PENNS WOODS BANCORP INC
Form 10-Q
November 07, 2007

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

x **Quarterly Report pursuant to Section 13 or 15 (d) of the Securities Exchange Act of 1934**

for the Quarterly Period Ended September 30, 2007.

o **Transition report pursuant to Section 13 or 15 (d) of the Exchange Act**

for the Transition Period from to .

No. 0-17077

(Commission File Number)

PENNS WOODS BANCORP, INC.

(Exact name of Registrant as specified in its charter)

PENNSYLVANIA	**23-2226454**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

300 Market Street, Williamsport, Pennsylvania **17701-0967**

(Address of principal executive offices) (Zip Code)

(570) 322-1111

Registrant s telephone number, including area code

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

YES x NO o

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

Large accelerated filer o Accelerated filer x Non-accelerated filer o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

YES o NO x

On November 1, 2007 there were 3,877,534 shares of the Registrant s common stock outstanding.

PENNS WOODS BANCORP, INC.

INDEX TO QUARTERLY REPORT ON FORM 10-Q

Page

Number

Number

Part I	**Financial Information**

Item 1. **Financial Statements**

Part II **Other Information**

Part I. FINANCIAL INFORMATION

Item 1. Financial Statements

PENNS WOODS BANCORP, INC.

CONSOLIDATED BALANCE SHEET

(UNAUDITED)

(In Thousands, Except Share Data)	**September 30, 2007**	**December 31, 2006**
ASSETS		
Noninterest-bearing balances	$ 13,228	$ 15,348
Interest-bearing deposits in other financial institutions	15	25
Total cash and cash equivalents	13,243	15,373
Investment securities, available for sale, at fair value	204,758	185,200
Investment securities held to maturity (fair value of $278 and $286)	276	283
Loans held for sale	6,503	3,716
Loans	357,715	360,384
Less: Allowance for loan losses	4,092	4,185
Loans, net	353,623	356,199
Premises and equipment, net	6,841	6,737
Accrued interest receivable	3,274	2,939
Bank-owned life insurance	12,275	11,346
Investment in limited partnerships	4,447	4,950
Goodwill	3,032	3,032
Other assets	5,057	2,510
TOTAL ASSETS	$ 613,329	$ 592,285
LIABILITIES		
Interest-bearing deposits	$ 331,864	$ 322,031
Noninterest-bearing deposits	72,990	73,160
Total deposits	404,854	395,191
Short-term borrowings	44,793	34,697
Long-term borrowings, Federal Home Loan Bank (FHLB)	86,378	82,878
Accrued interest payable	1,838	1,532
Other liabilities	3,914	3,393
TOTAL LIABILITIES	541,777	517,691
SHAREHOLDERS EQUITY		
Common stock, par value $8.33, 10,000,000 shares authorized; 4,006,084 and 4,003,514 shares issued	33,384	33,362
Additional paid-in capital	17,869	17,810
Retained earnings	27,552	25,783
Accumulated other comprehensive income (loss):		
Net unrealized (loss) gain on available for sale securities	(1,861)	2,139
Defined benefit plan	(579)	(579)
Less: Treasury stock at cost, 128,802 and 102,772 shares	(4,813)	(3,921)
TOTAL SHAREHOLDERS EQUITY	71,552	74,594

TOTAL LIABILITIES AND SHAREHOLDERS EQUITY	$	613,329	$	592,285

See accompanying notes to the unaudited consolidated financial statements.

PENNS WOODS BANCORP, INC.

CONSOLIDATED STATEMENT OF INCOME

(UNAUDITED)

(In Thousands, Except Per Share Data)	Three Months Ended September 30, 2007	Three Months Ended September 30, 2006	Nine Months Ended September 30, 2007	Nine Months Ended September 30, 2006
INTEREST AND DIVIDEND INCOME				
Loans including fees	$ 6,621	$ 6,355	$ 19,560	$ 18,250
Investment Securities:				
Taxable	964	874	2,711	2,691
Tax-exempt	1,108	1,004	3,271	2,993
Dividend and other interest income	284	314	907	982
TOTAL INTEREST AND DIVIDEND INCOME	8,977	8,547	26,449	24,916
INTEREST EXPENSE				
Deposits	2,835	2,447	8,215	6,252
Short-term borrowings	368	306	1,100	1,221
Long-term borrowings, FHLB	909	954	2,735	2,844
TOTAL INTEREST EXPENSE	4,112	3,707	12,050	10,317
NET INTEREST INCOME	4,865	4,840	14,399	14,599
PROVISION FOR LOAN LOSSES	10	89	60	485
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	4,855	4,751	14,339	14,114
NON-INTEREST INCOME				
Deposit service charges	546	596	1,654	1,773
Securities gains, net		561	619	1,385
Bank-owned life insurance	109	94	310	272
Gain on sale of loans	282	264	654	624
Insurance commissions	625	502	1,613	1,732
Other	444	370	1,316	1,154
TOTAL NON-INTEREST INCOME	2,006	2,387	6,166	6,940
NON-INTEREST EXPENSE				
Salaries and employee benefits	2,330	2,174	6,912	6,620
Occupancy, net	319	308	987	826
Furniture and equipment	267	309	850	894
Pennsylvania shares tax	160	151	482	447
Other	1,354	1,172	3,667	3,356
TOTAL NON-INTEREST EXPENSE	4,430	4,114	12,898	12,143
INCOME BEFORE INCOME TAX PROVISION	2,431	3,024	7,607	8,911
INCOME TAX PROVISION	109	560	669	1,558
NET INCOME	$ 2,322	$ 2,464	$ 6,938	$ 7,353
EARNINGS PER SHARE - BASIC	$ 0.60	$ 0.63	$ 1.78	$ 1.87
EARNINGS PER SHARE - DILUTED	$ 0.60	$ 0.63	$ 1.78	$ 1.87

