

SECURITIES AND EXCHANGE COMMISSION

FORM 10-Q

Quarterly report pursuant to sections 13 or 15(d)

Filing Date: **1996-11-14** | Period of Report: **1996-09-30**  
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FILER

**USB HOLDING CO INC**

CIK: **707805** | IRS No.: **363197969** | State of Incorpor.: **DE** | Fiscal Year End: **1231**  
Type: **10-Q** | Act: **34** | File No.: **000-10950** | Film No.: **96663752**  
SIC: **6022** State commercial banks

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SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

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

For the Quarter Ended September 30, 1996 Commission File No. 010950

U.S.B. HOLDING CO., INC.

(Exact name of registrant as specified in its charter)

DELAWARE  
(State or other jurisdiction of  
incorporation or organization)

36-3197969  
(I.R.S. Employer  
Identification No.)

100 DUTCH HILL ROAD, ORANGETOWN, NEW YORK 10962  
(Address of principal executive office with zip code)

914-365-4600  
(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 and (2) has been subject to such filing requirements for the past 90 days.

YES  NO

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

CLASS	OUTSTANDING AT NOVEMBER 3, 1996
----	-----
Common stock, par value \$5 per share	3,085,609

U.S.B. HOLDING CO., INC.

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PART I - FINANCIAL INFORMATION

U.S.B. HOLDING CO., INC.  
CONSOLIDATED STATEMENTS OF CONDITION

	September 30, 1996 Unaudited	December 31, 1995
	-----	-----
	(000's, Except Share Data)	
<b>ASSETS</b>		
Cash and due from banks	\$ 22,872	\$ 23,469
Federal funds sold	13,800	13,800
	-----	-----
Cash and cash equivalents	36,672	37,269
Interest bearing deposits in other banks	99	2,069
Securities:		
Available for sale (at fair value)	173,471	170,889
Held to maturity (fair value \$83,474 in 1996 and \$62,684 in 1995)	81,936	60,266
Loans held for sale	60	394
Loans, net of allowance for loan losses of \$5,224 in 1996 and \$3,904 in 1995	486,220	387,043
Premises and equipment, net	10,446	10,088
Accrued interest receivable	6,169	5,288
Other real estate owned (OREO)	699	939
Other assets	6,952	4,538
	-----	-----
<b>TOTAL ASSETS</b>	<b>\$802,724</b>	<b>\$678,783</b>
	=====	=====
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>Liabilities:</b>		
Non-interest bearing deposits	\$ 96,038	\$ 82,363
Interest bearing deposits:		
Money Market	53,128	55,672
Savings	213,156	182,567
NOW	40,627	38,111
Time	301,643	251,922
	-----	-----
Total deposits	704,592	610,635
Accrued interest payable	1,815	1,769
Accrued expenses and other liabilities	2,219	5,046
Securities sold under agreements to repurchase	20,020	--
Federal Home Loan Bank advances	20,534	10,000
	-----	-----
Total liabilities	749,180	627,450
Commitments and contingencies (Note 9)		
<b>Stockholders' equity:</b>		
Preferred stock, no par value; authorized shares 100,000; outstanding shares: 32,500 in 1996 and 37,500 in 1995	3,250	3,750
Common stock, \$5 par value; 7,000,000 shares authorized and issued shares of 3,163,173 in 1996 and 2,880,397 in 1995	15,816	14,402
Additional paid-in capital	26,478	19,046
Retained earnings	10,361	14,072
Treasury stock at cost, 77,564 shares in 1996 and 86,316 shares in 1995	(966)	(1,075)
Unrealized (loss) gain on available for sale securities, net of tax	(1,395)	1,138
	-----	-----
Total stockholders' equity	53,544	51,333
	-----	-----
<b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>	<b>\$802,724</b>	<b>\$678,783</b>
	=====	=====

See notes to consolidated financial statements.

Three Months Ended  
September 30, 1996      September 30, 1995

	----- 1996	----- 1995
(000's, Except Share Data)		
INTEREST INCOME:		
Interest and fees on loans	\$ 10,497	\$ 8,480
Interest on federal funds sold	103	147
Interest and dividends on securities:		
Mortgage-backed securities	1,718	2,140
U.S. Treasury and Government	1,463	764
Obligations of states and political subdivisions	822	826
Corporate and other	100	306
Interest on deposits in other banks	1	38
Dividends on Federal Home Loan Bank stock	47	38
Total interest income	----- 14,751	----- 12,739
INTEREST EXPENSE:		
Interest on deposits	6,551	6,011
Interest on borrowings	554	247
Total interest expense	----- 7,105	----- 6,258
NET INTEREST INCOME	7,646	6,481
Provision for loan losses	600	275
Net interest income after provision for loan losses	----- 7,046	----- 6,206
NON-INTEREST INCOME:		
Gain on securities transactions - net	--	140
Gain on loans sold	10	--
Service charges and fees	593	653
Other income	251	247
Total non-interest income	----- 854	----- 1,040
NON-INTEREST EXPENSES:		
Salaries and employee benefits	2,610	2,271
Occupancy and equipment expense	837	851
Advertising and business development	273	219
Professional fees	260	217
Communications	145	143
Stationery and printing	92	95
FDIC insurance	1	(1)
Other expenses	351	342
Total non-interest expenses	----- 4,569	----- 4,137
Income before income taxes	3,331	3,109
Provision for income taxes	1,156	1,034
NET INCOME	----- \$ 2,175	----- \$ 2,075
NET INCOME PER COMMON AND COMMON EQUIVALENT SHARE	----- \$ .65	----- \$ .63
WEIGHTED AVERAGE COMMON AND COMMON EQUIVALENT SHARES OUTSTANDING	----- 3,248,247	----- 3,176,188

