The Company has not recorded a loss provision in regard to this matter.

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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, 2002, there were 902,573 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.

Critical Accounting Policies

The Notes to our Audited Consolidated Financial Statements for the year ended September 30, 2002, included in our Annual Report, contain a summary of our significant accounting policies. We believe our policies

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with respect to the methodology for our determination of the allowance for loan losses, the valuation of mortgage servicing rights and asset impairment judgments, and other than temporary declines in the value of our securities, involve a higher degree of complexity and require management to make difficult and subjective judgments which often require assumptions or estimates about highly uncertain matters. Changes in these judgments, assumptions or estimates could cause reported results to differ materially. These critical policies and their application are periodically reviewed by the Audit Committee and our Board of Directors.

Comparison of Financial Condition at December 31, 2002 and September 30, 2002.

Company's total assets decreased by \$1.3 million, or 0.8%, from \$154.5 million at September 30, 2002 to \$153.2 million at December 31, 2002. Total deposits decreased \$1.6 million or 1.2%, from \$131.7 million at September 30, 2002 to \$130.1 million at December 31, 2002. This decrease was due, in part, to withdrawals from demand deposits and certificates of deposit during the period. Total net loans were \$84.8 million or 65.2% of total deposits at December 31, 2002, as compared to \$95.0 million or 72.1% of total deposits at September 30, 2001, representing a decrease of \$10.2 million for the quarter. This decrease was due, in part, to mortgage loans refinanced at lower rates and sold in the secondary market with the loan servicing retained. Investment securities were \$51.3 million or 33.5% of total assets at December 31, 2002, as compared to \$47.7 million or 30.9% of total assets at September 30, 2002. Investment securities increased \$3.7 million or 7.8%, in part due to the reinvestment of cash flows generated from loan payoffs and sold loans into short-term securities.

Borrowed funds from the Federal Home Loan Bank of Boston decreased from \$5,178,000 at September 30, 2002 to \$5,154,000 at December 31, 2002. The decrease of \$24,000 was the result of normal amortization

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of long term borrowings.

Securities sold under an agreement to repurchase (sweep accounts for commercial depositors) increased from \$472,000 at September 30, 2002 to \$582,000 at December 31, 2002. The increase was attributed to a pricing adjustment on these relationships as well as the seasonal liquidity requirements of account holders.

Stockholders' equity was \$16.9 million at December 31, 2002, and \$16.3 million at September 30, 2002. The change in stockholders' equity was due to an increase in retained earnings of \$258,000, an increase in accumulated other comprehensive income of \$163,000 and the routine effects of stock based benefit plans of \$109,000. The ratio of stockholders' equity to total assets was 11.0% at December 31, 2002, and the book value per share of common stock was \$18.69, compared to 10.6% and \$18.14, respectively, at September 30, 2002.

The ratio of the allowance for loan losses to total loans was 1.10% at December 31, 2002. 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, during its regular reviews of delinquencies and its loan portfolio, may provide additional provisions as deemed necessary to maintain a sufficient allowance for the loan loss to total loan ratio.

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Net Income. The Company's net income for the three months ended December 31, 2002 was \$375,000, as compared to \$467,000 for the three months ended December 31, 2001. The decrease in net income of \$92,000 was due, in part, to a decrease in interest and dividend income of \$394,000 that was offset, in part, by a decrease in interest expense of \$268,000. Other key factors included an increase in other income of \$75,000, a decrease in the provision for loan losses of \$50,000, an increase in other expenses of \$134,000 and a decrease in income taxes of \$43,000. The annualized return on average assets (ROA) for the three months ended December 31, 2002 was 0.97%, a decrease of 29 basis points, as compared to 1.26% for the same period of the prior year. Interest and dividend income decreased, primarily as the result of low interest rates, loan payoffs, and loan sales during the period. The decrease in interest expense was primarily due to a reduction in the general level of interest rates and a slight reduction in total deposits at the same time.

Interest and Dividend Income. Total interest and dividend income for the three months ended December 31, 2002 was \$1.9 million, a decrease of \$394,000, as compared to \$2.3 million for the three month period ended December 31, 2001. The decrease was attributable to a decrease in interest and fees on loans of \$527,000, which was the result of generally lower interest rates and a decrease in loans held for investment, offset by an increase in interest on debt securities, dividends on equity securities and other interest of \$133,000.

Interest Expense. Total interest expense for the three months ended December 31, 2002 was \$718,000 as compared to \$986,000 for the same period of the prior year, a decrease of \$268,000. The decrease in interest expense is primarily due to declining short term interest rates, offset by an \$6.2 million growth in interest bearing deposits for the twelve months ended December 31, 2002.

Net Interest and Dividend Income. Net interest and dividend income was \$1.2 million for the three-month period ended December 31, 2002 and \$1.3 million for the three months ended December 31, 2001. The \$126,000 decrease was the result of a \$394,000 decrease in interest and dividend income, offset by a \$268,000 decrease in interest expense. The net interest margin for the three months ended December 31, 2002 was 3.20%, a decrease of 45 basis points, as compared to 3.65% for the three months ended December 31, 2001. The decrease in net interest margin was primarily the result of a decrease in the yield on interest earning assets.

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Provision for Loan Losses. The Bank made no additional provision to its allowance for loan losses during the quarter ended December 31, 2002, as compared to a provision of \$50,000 for the quarter ended December 31, 2001. This was the result of management's 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.