WEIGHTED AVERAGE SHARES OUTSTANDING - BASIC	3,881,488	3,927,261	3,889,310	3,942,533
WEIGHTED AVERAGE SHARES OUTSTANDING - DILUTED	3,881,676	3,927,740	3,889,573	3,943,016
DIVIDENDS PER SHARE	$ 0.45	$ 0.44	$ 1.33	$ 1.29

See accompanying notes to the unaudited consolidated financial statements.

PENNS WOODS BANCORP, INC.

CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

(UNAUDITED)

(In Thousands Except Per Share Data)	COMMON STOCK SHARES	COMMON STOCK AMOUNT	ADDITIONAL PAID-IN CAPITAL	RETAINED EARNINGS	ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)	TREASURY STOCK	TOTAL SHAREHOLDERS EQUITY
Balance, December 31, 2006	4,003,514	$ 33,362	$ 17,810	$ 25,783	$ 1,560	$ (3,921)	$ 74,594
Comprehensive Income:							
Net income				6,938			6,938
Unrealized loss on investments available for sale, net of reclassification adjustment, net of income tax benefit of $2,061					(4,000)		(4,000)
Total comprehensive income							2,938
Dividends declared, ($1.33 per share)				(5,169)			(5,169)
Purchase of treasury stock (26,030 shares)						(892)	(892)
Stock options exercised	330	3	5				8
Common shares issued for employee stock purchase plan	2,240	19	54				73
Balance, Septamber 30, 2007	4,006,084	$ 33,384	$ 17,869	$ 27,552	$ (2,440)	$ (4,813)	$ 71,552

(In Thousands Except Per Share Data)	COMMON STOCK SHARES	COMMON STOCK AMOUNT	ADDITIONAL PAID-IN CAPITAL	RETAINED EARNINGS	ACCUMULATED OTHER COMPREHENSIVE INCOME	TREASURY STOCK	TOTAL SHAREHOLDERS EQUITY
Balance, December 31, 2005	4,002,159	$ 33,351	$ 17,772	$ 22,938	$ 850	$ (992)	$ 73,919
Comprehensive Income:							
Net income				7,353			7,353
Unrealized gain on investments available for sale, net of reclassification adjustment, net of income tax of $424					824		824
Total comprehensive income							8,177
Dividends declared, ($1.29 per share)				(5,083)			(5,083)
Purchase of treasury stock (60,000 shares)						(2,303)	(2,303)
Common shares issued for employee stock purchase plan	421	3	12				15
Balance, September 30, 2006	4,002,580	$ 33,354	$ 17,784	$ 25,208	$ 1,674	$ (3,295)	$ 74,725

See accompanying notes to the unaudited consolidated financial statements.

PENNS WOODS BANCORP, INC.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

(UNAUDITED)

(In Thousands)	**Three Months Ended September 30, 2007**	**2006**	**Nine Months Ended September 30, 2007**	**2006**
Net Income				
Other comprehensive (loss) income:	$ 2,322	$ 2,464	$ 6,938	$ 7,353
Change in net unrealized gains (losses) on available for sale securities	2,415	5,026	(5,442)	2,633
Less: Reclassification adjustment for net gains included in net income		561	619	1,385
Other comprehensive income (loss) before tax	2,415	4,465	(6,061)	1,248
Income tax expense (benefit) related to other comprehensive income (loss)	821	1,518	(2,061)	424
Other comprehensive income (loss), net of tax	1,594	2,947	(4,000)	824
Comprehensive income	$ 3,916	$ 5,411	$ 2,938	$ 8,177

See accompanying notes to the unaudited consolidated financial statements.

PENNS WOODS BANCORP, INC.

CONSOLIDATED STATEMENT OF CASH FLOWS

(UNAUDITED)