See notes to consolidated financial statements.

U.S.B. HOLDING CO., INC.  
CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)

Nine Months Ended  
September 30, 1996      September 30, 1995

	----- 1996	----- 1995
(000's, Except Share Data)		
INTEREST INCOME:		
Interest and fees on loans	\$ 29,424	\$ 24,327
Interest on federal funds sold	490	601
Interest and dividends on securities:		

Mortgage-backed securities	5,194	5,720
U.S. Treasury and Government	3,540	2,077
Obligations of states and political subdivisions	2,373	2,575
Corporate and other	470	922
Interest on deposits in other banks	37	104
Dividends on Federal Home Loan Bank stock	115	119
	-----	-----
Total interest income	41,643	36,445
	-----	-----
INTEREST EXPENSE:		
Interest on deposits	18,885	17,172
Interest on borrowings	1,031	707
	-----	-----
Total interest expense	19,916	17,879
	-----	-----
NET INTEREST INCOME	21,727	18,566
Provision for loan losses	1,675	700
	-----	-----
Net interest income after provision for loan losses	20,052	17,866
	-----	-----
NON-INTEREST INCOME:		
Gain on securities transactions - net	592	124
(Loss) gain on loans sold and held for sale	(68)	14
Service charges and fees	1,807	1,950
Other income	731	735
	-----	-----
Total non-interest income	3,062	2,823
	-----	-----
NON-INTEREST EXPENSES:		
Salaries and employee benefits	7,462	6,508
Occupancy and equipment expense	2,514	2,428
Advertising and business development	711	652
Professional fees	753	688
Communications	454	426
Stationery and printing	284	243
FDIC insurance	2	606
Other expenses	947	1,389
	-----	-----
Total non-interest expenses	13,127	12,940
	-----	-----
Income before income taxes	9,987	7,749
Provision for income taxes	3,437	2,474
	-----	-----
NET INCOME	\$ 6,550	\$ 5,275
	=====	=====
NET INCOME PER COMMON AND COMMON EQUIVALENT SHARE	\$ 1.95	\$ 1.61
	=====	=====
WEIGHTED AVERAGE COMMON AND COMMON EQUIVALENT SHARES OUTSTANDING	3,242,234	3,131,038
	=====	=====

See notes to consolidated financial statements.

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U.S.B. HOLDING CO., INC.  
CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

	Nine Months Ended	
	September 30, 1996	September 30, 1995
	-----	-----
	(000's)	
OPERATING ACTIVITIES:		
Net income	\$ 6,550	\$ 5,275
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	1,675	700
Depreciation and amortization	975	1,113
Amortization/accretion of premiums/discounts on securities - net	187	91
Gain on securities transactions - net	(592)	(124)
Loss (gain) on loans sold and held for sale - net	68	(14)
Origination of loans held for sale	(1,628)	(1,862)
Proceeds from loans sold	--	2,674
Increase in accrued interest receivable	(881)	(969)
Other - net	(2,666)	453
	-----	-----
Net cash provided by operating activities	3,688	7,337
	-----	-----
INVESTING ACTIVITIES:		

Proceeds from sales of securities available for sale	47,113	43,569
Proceeds from principal paydowns and maturities of securities available for sale	13,619	16,290
Proceeds from maturities of securities held to maturity	5,515	18,067
Purchases of securities available for sale	(67,104)	(97,044)
Purchases of securities held to maturity	(27,378)	(2,401)
Net decrease (increase) in interest bearing deposits in other banks	1,970	(883)
Loans originated, net of principal collections	(99,739)	(35,708)
Loans purchased	--	(372)
Purchases of premises and equipment - net	(1,316)	(1,091)
Purchases of Federal Home Loan Bank stock	(1,016)	--
Proceeds from sales of OREO	1,346	652
	-----	-----
Net cash used for investing activities	(126,990)	(58,921)
	-----	-----

FINANCING ACTIVITIES:

Net increase in non-interest bearing deposits, NOW, money market, and savings accounts	44,236	29,541
Increase in time deposits, net of withdrawals and maturities	49,721	28,672
Net decrease in federal funds purchased and Federal Home Loan advances - short-term	--	(7,400)
Proceeds from Federal Home Loan Bank advances - long-term	10,797	5,000
Repayment of Federal Home Loan Bank advances - long-term	(263)	--
Proceeds from securities sold under agreements to repurchase	20,020	--
Redemption of long-term debt qualifying as regulatory capital	--	(1,800)
Cash dividends paid	(1,571)	(1,141)
Redemption of preferred stock	(500)	--
Proceeds from issuance of common stock	15	1,610
Proceeds from issuance of treasury stock	250	--
	-----	-----
Net cash provided by financing activities	122,705	54,482
	-----	-----

-Continued-

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U.S.B. HOLDING CO., INC.  
CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED) (cont'd)

	Nine Months Ended	
	September 30, 1996	September 30, 1995
	-----	-----
	(000's)	
(Decrease) Increase in Cash and Cash Equivalents	(597)	2,898
Cash and Cash Equivalents, Beginning of Period	37,269	24,465
	-----	-----
Cash and Cash Equivalents, End of Period	\$ 36,672	\$ 27,363
	=====	=====
Supplemental Disclosures:		
Interest paid	\$ 19,870	\$ 17,150
	-----	-----
Income tax payments	\$ 5,755	\$ 2,465
	-----	-----
Transfer of assets to OREO	\$ 781	\$ 1,199
	-----	-----
Transfer of loans held for sale to loans held to maturity at lower of cost or fair value	\$ 1,962	\$ --
	-----	-----
Change in unrealized gain/loss on securities available for sale - net of tax	\$ (2,533)	\$ 2,654
	-----	-----

See notes to consolidated financial statements.

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U.S.B. HOLDING CO., INC.  
CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY (UNAUDITED)

<TABLE> <CAPTION>	Preferred Stock No Par Value	COMMON STOCK Shares Outstanding	COMMON STOCK \$5 Par Value	Additional Paid-In Capital	Retained Earnings	Treasury Stock	Unrealized Gain (Loss) on Available for Sale Securities
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
Balance at January 1, 1996	\$ 3,750	2,794,081	\$ 14,402	\$ 19,046	\$ 14,072	\$ (1,075)	\$ 1,138
Net income					6,550		
Cash dividends:							
Common (\$ .44 per share)					(1,345)		
Preferred					(226)		
Redemption of preferred stock	(500)						
Common stock issued:							
Incentive stock options exercised (\$8.46 - \$10.75 per share)		2,864	14	13			
10% stock dividend		279,912	1,400	7,278	(8,690)		
Issuance of treasury stock		8,752		141		109	
Change in unrealized gain (loss) on available for sale securities, net of tax	-----	-----	-----	-----	-----	-----	(2,533)
Balance at September 30, 1996	\$ 3,250 =====	3,085,609 =====	\$ 15,816 =====	\$ 26,478 =====	\$ 10,361 =====	\$ (966) =====	\$ (1,395) =====

</TABLE>

See notes to consolidated financial statements.

U.S.B. HOLDING CO., INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

1. Principles of Consolidation

The consolidated financial statements include the accounts of U.S.B. Holding Co., Inc. (the "Company"), Union State Bank (the "Bank"), the Company's non-bank subsidiary, Ad Con, Inc., and until December 31, 1995, its wholly-owned subsidiary, Royal Oak Savings Bank, F.S.B. ("Royal"). On December 31, 1995, Royal was sold to Monocacy Bancshares, Inc., parent company of Taneytown Bank & Trust Company, Taneytown, Maryland.

2. Reclassifications

Certain reclassifications have been made to prior year accounts to conform to the current year's presentation.

3. Basis of Presentation

In the opinion of Management, the accompanying unaudited consolidated financial statements include all adjustments (comprising only normal recurring accruals) necessary to present fairly the financial position of the Company as of September 30, 1996, the results of operations for the three and nine month periods ended September 30, 1996 and 1995, cash flows for the nine month periods then ended, and changes in stockholders' equity for the nine months ended September 30, 1996. A summary of the Company's significant accounting policies is set forth in Note 2 to the Consolidated Financial Statements included in the Company's 1995 Annual Report to Shareholders.

The consolidated financial statements have been prepared in accordance with generally accepted accounting principles and predominant practices used

within the banking industry. In preparing such financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the dates of the consolidated statements of condition and the revenues and expenses for the periods reported. Actual results could differ significantly from those estimates.

Estimates that are particularly susceptible to significant change relate to the determination of the allowance for loan losses and the valuation of other real estate acquired in connection with foreclosures or in satisfaction of loan receivables. In connection with the determination of the allowance for loan losses and other real estate owned, management obtains independent appraisals for significant properties, where applicable.