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If losses appear imminent 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 \$10.2 million for the three months ended December 31, 2002, primarily due to 1-4 family loan sales. This decrease aided in improving the Bank's allowance for loan loss to 1.10% 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, 2002. As of December 31, 2002, the Bank had one non-performing commercial loan with a principal balance of \$42,000.

Other Income. Other income for the three-month period ended December 31, 2002 was \$416,000, as compared to \$341,000 for the three months ended December 31, 2001. The \$75,000 increase was primarily the result of an increase in service charge income of \$1,000, an increase in net gains on mortgages sold of \$139,000, and an increase in loan servicing fees and other income of \$29,000. This was offset, in part, by an increase in net losses realized from the sale of investment securities of \$94,000. Gains on sales of mortgage loans of \$325,000 for the three months ended December 31, 2002 was due to the increased sales of mortgage loans in the secondary market.

Operating Expenses. Operating expenses for the three months ended December 31, 2002 were \$984,000, as compared to \$850,000 for the three months ended December 31, 2001. The \$134,000 increase was primarily due to the combination of an increase in salaries and employee benefits of \$57,000, an increase in Directors' fees of \$6,000, an increase in legal and professional costs of \$9,000, and an increase in other expenses of \$73,000, combined with a decrease in data processing expense of \$6,000 a decrease in occupancy expense of \$1,000, and a decrease in equipment expense of \$4,000. The annualized ratio of operating expenses to average total assets for the three months ended December 31, 2002 was 2.54%, as compared to 2.29% for the three-month period ended December 31, 2001, an increase of 25 basis points. The increase in other expenses was primarily due to the amortization of mortgage servicing rights of the large number of re-financed mortgages sold.

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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, 2002 was 46.0%.

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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, 2002, regulatory liquidity totaled \$62.4 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 Federal Home Loan Bank of Boston (FHLB). At December 31, 2002, the Bank had outstanding advances from the FHLB in the amount of \$5.2 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, 2002, the Bank had \$8.8 million in outstanding residential and commercial commitments to originate loans, as well as \$22.8 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 FHLB. Certificates of deposit that are scheduled to mature in one year or less totaled \$42.0 million at December 31, 2002. Based on historical experience, management believes that a significant portion of such deposits will remain with the Bank.

At December 31, 2002 the Bank exceeded all of its regulatory capital requirements.

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Part 1. Item 3.

Controls and Procedures.

During the 90-day period prior to the filing date of this report, management, including the Company's President and Chief Executive Officer and Senior Vice President and Chief Financial Officer, evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures. Based upon and as of the date of that evaluation, the President and Chief Executive Officer and Senior Vice President and Chief Financial Officer concluded that the disclosure controls and procedures were effective, in all material respects, to ensure that information required to be disclosed in the reports the Company files and submits under the Exchange Act is recorded, processed, summarized and reported as and when required.

There have been no significant changes in the Company's internal controls or in other factors which could significantly affect internal controls subsequent to the date the Company carried out its evaluation. There were no significant deficiencies or material weaknesses identified in the evaluation and therefore, no corrective actions were taken.

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OTHER INFORMATION

Part II.

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- 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

The Company's Chief Executive Officer and Chief Financial Officer have furnished statements relating to its Form 10-Q for the quarter ended December 31, 2002 pursuant to 18 U.S.C. section 1350, as adopted pursuant to section 906 of the Sarbanes-Oxley Act of 2002. The statements are attached hereto as Exhibits 99.1 and 99.2.

Item 6. Exhibits and Reports on Form 8-K

- (a) Exhibits
 - Exhibit 99.1, Statement Furnished Pursuant to Section 906 of the Sarbanes-Oxley Act.
 - Exhibit 99.2, Statement Furnished Pursuant to Section 906 of the Sarbanes-Oxley Act.
- (b) Reports on Form 8-K
None

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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: 2/1/03

By: /s/ Santo P. Pasqualucci

Santo P. Pasqualucci
President and Chief Executive Officer

Date: 2/1/03

By: /s/ George E. Young, III

George E. Young, III
Senior Vice President and Chief

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Financial Officer

CERTIFICATIONS

I, Santo P. Pasqualucci, certify that:

1. I have reviewed this quarterly report on Form 10-QSB of Falmouth Bancorp, Inc.;
2. Based on my knowledge, this annual 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 annual report; and
3. Based on my knowledge, the financial statements, and other financial information included in this annual 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 annual report.
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and have:
 - (a) designed such disclosure controls and procedures 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 annual report is being prepared;
 - (b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this annual report (the "Evaluation Date"); and
 - (c) presented in this annual report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent function):
 - (a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
 - (b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and
6. The registrant's other certifying officers and I have indicated in this annual report whether or not there significant changes in

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internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: February 3, 2003

/s/ Santo P. Pasqualucci

Santo P. Pasqualucci
President and Chief Executive
Officer

I, George E. Young, III, certify that

1. I have reviewed this quarterly report on Form 10-QSB of Falmouth Bancorp, Inc.;
2. Based on my knowledge, this annual 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 annual report; and
3. Based on my knowledge, the financial statements, and other financial information included in this annual 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 annual report.
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:
 - (a) designed such disclosure controls and procedures 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 annual report is being prepared;
 - (b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this annual report (the "Evaluation Date"); and
 - (c) presented in this annual report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent function):
 - (a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

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(b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6. The registrant's other certifying officers and I have indicated in this annual report whether or not there significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: February 3, 2003

/s/ George E. Young, III

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