(In Thousands)	**Nine Months Ended September 30, 2007**	**2006**
OPERATING ACTIVITIES		
Net Income	$ 6,938	$ 7,353
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	523	549
Provision for loan losses	60	485
Accretion and amortization of investment security discounts and premiums	(738)	(575)
Securities gains, net	(619)	(1,385)
Originations of loans held for sale	(33,903)	(28,031)
Proceeds of loans held for sale	31,770	27,454
Gain on sale of loans	(654)	(624)
Earnings on bank-owned life insurance	(310)	(272)
Other, net	303	132
Net cash provided by operating activities	3,370	5,086
INVESTING ACTIVITIES		
Investment securities available for sale:		
Proceeds from sales	39,226	35,879
Proceeds from calls and maturities	4,290	5,445
Purchases	(67,067)	(31,938)
Investment securities held to maturity:		
Proceeds from calls and maturities	11	25
Purchases		(25)
Net decrease (increase) in loans	2,516	(18,288)
Acquisition of bank premises and equipment	(627)	(767)
Proceeds from the sale of foreclosed assets	66	83
Purchase of bank-owned life insurance	(619)	(212)
Investment in limited partnership		(1,535)
Proceeds from redemption of regulatory stock	3,045	3,177
Purchases of regulatory stock	(3,620)	(2,034)
Net cash used for investing activities	(22,779)	(10,190)
FINANCING ACTIVITIES		
Net increase in interest-bearing deposits	9,833	51,160
Net decrease in noninterest-bearing deposits	(170)	(1,730)
Proceeds of long-term borrowings, FHLB	20,000	
Repayment of long-term borrowings, FHLB	(16,500)	(1,600)
Net increase (decrease) in short-term borrowings	10,096	(35,977)
Dividends paid	(5,169)	(5,083)
Issuance of common stock	73	15
Stock options exercised	8	
Purchase of treasury stock	(892)	(2,303)
Net cash provided by financing activities	17,279	4,482
NET DECREASE IN CASH AND CASH EQUIVALENTS	(2,130)	(622)
CASH AND CASH EQUIVALENTS, BEGINNING	15,373	14,090
CASH AND CASH EQUIVALENTS, ENDING	$ 13,243	$ 13,468
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION		

Interest paid	$	11,744	$	9,915
Income taxes paid		1,185		2,075
Transfer of loans to foreclosed real estate				51

See accompanying notes to the unaudited consolidated financial statements.

PENNS WOODS BANCORP, INC. AND SUBSIDIARIES

NOTES TO
CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 1. Basis of Presentation

The consolidated financial statements include the accounts of Penns Woods Bancorp, Inc. (the Company) and its wholly-owned subsidiaries: Woods Investment Company, Inc., Woods Real Estate Development Company, Inc., and Jersey Shore State Bank (the Bank) and its wholly-owned subsidiary The M Group, Inc. D/B/A The Comprehensive Financial Group (The M Group). All significant inter-company balances and transactions have been eliminated in the consolidation.

The interim financial statements are unaudited but, in the opinion of management, reflect all adjustments necessary for the fair presentation of results for such periods. All of those adjustments are of a normal, recurring nature. The results of operations for any interim period are not necessarily indicative of results for the full year. These financial statements should be read in conjunction with financial statements and notes thereto contained in the Company s Annual Report on Form 10-K for the year ended December 31, 2006.

The accounting policies followed in the presentation of interim financial results are the same as those followed on an annual basis. These policies are presented on pages 40 thru 46 of the Annual Report on Form 10-K for the year ended December 31, 2006.

In reference to the attached financial statements, all adjustments are of a normal recurring nature pursuant to Rule 10-01 (b) (8) of Regulation S-X.

Note 2. Recent Accounting Pronouncements

In February 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (FAS) No. 155, *Accounting for Certain Hybrid Instruments, as an amendment of FASB Statements No. 133 and 140*. FAS No. 155 allows financial instruments that have embedded derivatives to be accounted for as a whole (eliminating the need to bifurcate the derivative from its host) if the holder elects to account for the whole instrument on a fair value basis. This statement is effective for all financial instruments acquired or issued after the beginning of an entity s first fiscal year that begins after September 15, 2006. The adoption of this standard is not expected to have a material effect on the Company s results of operations or financial position.

In March 2006, the FASB issued FAS No. 156, *Accounting for Servicing of Financial Assets*. This Statement, which is an amendment to FAS No. 140, will simplify the accounting for servicing assets and liabilities, such as those common with mortgage securitization activities. Specifically, FAS No. 156 addresses the recognition and measurement of separately recognized servicing assets and liabilities and provides an approach to simplify efforts to obtain hedge-like (offset) accounting. FAS No. 156 also clarifies when an obligation to service financial assets should be separately recognized as a servicing asset or a servicing liability, requires that a separately recognized servicing asset or servicing liability be initially measured at fair value, if practicable, and permits an entity with a separately recognized servicing asset or servicing liability to choose either of the amortization or fair value methods for subsequent measurement. The provisions of FAS No. 156 are effective as of the beginning of the first fiscal year that begins after September 15, 2006. The adoption of this standard is not expected to have a material effect on the Company s results of operations or financial position.

In September 2006, the FASB issued FAS No. 157, *Fair Value Measurements*, which provides enhanced guidance for using fair value to measure assets and liabilities. The standard applies whenever other standards require or permit assets or liabilities to be measured at fair value. The standard does not expand the use of fair value in any new circumstances. FAS No. 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. Early adoption is permitted. The adoption of this standard is not expected to have a material effect on the Company s results of operations or financial position.

In September 2006, the FASB issued FAS No. 158, *Employers Accounting for Defined Benefit Pension and Other Post Retirement Plans, an amendment of FASB Statements No. 87, 88, 106 and 132(R)*. FAS No. 158 requires that a company recognize the overfunded or underfunded status of its defined benefit post retirement plans (other than multiemployer plans) as an asset or liability in its statement of financial position and that it recognize changes in the funded status in the year in which the changes occur through other comprehensive income. FAS No. 158 also requires the measurement of defined benefit plan assets and obligations as of the fiscal year end, in addition to footnote disclosures. On December 31, 2006, the Company adopted FAS No. 158, except for the measurement provisions, which are effective for fiscal years ending after December 15, 2008. The adoption of this standard is not expected to have a material effect on the Company s results of operations or financial position.