#### 4. Accounting for Stock-Based Compensation

In October 1995, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards ("SFAS") No. 123, "Accounting for Stock-Based Compensation." SFAS No. 123 establishes a fair value based method of accounting for stock-based compensation plans and encourages, but does not require, entities to adopt that method in place of the provisions of Accounting Principles Board Opinion ("APB") No. 25, "Accounting for Stock Issued to Employees," for all arrangements under which employees receive shares of stock or other equity instruments of the employer or the employer incurs

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U.S.B. HOLDING CO., INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (Cont'd)

#### 4. Accounting for Stock-Based Compensation (Cont'd)

liabilities to employees in amounts based on the price of the Company's stock. SFAS No. 123 requires significantly expanded disclosure in complete financial statements, including disclosure of pro forma net income and earnings per share as if the fair value based method were used to account for stock based compensation, if the intrinsic value method of APB No. 25 is retained. SFAS No. 123 also establishes fair value as the measurement basis for transactions in which an entity acquires goods or services from non-employees in exchange for equity instruments.

The accounting provisions of SFAS No. 123 are effective for transactions entered into after December 15, 1995. Effective January 1, 1996, the Company adopted SFAS No. 123 and has decided that it will continue to measure compensation cost for employee stock compensation plans in accordance with the provisions of APB No. 25.

#### 5. Accounting for Mortgage Servicing Rights

SFAS No. 122, "Accounting for Mortgage Servicing Rights," modifies the treatment of the capitalization of servicing rights by mortgage banking enterprises. The change eliminates the separate treatment of servicing rights acquired through loans originated and those acquired through purchase transactions, as previously required under SFAS No. 65, "Accounting for Certain Mortgage Banking Activities." SFAS No. 122 requires mortgage servicing rights acquired or originated subsequent to December 31, 1995, to be recorded as assets distinct from the loans to which they relate. SFAS No. 122 also requires periodic evaluation of capitalized servicing rights for deterioration of value, due to increases in prepayments and other factors. The Company's adoption of SFAS No. 122 as of January 1, 1996 has not had any effect on the Consolidated Financial Statements of the Company for the nine months ended September 30, 1996.

#### 6. Accounting for Impairment of a Loan

As of January 1, 1995, the Company adopted SFAS No. 114, "Accounting for Impairment of a Loan," as amended by SFAS No. 118, "Accounting by Creditors for Impairment of a Loan-Income Recognition and Disclosures," which requires recognition of an impairment of a loan within its scope when it is probable that either principal and/or interest are not collectible in accordance with the terms of the loan agreement. Measurement of the impairment is based on the present value of expected cash flows discounted at the loan's effective rate or, as a practical expedient, at the loan's observable market price or the fair value of the collateral if the loan is collateral-dependent. If the fair value of the impaired loan is less than the related recorded amount, a specific valuation allowance is established or the write-down is charged against the allowance for loan losses if the impairment is considered to be permanent. Small homogeneous loans such as residential mortgage, home equity, and installment loans are not separately reviewed for impaired status. Such loans are typically collateralized by

residential or other personal property and require monthly payments. Separate allocations of the allowance for loan losses are made based on payment trends and prior loss experience and the composition of credit risk inherent in

U.S.B. HOLDING CO., INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (Cont'd)

6. Accounting for Impairment of a Loan (Cont'd)

these loan types. The impact of adopting these Statements did not have a material effect on the Consolidated Financial Statements of the Company.

At September 30, 1996, the recorded investment in loans that are considered to be impaired under SFAS No. 114 approximated \$8.0 million. Impaired loans aggregating \$7.1 million were in nonaccrual status. Restructured loans in the amount of \$878,00 that are considered to be impaired due to a reduction in the contractual interest rate are on accrual status since the collateral securing the loan is sufficient to protect the contractual principal and interest of the restructured loans. These loans have been performing for a reasonable period of time. Interest accrued on these loans not yet collected as of September 30, 1996 approximated \$6,000.

A related allowance for loan losses determined in accordance with SFAS No. 114 is allocated to each impaired loan, as applicable. The total allowance for credit losses related to impaired loans was \$1,345,000 as of September 30, 1996. The average recorded investment in impaired loans for the three and nine month periods ended September 30, 1996 was approximately \$8.0 million and \$7.2 million, respectively. For the three and nine month periods ended September 30, 1996 and 1995, interest income recognized by the Company on impaired loans was not material.

7. Securities and Loans Held for Sale

The Company accounts for securities under SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities." Securities that may be sold as part of the Company's asset/liability or liquidity management, or in response to or in anticipation of changes in interest rates and resulting prepayment risk, or for other similar factors, are classified as available for sale and carried at fair value. Securities that the Company has the ability and positive intent to hold to maturity are classified as held to maturity and carried at amortized cost.

The decision to sell available for sale securities is based on management's assessment of changes in economic or financial market conditions, interest rate risk, and the Company's financial position and liquidity. Fair values for securities are based on quoted market prices, where available. If quoted market prices are not available, fair values are based on quoted market prices of comparable instruments.

The Company does not acquire securities for the purpose of engaging in trading activities.

In December 1995, the Company transferred, at fair value, securities having a fair value of \$68.8 million (amortized cost of \$68.1 million) from its held to maturity security portfolio to its portfolio of available for sale securities. This was done to enhance the Company's ability to respond to changes in interest rates. The securities transferred represented all of the readily marketable securities that were previously classified as held to maturity, except for obligations of states and political subdivisions. This transfer was made in accordance with the FASB's "A Guide to Implementation of Statement 115 on Accounting for Certain

U.S.B. HOLDING CO., INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (Cont'd)

7. Securities and Loans Held for Sale (Cont'd)

Investments in Debt and Equity Securities" issued in November 1995. Concurrent with the adoption of this guidance, corporations were permitted, through December 31, 1995, to reclassify their available for sale and held to maturity securities without calling into question the past intent of an entity to hold securities to maturity. The effect of this transfer, after tax, was a \$.4 million increase in shareholders' equity.

Realized gains and losses on the sales of all securities are reported in earnings. Unrealized gains and losses on available for sale securities are shown, net of taxes, as a separate component of stockholders' equity. At September 30, 1996, the effect of SFAS No. 115 resulted in a reduction of securities available for sale of \$2,417,000 which, after the applicable tax effect, resulted in a reduction to stockholders' equity of \$1,395,000, representing the unrealized loss. At December 31, 1995, the effect of SFAS No. 115 resulted in an increase of securities available for sale of \$1,971,000 which, after the applicable tax effect, resulted in an increase to stockholders' equity of \$1,138,000, representing the net unrealized gain.

A summary of the amortized cost and fair value of securities and related gross unrealized gains and losses at September 30, 1996 and December 31, 1995, follows:

<TABLE>  
<CAPTION>

(000's)				
September 30, 1996:	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
<S>	<C>	<C>	<C>	<C>
Available for Sale:				
U.S. Treasury and Government agencies	\$ 73,566	\$ --	\$ 1,100	\$ 72,466
Obligations of states and political subdivisions	3,066	26	--	3,092
Mortgage-backed securities	95,273	400	1,862	93,811
Corporate bonds	3,894	119	--	4,013
Other	89	--	--	89
-----				
Total available for sale securities	\$175,888	\$ 545	\$ 2,962	\$173,471
-----				
Held to Maturity:				
Obligations of states and political subdivisions	\$ 62,141	\$ 1,802	\$ 82	\$ 63,861
Mortgage-backed securities	9,797	--	156	9,641
U.S. Government agencies	9,998	--	26	9,972
-----				
Total securities held to maturity	\$ 81,936	\$ 1,802	\$ 264	\$ 83,474
=====				

</TABLE>

U.S.B. HOLDING CO., INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (Cont'd)

7. Securities and Loans Held for Sale (Cont'd)

<TABLE>  
<CAPTION>

(000's)				
December 31, 1995:	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
<S>	<C>	<C>	<C>	<C>
Available for Sale:				
U.S. Treasury and Government agencies	\$ 46,011	\$ 654	\$ 95	\$ 46,570
Obligations of states and political subdivisions	3,067	40	--	3,107
Mortgage-backed securities	109,375	1,169	181	110,363
Corporate bonds	10,406	384	--	10,790
Other	59	--	--	59
-----				
Total available for sale securities	\$168,918	\$ 2,247	\$ 276	\$170,889
-----				
Held to Maturity:				
Obligations of states and political subdivisions	\$ 60,266	\$ 2,456	\$ 38	\$ 62,684
-----				
Total securities held to maturity	\$ 60,266	\$ 2,456	\$ 38	\$ 62,684
=====				

</TABLE>

At September 30, 1996 and December 31, 1995, residential fixed rate real

estate loans held for sale had a cost of \$60,000 and \$394,000 and fair value of \$61,000 and \$393,000, respectively. There were no commitments of loans available for sale which had not yet closed at September 30, 1996. During the first quarter of 1996, the Bank transferred residential fixed rate real estate loans with an aggregate cost of \$2,824,000, which included commitments not yet closed of \$1,445,000, representing its entire held for sale portfolio at that time, to its held to maturity portfolio. This transfer resulted in a write-down of \$78,000, as the loans were transferred at the lower of cost or fair value.

During the third quarter of 1996, the Bank transferred additional residential fixed rate real estate loans with an aggregate cost of \$618,000 to its held to maturity portfolio, which did not result in a write down as the fair value exceeded the cost of the loans at the time of the transfer.