In February 2007, the FASB issued FAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115*, which provides all entities with an option to report selected financial assets and liabilities at fair value. The objective of the FAS No. 159 is to improve financial reporting by providing entities with the opportunity to mitigate volatility in earnings caused by measuring related assets and liabilities differently without having to apply the complex provisions of hedge accounting. FAS No. 159 is effective as of the beginning of an entity s first fiscal year beginning after November 15, 2007. Early adoption is permitted as of the beginning of a fiscal year that begins on or before November 15, 2007 provided the entity also elects to apply the provisions of FAS No. 157, *Fair Value Measurements*. The adoption of this standard is not expected to have a material effect on the Company s results of operations or financial position.

In June 2006, the FASB issued FASB Interpretation No. 48 (FIN 48), *Accounting for Uncertainty in Income Taxes*. FIN 48 is an interpretation of FAS No. 109, *Accounting for Income Taxes*, and it seeks to reduce the diversity in practice associated with certain aspects of measurement and recognition in accounting for income taxes. In addition, FIN No. 48 requires expanded disclosure with respect to the uncertainty in income taxes and is effective for fiscal years beginning after December 15, 2006. The adoption of this standard is not expected to have a material effect on the Company s results of operations or financial position.

In September 2006, the FASB reached consensus on the guidance provided by Emerging Issues Task Force Issue 06-4 (EITF 06-4), *Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements*. The guidance is applicable to endorsement split-dollar life insurance arrangements, whereby the employer owns and controls the insurance policy, that are associated with a postretirement benefit. EITF 06-4 requires that for a split-dollar life insurance arrangement within the scope of the Issue, an employer should recognize a liability for future benefits in accordance with FAS No. 106 (if, in substance, a postretirement benefit plan exists) or Accounting Principles Board Opinion No. 12 (if the arrangement is, in substance, an individual deferred compensation contract) based on the substantive agreement with the employee. EITF 06-4 is effective for fiscal years beginning after December 15, 2007. The Company is currently evaluating the impact the adoption of the EITF will have on the Company s results of operations or financial condition.

In September 2006, the FASB reached consensus on the guidance provided by Emerging Issues Task Force Issue 06-5 (EITF 06-5), *Accounting for Purchases of Life Insurance Determining the Amount That Could Be Realized in Accordance with FASB Technical Bulletin No. 85-4, Accounting for Purchases of Life Insurance*. EITF 06-5 states that a policyholder should consider any additional amounts included in the contractual terms of the insurance policy other than the cash surrender value in determining the amount that could be realized under the insurance contract. EITF 06-5 also states that a policyholder should determine the amount that could be realized under the life insurance contract assuming the surrender of an individual-life by individual-life policy (or certificate by certificate in a group policy). EITF 06-5 is effective for fiscal years beginning after December 15, 2006. The Company is currently evaluating the impact the adoption of the standard will have on the Company s results of operations or financial condition.

In March 2007, the FASB ratified Emerging Issues Task Force Issue No. 06-10 (EITF 06-10), *Accounting for Collateral Assignment Split-Dollar Life Insurance Agreements*. EITF 06-10 provides guidance for determining a liability for the postretirement benefit obligation as well as recognition and measurement of the associated asset on the basis of the terms of the collateral assignment agreement. EITF 06-10 is effective for fiscal years beginning after December 15, 2007. The Company is currently evaluating the impact the adoption of the EITF will have on the Company s results of operations or financial condition.

In June 2007, the FASB ratified Emerging Issues Task Force Issue No. 06-11 (EITF 06-11), *Accounting for Income Tax Benefits of Dividends on Share-Based Payment Awards*. EITF 06-11 applies to share-based payment arrangements with dividend protection features that entitle employees to receive (a) dividends on equity-classified nonvested shares, (b) dividend equivalents on equity-classified nonvested share units, or (c) payments equal to the dividends paid on the underlying shares while an equity-classified share option is outstanding, when those dividends or dividend equivalents are charged to retained earnings under FAS No. 123R, *Share-Based Payment*, and result in an income tax deduction for the employer. A consensus was reached that a realized income tax benefit from dividends or dividend equivalents that are charged to retained earnings and are paid to employees for equity-classified nonvested equity shares, nonvested equity share units, and outstanding equity share options should be recognized as an increase in additional paid-in capital. EITF 06-11 is effective for fiscal years beginning after December 15, 2007, and interim periods within those fiscal years. The impact of the adoption of the EITF will not have an impact on the Company s financial condition.