8. Borrowings, Stockholders' Equity and Net Income Per Common Share Data

At September 30, 1996, the Bank had outstanding term advances with the Federal Home Loan Bank of New York ("FHLB") in the amount of \$20,534,000 with maturities and interest rates as follows:

U.S.B. HOLDING CO., INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (Cont'd)

8. Borrowings, Stockholders' Equity and Net Income Per Common Share Data  
(Cont'd)

Date of Borrowing	Outstanding Advance Amount	Interest Rate	Maturity Date
November 14, 1994	\$5,000,000	5.70%	November 15, 1999
June 21, 1995	5,000,000	6.20	June 22, 1998
February 15, 1996	3,647,000	5.41	March 1, 2001
April 24, 1996	4,000,000	6.49	April 26, 1999
April 24, 1996	2,887,000	6.72	May 1, 2003

All of the advances are at fixed interest rates with the exception of the November 14, 1994 advance, which has an interest rate adjusting monthly to 20 basis points over the one month London Inter-Bank Offer Rate ("LIBOR"). In addition, each advance is subject to prepayment penalties except for the November 14, 1994 advance, which may be prepaid without penalty in whole or in part semiannually on May 14th and November 14th. The advances taken on February 15, 1996 and April 24, 1996 are fully amortizing.

The Bank has pledged under a blanket agreement to the FHLB, a security interest in the Bank's holdings of capital stock in the FHLB, certain mortgage loans, securities and other assets of the Bank for all FHLB outstanding advances.

As of September 30, 1996, the Bank is party to two repurchase agreements. These agreements represent funds borrowed in the amount of \$20.0 million on a short-term basis through the sale of securities to a counterparty under agreements to repurchase the same securities on October 28, 1996 (\$9.8 million) and December 23, 1996 (\$10.2 million). The transaction proceeds are recorded as "Securities sold under agreements to repurchase" and the underlying securities remain in the Bank's securities portfolio. The agreements are secured by U.S. Government agency and mortgage-backed securities with an amortized cost of \$20.5 million and fair value of \$20.3 million at September 30, 1996. Interest for the repurchase agreements adjusts monthly to the one month and three month LIBOR rates, which were 5.38 percent and 5.50 percent at September 30, 1996 for the repurchase agreements maturing on October 28, 1996 and December 23, 1996, respectively.

The dividend rate on the Company's Series "A" preferred stock issued to a single investor is determined quarterly and is subject to certain minimum and maximum per annum dividend rates as specified in the agreement. For the three and nine month periods ended September 30, 1996 and 1995, the weighted average dividend rates were 8.4 percent (the minimum rate) for each period. Net income per common share reflects the preferred stock dividends declared and accrued totaling \$71,000 and \$79,000 for each three month period and \$226,000 and \$236,000 for each nine month period ended September 30, 1996 and 1995, respectively. The Company redeemed \$250,000 of preferred stock on both May 15, 1996 and August 15, 1996.

In December 1993, the Company implemented a Dividend Reinvestment Plan ("DRIP"). The DRIP allows stockholders to invest cash dividends in shares of the Company's stock at fair value and, in the third quarter of 1994, a stock purchase feature was added to allow stockholders to purchase additional common stock at fair value up to \$2,500 per quarter.

U.S.B. HOLDING CO., INC.  
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (Cont'd)

8. Borrowings, Stockholders' Equity and Net Income Per Common Share Data  
 (Cont'd)

The DRIP was temporarily suspended for dividends paid after January 1, 1996. As of September 30, 1996, 200,000 shares of common stock are reserved for issuance in connection with the Plan, of which 98,020 shares have been issued.

On March 3, 1996, the Company issued 8,752 shares of its treasury stock. These shares were purchased by the Company's Employee Stock Ownership Plan (with Code Section 401(k) Provisions) ("KSOP") and Supplemental Employees' Investment Plan ("SEIP") at fair value.

The Company declared a 10 percent stock dividend on April 24, 1996 to shareholders of record May 31, 1996, which was distributed on June 14, 1996. In addition, the Company issued a 10 percent stock dividend to shareholders of record June 15, 1995, which was distributed on July 1, 1995. The weighted average shares outstanding and per share amounts have been adjusted to reflect the stock dividend distributed in 1996.

The Company and the Bank's ability to pay cash dividends in the future are restricted by various regulatory requirements. The Company's ability to pay cash dividends to its shareholders is primarily dependent upon the receipt of dividends from the Bank. The Bank's dividends to the Company may not exceed the sum of the Bank's net income for that year and its undistributed net income for the preceding two years, less any required transfers to additional paid-in capital. At September 30, 1996, the Bank could pay dividends to the Company of \$15.6 million without having to obtain prior regulatory approval.

Net income per common share is based on net income after preferred stock dividend requirements, the weighted average number of common shares outstanding and common equivalent shares (for the quarter and nine month periods ended September 30, 1995, adjusted for the common stock dividend distributed in 1996). Outstanding stock options granted that are dilutive and currently exercisable under the Company's stock option plans are considered to be common stock equivalents for earnings per share calculations.