Note 3. Per Share Data

The following table sets forth the composition of the weighted average common shares (denominator) used in the basic and dilutive per share computation. There are no convertible securities which would affect the numerator in calculating basic and diluted earnings per share; therefore, net income as presented on the consolidated statement of income will be used as the numerator.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	2006	2007	2006
Weighted average common shares outstanding	4,005,583	4,002,340	4,004,778	4,002,220
Average treasury stock shares	(124,095)	(75,079)	(115,468)	(59,687)
Weighted average common shares and common stock equivalents used to calculate basic earnings per share	3,881,488	3,927,261	3,889,310	3,942,533
Additional common stock equivalents(stock options) used to calculatediluted earnings per share	188	479	263	483
Weighted average common shares and common stock equivalents used to calculate diluted earnings per share	3,881,676	3,927,740	3,889,573	3,943,016

Options to purchase 8,276 and 9,002 shares of common stock at the price of $40.29 were outstanding during the three and nine months ended September 30, 2007 and 2006, respectively, but were not included in the computation of diluted earnings per share as they were anti-dilutive due to the strike price being greater than the market price as of September 30, 2007 and 2006, respectively.

Note 4. Net Periodic Benefit Cost-Defined Benefit Plans

For a detailed disclosure on the Company s pension and employee benefits plans, please refer to Note 11 of the Company s Consolidated Financial Statements included in the Annual Report on Form 10-K for the year ended December 31, 2006.

The following sets forth the components of the net periodic benefit cost of the domestic non-contributory defined benefit plan for the three and nine months ended September 30, 2007 and 2006, respectively:

10

(In Thousands)	Three Months Ended September 30, 2007	Three Months Ended September 30, 2006	Nine Months Ended September 30, 2007	Nine Months Ended September 30, 2006
Service cost	$ 117	$ 117	$ 350	$ 350
Interest cost	121	108	364	325
Expected return on plan assets	(140)	(121)	(421)	(364)
Amortization of transition	(1)	(1)	(2)	(2)
Amortization of prior service cost	6	6	19	19
Amortization of net loss		6		17
Net periodic cost	$ 103	$ 115	$ 310	$ 345

Employer Contributions

The Company previously disclosed in its consolidated financial statements, included in the Annual Report on Form 10-K for the year ended December 31, 2006, that it expected to contribute $500,000 to its defined benefit plan in 2007. As of September 30, 2007, a contribution in the amount of $580,000 was made for the 2006 plan year with no additional contributions anticipated.

Note 5. Off Balance Sheet Risk

The Company is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments are primarily comprised of commitments to extend credit and standby letters of credit. These instruments involve, to varying degrees, elements of credit, interest rate, or liquidity risk in excess of the amount recognized in the consolidated balance sheet. The contract amounts of these instruments express the extent of involvement the Company has in particular classes of financial instruments.

The Company s exposure to credit loss from nonperformance by the other party to the financial instruments for commitments to extend credit and standby letters of credit is represented by the contractual amount of these instruments. The Company uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments. The Company may require collateral or other security to support financial instruments with off-balance sheet credit risk.

Outstanding financial instruments with off balance sheet risk are as follows:

(In Thousands)	September 30, 2007	December 31, 2006
Commitments to extend credit	$ 71,588	$ 61,736
Standby letters of credit	1,345	1,033

Note 6. Reclassification of Comparative Amounts

Certain comparative amounts for the prior period have been reclassified to conform to current period presentations. Such reclassifications had no effect on net income or shareholders equity.

Note 7. Employee Stock Purchase Plan

Effective April 26, 2006, the Company implemented the Penns Woods Bancorp, Inc. 2006 Employee Stock Purchase Plan (Plan). The Plan is intended to encourage employee participation in the ownership and economic progress of the Company. The Plan allows for up to 1,000,000 shares to be purchased by employees. The purchase price of the shares is 95% of market value with an employee eligible to purchase up to the lesser of 15% of base compensation or $12,000 in market value annually. During the nine months ended September 30, 2007 and 2006, there were 2,240 and 421 shares issued under the plan, respectively.

CAUTIONARY STATEMENT FOR PURPOSES OF THE PRIVATE

SECURITIES LITIGATION REFORM ACT OF 1995

This Report contains certain forward-looking statements including statements concerning plans, objectives, future events or performance and assumptions and other statements which are other than statements of historical fact. The Company wishes to caution readers that the following important factors, among others, may have affected and could in the future affect the Company s actual results and could cause the Company s actual results for subsequent periods to differ materially from those expressed in any forward-looking statement made by or on behalf of the Company herein: (i) the effect of changes in laws and regulations, including federal and state banking laws and regulations, with which the Company must comply, and the associated costs of compliance with such laws and regulations either currently or in the future as applicable; (ii) the effect of changes in accounting policies and practices, as may be adopted by the regulatory agencies as well as by the Financial Accounting Standards Board, or of changes in the Company s organization, compensation and benefit plans; (iii) the effect on the Company s competitive position within its market area of the increasing consolidation within the banking and financial services industries, including the increased competition from larger regional and out-of-state banking organizations as well as non-bank providers of various financial services; (iv) the effect of changes in interest rates; and (v) the effect of changes in the business cycle and downturns in the local, regional or national economies.

Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operation

EARNINGS SUMMARY

Comparison of the Three and Nine Months Ended September 30, 2007 and 2006

Summary Results

Net income for the three months ended September 30, 2007 was $2,322,000 compared to $2,464,000 for the same period of 2006. Basic and diluted earnings per share for the three months ended September 30, 2007 were $0.60 as compared to $0.63 for the three months ended September 30, 2006. Return on average assets and return on average equity were 1.57% and 13.21% for the three months ended September 30, 2007 as compared to 1.71% and 13.41% for the corresponding period of 2006. Net income from core operations (operating earnings) for the three months ended September 30, 2007 and 2006, which excludes net after-tax securities gains of $370,000 for the 2006 period, increased $228,000 to $2,322,000 for the three months ended September 30, 2007 as compared to $2,094,000 for the same period of 2006. Operating earnings per share for the three months ended September 30, 2007 increased 13.2% or $0.07 to $0.60 basic and dilutive as compared to the three months ended September 30, 2006. Operating earnings per share for the three months ended September 30, 2007 represent a $0.05 basic and dilutive increase from the previous three month period as core earnings continued to build upon the $0.02 increase from the first to second quarters of 2007.

The nine months ended September 30, 2007 generated net income of $6,938,000 compared to $7,353,000 for the same period of 2006. Earnings per share, basic and diluted, for the nine months ended September 30, 2007 were $1.78 as compared to $1.87 for the comparable period of 2006. Return on average assets and return on average equity were 1.57% and 12.63% for the nine months ended September 30, 2007 as compared to 1.71% and 13.20% for the corresponding period of 2006. Operating earnings for the nine months ended September 30, 2007 and 2006, which excludes net after-tax securities gains of $409,000 and $914,000, respectively, increased $90,000 to $6,529,000 for the 2007 period compared to $6,439,000 for the 2006 period. Operating earnings per share, basic and dilutive, increased 3.1% to $1.68 for the nine months ended September 30, 2007 as compared to $1.63 for the comparable period of 2006.

(Management uses the non-GAAP measure of net income from core operations in its analysis of the Company s performance. This measure, as used by the Company, adjusts net income by significant gains or losses that are unusual in nature. Because certain of these items and their impact on the Company s performance are difficult to predict, management believes the presentation of financial measures excluding the impact of such items provides useful supplemental information in evaluating the operating results of the Company s core businesses. For purposes of this Quarterly Report on Form 10-Q, net income from core operations means net income adjusted to exclude after-tax net securities gains. These disclosures should not be viewed as a substitute for net income determined in accordance with GAAP, nor are they necessarily comparable to non-GAAP performance measures that may be presented by other companies.)

Interest Income

Interest income for the three months ended September 30, 2007 increased $430,000 to $8,977,000 as compared to $8,547,000 for the same period of 2006. The increase in interest income was primarily the result of growth in average loans of $5,736,000 coupled with an 18 basis point (bp) increase in loan portfolio yields for the three months ended September 30, 2007 over the same period of 2006. Over the same time frame, the average balance of investment securities and interest bearing deposits increased $5,693,000 with the portfolio yield increasing 28 bp resulting in a $164,000 increase in interest income. On a taxable equivalent basis, the interest income from the investment portfolio and interest bearing deposits increased $218,000 due to the investment portfolio being strategically shifted toward tax-exempt instruments. The decrease in dividends received is the result of a decrease in equity investments.

During the nine months ended September 30, 2007, interest income was $26,449,000, an increase of $1,533,000 over the same period in 2006. The reasons for the 6.2% growth in interest income for the nine month period are identical to those for the three month period ending September 30, 2007 discussed above. The growth in average loans of $11,727,000 coupled with a 26 bp increase in the loan portfolio yield resulted in an increase of $1,310,000 in loan interest and fee income. Average investment securities and interest bearing deposits remained stable, however, interest income increased $223,000 due to a 24 bp increase in yield. The increase in yield was due to an increase in yield on taxable securities as portfolio cash flow was reinvested into higher yielding bonds over the past year. The asset allocation between loans and the investment portfolio composition resulted in taxable equivalent interest income increasing $1,673,000 for the nine months ended September 30, 2007 as compared to the same period of 2006.

Interest income composition for the three and nine months ended September 30, 2007 and 2006 was as follows:

	For The Three Months Ended					
	September 30, 2007		September 30, 2006		Change	
(In Thousands)	Amount	% Total	Amount	% Total	Amount	%
Loans including fees	$ 6,621	73.8%	$ 6,355	74.4%	$ 266	4.2%
Investment securities:						
Taxable	964	10.7	874	10.2	90	10.3
Tax-exempt	1,108	12.3	1,004	11.7	104	10.4
Dividend and other interest income	284	3.2	314	3.7	(30)	(9.6)
Total interest income	$ 8,977	100.0%	$ 8,547	100.0%	$ 430	5.0%

	For The Nine Months Ended					
	September 30, 2007		September 30, 2006		Change	
(In Thousands)	Amount	% Total	Amount	% Total	Amount	%
Loans including fees	$ 19,560	74.0%	$ 18,250	73.3%	$ 1,310	7.2%
Investment securities:						
Taxable	2,711	10.2	2,691	10.8	20	0.7
Tax-exempt	3,271	12.4	2,993	12.0	278	9.3
Dividend and other interest income	907	3.4	982	3.9	(75)	(7.6)
Total interest income	$ 26,449	100.0%	$ 24,916	100.0%	$ 1,533	6.2%

Interest Expense

Interest expense for the three months ended September 30, 2007 increased $405,000 to $4,112,000 as compared to $3,707,000 for the same period of 2006. The increased expense associated with deposits is primarily the result of rate increases for time deposits, which are comprised of various certificates of deposit (CD) accounts, from the three months ended September 30, 2006 to the corresponding period of 2007. Factors that led to the rate increases include, but are not limited to, competitive market pricing pressure and campaigns conducted to attract 8 to 12 month maturity CDs that provide greater funding flexibility. The increase in CD interest rates has exceeded the increase for other deposit accounts. This has led to a shift of a portion of the money market and savings deposit portfolios into higher yielding CDs. Borrowing interest expense on FHLB advances and customer repurchase accounts increased $17,000 as rates paid increased 4 bp, while the average balance of borrowed funds remained constant.