In May, 1995, the Company repaid the \$1,800,000 of Series "A" subordinated notes outstanding that qualified as Tier II capital under risk-based capital guidelines. Interest on the notes was at prime plus one-half percent, payable quarterly. The weighted average interest rate was 9.39 percent for the period of January 1, 1995 through May 17, 1995 (the date the notes were prepaid).

9. Commitments and Contingencies

At September 30, 1996, the Bank was committed under an employment agreement with a key officer, director and shareholder requiring annual salary and other payments of \$400,000, increasing annually by \$30,000 during the term of the contract, annual stock option grants of 24,200 shares, issued at fair value (110 percent of fair value if the key officer's ownership of the Company equals or exceeds 10 percent at the date of grant) and other benefits for the term of the contract expiring July 1, 1999.

U.S.B. HOLDING CO., INC.  
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (Cont'd)

9. Commitments and Contingencies (Cont'd)

In the normal course of business, various commitments to extend credit are made which are not reflected in the accompanying Consolidated Financial Statements. At September 30, 1996, formal credit line and loan commitments which are primarily loans collateralized by real estate approximated \$102.8 million, and outstanding letters of credit totaled \$14.9 million. Such amounts represent the maximum risk of loss on these commitments.

During the nine month period ended September 30, 1995, the Bank sold in the secondary market for cash, mortgage loans with net proceeds totaling \$2.7 million. There were no such sales during the nine months ended September 30, 1996.

At September 30, 1996, the principal balance of the loans sold and exchanged with the Federal Home Loan Mortgage Corporation which remain uncollected approximated \$84.8 million. The Bank is committed to service these loans.

In the ordinary course of business, the Company is party to various legal proceedings, which in the opinion of management, will not have a material effect in the aggregate on the Company's consolidated financial position or results of operations.

In connection with its asset and liability management program, during 1994 the Bank entered into a protected rate agreement ("cap") which has an aggregate notional amount of \$3.5 million at September 30, 1996. The premium paid in the amount of \$85,000 was deferred and is being amortized over the five year life of the cap. Under the terms of the cap, the Bank will be reimbursed for increases in one month LIBOR for any month during the term of the agreement in which such rate exceeds the "strike level" of 8.1875 percent. Interest rate cap agreements allow the Bank to limit its exposure to unfavorable interest rate fluctuations over and above the "capped" rate. The purchased cap hedges income payments from a mortgage-backed security with an interest rate adjusted annually to the one year Treasury rate. This agreement is subject to the counterparty's ability to perform in accordance with the terms of the agreement. The Bank's risk of loss is equal to the original premium paid to enter into this agreement.

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U.S.B. HOLDING CO., INC.  
MANAGEMENT'S DISCUSSIONS AND ANALYSIS  
OF FINANCIAL CONDITION AND RESULTS OF OPERATION

FINANCIAL CONDITION

At September 30, 1996, the Company had total assets of \$802.7 million, an increase of 18.3 percent, or \$123.9 million from December 31, 1995. Total deposits increased \$94.0 million for the nine month period ended September 30, 1996, to \$704.6 million, which represented a 15.4 percent increase from December 31, 1995. Time deposits accounted for the greatest component of deposit increases, \$49.7 million. Time deposits greater than \$100,000 from local municipalities, which are obtained on a bidding basis with maturities of 30 to 180 days, increased by \$34.7 million as part of the Bank's overall leveraging strategy. IRAs/Keoghs increased by \$11.1 million due to promotions of this product during 1996. Other time deposits under \$100,000 increased by \$11.9 million due primarily to time deposit promotions associated with the opening of the Bank's seventeenth and eighteenth branches in Stony Point (January 1996) and Nanuet (September 1996), respectively, and relocation of the Bank's Orangeburg branch (September 1996). Retail time deposits over \$100,000 decreased by \$8.1 million during the nine month period ended September 30, 1996. Such deposits included a temporary deposit of approximately \$8.0 million which matured in July 1996. Savings deposits increased by \$30.6 million, as the Company introduced and promoted two new products, the "Golden Statement" account, which replaced the Liquid Gold account, and the Golden Passbook account, accounting for the majority of the increase in the savings deposit category. Both of these accounts provide attractive yields for high balance accounts. NOW accounts and demand deposits increased by \$2.5 million and \$13.7 million, respectively, while money market deposits decreased by \$2.5 million as customers generally switched money market account balances to higher yielding deposit products.

The securities portfolio of \$255.4 million and \$231.2 million at September 30, 1996 and December 31, 1995, respectively, consists of securities held to maturity at amortized cost of \$81.9 million and \$60.3 million, and securities available for sale at fair value totaling \$173.5 million and \$170.9 million, respectively.