Interest expense for the nine months ended September 30, 2007 increased $1,733,000 to $12,050,000 from $10,317,000 for the comparable period of 2006. Interest on deposits accounted for $1,963,000 of the increase due to the reasons noted in the above three month analysis. Borrowing costs declined primarily due to the previously noted CD campaigns that allowed for average FHLB advances to be reduced for the nine months ended September 30, 2007 as compared to the same period of 2006.

Interest expense composition for the three and nine months ended September 30, 2007 and 2006 was as follows:

	For The Three Months Ended					
	September 30, 2007		September 30, 2006		Change	
(In Thousands)	Amount	% Total	Amount	% Total	Amount	%
Deposits	$ 2,835	68.9%	$ 2,447	66.0%	$ 388	15.9%
Short-term borrowings	368	9.0	306	8.3	62	20.3
Long-term borrowings, FHLB	909	22.1	954	25.7	(45)	(4.7)
Total interest expense	$ 4,112	100.0%	$ 3,707	100.0%	$ 405	10.9%

	For The Nine Months Ended					
	September 30, 2007		September 30, 2006		Change	
(In Thousands)	Amount	% Total	Amount	% Total	Amount	%
Deposits	$ 8,215	68.2%	$ 6,252	60.6%	$ 1,963	31.4%
Short-term borrowings	1,100	9.1	1,221	11.8	(121)	(9.9)
Long-term borrowings, FHLB	2,735	22.7	2,844	27.6	(109)	(3.8)
Total interest expense	$ 12,050	100.0%	$ 10,317	100.0%	$ 1,733	16.8%

Net Interest Margin

The net interest margin (NIM) for the three months ended September 30, 2007 was 3.98% as compared to 4.00% for the corresponding period of 2006 and increased slightly from 3.95% for the three months ended June 30, 2007. The decrease in the NIM for the three months ended September 30, 2007 compared to the same period in 2006 was due to the cost of interest bearing liabilities continuing to increase at a rate greater than the increase in the yield on earning assets as has been the trend over the past twelve months. The negative impact of the disparity between the asset yield increases and the liability rate increases, however, declined for the three months ended September 30, 2007 as compared to the same period of 2006. Average loan growth of $5,736,000 and a shift in the investment portfolio toward tax-exempt bonds paved the way for the increase in yield on earning assets of 21 bp for the three month period ended September 2007 as compared to 2006. The average investment securities portfolio increased by $6,088,000, as the tax-exempt segment increased to $95,383,000 at September 30, 2007 as compared to $91,234,000 at September 30, 2006. The growth in tax-exempt bonds was part of the Company s tax strategy and was strategically undertaken to provide the cash flow and yield desired from the portfolio as a whole. The increase in the cost of interest bearing liabilities to 3.67% from 3.42% was driven primarily by the cost of time deposits increasing 48 bp for the three months ended September 30, 2007 as compared to the previous year, while the average balance of time deposits increased $17,503,000. The increase in cost of time deposits was impacted by the Federal Open Market Committee rate increases during 2006 of 100 bp, utilization of brokered deposits, and our strategic decision to gather time deposits as part of marketing campaigns associated with a branch opening and branch anniversaries in 2006 and 2007

The NIM for the nine months ended September 30, 2007 was 3.96% as compared to 4.06% for the corresponding period of 2006. The decrease in the NIM was the result of the previously mentioned growth and change in mix of the earnings assets offset by increased rates paid on interest bearing liabilities and growth in the average CD portfolio of $29,282,000.

Following is a schedule of average balances and associated yields for the three and nine month periods ended September 30, 2007 and 2006:

AVERAGE BALANCES AND INTEREST RATES

	Three Months Ended September 30, 2007			Three Months Ended September 30, 2006		
(In Thousands)	**Average Balance**	**Interest**	**Average Rate**	**Average Balance**	**Interest**	**Average Rate**
Assets:						
Tax-exempt loans	$ 7,652	$ 118	6.12%	$ 8,275	$ 127	6.09%
All other loans	354,032	6,543	7.33%	347,673	6,271	7.16%
Total loans	361,684	6,661	7.31%	355,948	6,398	7.13%
Taxable investment securities	91,788	1,247	5.43%	89,849	1,181	5.26%
Tax-exempt investment securities	95,383	1,679	7.04%	91,234	1,521	6.67%
Total securities	187,171	2,926	6.25%	181,083	2,702	5.97%
Interest bearing deposits	40	1	9.92%	435	7	6.38%
Total interest-earning assets	548,895	9,588	6.95%	537,466	9,107	6.74%
Other assets	43,706			42,042		
Total assets	$ 592,601			$ 579,508		
Liabilities:						
Savings	$ 60,262	114	0.75%	$ 63,081	142	0.89%
Super Now deposits	46,531	153	1.30%	47,071	170	1.43%
Money market deposits	23,183	131	2.24%	23,300	131	2.23%
Time deposits	203,690	2,437	4.75%	186,187	2,004	4.27%
Total deposits	333,666	2,835	3.37%	319,639	2,447	3.04%
Short-term borrowings	32,910	368	4.44%	27,255	306	4.45%
Long-term borrowings, FHLB	77,791	909	4.64%	82,878	954	4.57%
Total borrowings	110,701	1,277	4.58%	110,133	1,260	4.54%
Total interest-bearing liabilities	444,367	4,112	3.67%	429,772	3,707	3.42%
Demand deposits	70,689			69,660		
Other liabilities	7,249			6,596		
Shareholders equity	70,296			73,480		
Total liabilities and shareholders equity	$ 592,601			$ 579,508		
Interest rate spread			3.28%			3.32%
Net interest income/margin		$ 5,476	3.98%		$ 5,400	4.00%

1. Information on this table has been calculated using average daily balance sheets to obtain average balances.

2. Nonaccrual loans have been included with loans for the purpose of analyzing net interest earnings.

3. Income and rates on a fully taxable equivalent basis include an adjustment for the difference between annual income from tax-exempt obligations and the taxable equivalent of such income at the standard 34% tax rate.

AVERAGE BALANCES AND INTEREST RATES

(In Thousands)	Nine Months Ended September 30, 2007 Average Balance	Interest	Average Rate	Nine Months Ended September 30, 2006 Average Balance	Interest	Average Rate
Assets:						
Tax-exempt loans	$ 7,913	$ 365	6.17%	$ 8,155	$ 377	6.18%
All other loans	353,219	19,320	7.31%	341,250	18,001	7.05%
Total loans	361,132	19,685	7.29%	349,405	18,378	7.03%
Taxable securities	85,930	3,600	5.59%	93,848	3,664	5.21%
Tax-exempt securities	99,497	4,956	6.64%	90,972	4,535	6.65%
Total securities	185,427	8,556	6.15%	184,820	8,199	5.91%
Interest bearing deposits	431	18	5.58%	161	9	7.47%
Total interest-earning assets	546,990	28,259	6.90%	534,386	26,586	6.65%
Other assets	42,390			39,747		
Total assets	$ 589,380			$ 574,133		
Liabilities:						
Savings	$ 59,726	329	0.74%	$ 63,150	398	0.84%
Super Now deposits	46,309	455	1.31%	47,835	488	1.36%
Money market deposits	24,362	414	2.27%	24,190	367	2.03%
Time deposits	198,401	7,017	4.73%	169,119	4,999	3.95%
Total Deposits	328,798	8,215	3.34%	304,294	6,252	2.75%
Short-term borrowings	32,443	1,100	4.53%	37,761	1,221	4.32%
Other borrowings	78,818	2,735	4.64%	83,359	2,844	4.56%
Total borrowings	111,261	3,835	4.61%	121,120	4,065	4.49%
Total interest-bearing liabilities	440,059	12,050	3.66%	425,414	10,317	3.24%
Demand deposits	69,203			69,219		
Other liabilities	6,866			5,245		
Shareholders equity	73,252			74,255		
	$ 589,380			$ 574,133		
Interest rate spread			3.24%			3.41%
Net interest income/margin		$ 16,209	3.96%		$ 16,269	4.06%

1. Information on this table has been calculated using average daily balance sheets to obtain average balances.

2. Nonaccrual loans have been included with loans for the purpose of analyzing net interest earnings.

3. Income and rates on a fully taxable equivalent basis include an adjustment for the difference between annual income from tax-exempt obligations and the taxable equivalent of such income at the standard 34% tax rate.

The following table presents the adjustment to convert net interest income to net interest income on a fully taxable equivalent basis for the three and nine month periods ended September 30, 2007 and 2006.

(In Thousands)	For the Three Months Ended September 30, 2007	2006	For the Nine Months Ended September 30, 2007	2006
Total interest income	$ 8,977	$ 8,547	$ 26,449	$ 24,916
Total interest expense	4,112	3,707	12,050	10,317
Net interest income	4,865	4,840	14,399	14,599
Tax equivalent adjustment	611	560	1,810	1,670
Net interest income (fully taxable equivalent)	$ 5,476	$ 5,400	$ 16,209	$ 16,269

The following table sets forth the respective impact that both volume and rate changes have had on net interest income on a fully taxable equivalent basis for the three and nine month periods ended September 30, 2007 and 2006:

	Three Months Ended September 30, 2007 vs 2006 Increase (Decrease) Due to			Nine Months Ended September 30, 2007 vs 2006 Increase (Decrease) Due to		
(In Thousands)	Volume	Rate	Net	Volume	Rate	Net
Interest income:						
Loans, tax-exempt	$ (10)	$ 1	$ (9)	$ (11)	$ (1)	$ (12)
Loans	118	154	272	642	677	1,319
Taxable investment securities	25	41	66	(419)	355	(64)
Tax-exempt investment securities	71	87	158	425	(4)	421
Interest bearing deposits	(6)		(6			