Obligations of U.S. Treasury and other Government agencies increased \$35.9 million during the nine months ended September 30, 1996 due primarily to purchases of \$72.6 million, net of sales that occurred during the first quarter of \$32.0 million, maturities and securities called of \$3.0 million, and a decline in fair value of available for sale securities of \$1.7 million. The U.S. Treasuries were sold to take advantage of market conditions, while the U.S. Government agencies were sold because of the expectation that they would be called. Mortgage-backed securities decreased \$6.8 million as principal amortization and prepayments of \$8.6 million, sales of \$10.0 million, a decline in fair value of available for sale securities of \$2.5 million, offset purchases of \$14.3 million. The security transactions that took place for the nine months ended September 30, 1996, resulted in maintaining the overall earnings and the high quality nature of the portfolio. The Bank's investment in obligations of states and political subdivisions (municipal securities) increased by \$1.9 million during the first nine months of 1996, as the Bank purchased \$7.6 million of such securities during the second and third quarters, which offset maturities that occurred throughout the first nine months of the year. The Bank considers

such securities as core investments which are high yielding on a tax equivalent basis and have diversified final maturities. Purchases of municipal securities are dependent upon their availability in the marketplace and the yield of such securities on a tax equivalent basis,

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U.S.B. HOLDING CO., INC.  
MANAGEMENT'S DISCUSSIONS AND ANALYSIS  
OF FINANCIAL CONDITION AND RESULTS OF OPERATION (Cont'd)

FINANCIAL CONDITION (Cont'd)

compared to other securities of equivalent credit risk and maturity. The Bank also maintains investments in medium-term corporate debt securities and other securities which are rated investment grade by nationally recognized rating organizations. For the nine months ended September 30, 1996, such securities decreased by \$6.8 million, principally due to sales of \$4.5 million and maturities of such securities during the period.

The Company continues to exercise its conservative approach to investing by making high quality investments and controlling interest rate risk by averaging investments in medium-term maturities.

At September 30, 1996, net loans were \$486.3 million, a net increase of \$98.8 million or 25.5 percent over December 31, 1995 due to net increases in all major loan categories, principally commercial and construction mortgages. Outstanding loan balances increased \$49.0 million in commercial mortgages, \$33.1 million in construction and real estate secured loans, \$12.1 million in residential mortgages and \$5.2 million in credit card balances outstanding. During the third quarter 1996, the Bank purchased a credit card portfolio with outstanding balances of \$1.8 million to increase its volume of business and market share. The Bank had approximately \$102.8 million in formal credit lines and loan commitments outstanding. Management considers its liquid resources to be adequate to fund future loans in the foreseeable future, principally by utilizing excess funds temporarily placed in federal funds sold, increases in deposits, Federal Home Loan Bank advances and securities sold under agreements to repurchase, and loan repayments and maturing securities.

The Bank has approximately \$3.3 million of loans, collateralized by lease receivables, to Bennett Funding Group, a lease finance company, which filed for bankruptcy protection during the first quarter of 1996. Collection of the Bank's loan continues to be delayed by the bankruptcy proceedings. The Bank has not yet determined the extent of losses, if any, that will be sustained on these loans. However, based upon Bennett's filing, the loans have been placed on nonaccrual status. Including the Bennett loans, the Bank's nonaccrual loans were less than one percent of total assets at September 30, 1996.

The Bank's allowance for loan losses increased \$1.3 million or 33.8 percent to \$5.2 million at September 30, 1996, from \$3.9 million at December 31, 1995. The allowance for loan losses represented 1.06 percent of gross loans outstanding at September 30, 1996, compared to one percent at December 31, 1995. The allowance reflects a provision of \$1,675,000 and net charge-offs of \$355,000 recorded thus far in 1996. Management takes a prudent and cautious position in evaluating various business and economic uncertainties in relation to the Bank's loan portfolio. In management's judgment, the allowance is considered adequate to absorb potential losses inherent in the loan portfolio.

During the nine months ended September 30, 1996, the Bank increased the amount of outstanding advances with the Federal Home Loan Bank of New York by \$10.5 million. In addition, in the second and third quarters, the Bank entered into repurchase agreements aggregating of \$20.0 million. These agreements represent funds borrowed on a short-term basis

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U.S.B. HOLDING CO., INC.  
MANAGEMENT'S DISCUSSIONS AND ANALYSIS  
OF FINANCIAL CONDITION AND RESULTS OF OPERATION (Cont'd)

FINANCIAL CONDITION (Cont'd)

through the sale of securities to a counterparty under an agreement to repurchase the same securities on October 28, 1996 (\$9.8 million) and December 23, 1996 (\$10.2 million). These transactions took place as part of the Bank's overall leveraging strategy.

Stockholders' equity increased to \$53.5 million at September 30, 1996, an increase of \$2.2 million from the December 31, 1995 balance of \$51.3 million.

The increase partially results from net income of \$6.6 million for the nine month period ended September 30, 1996, which was offset by cash dividends on preferred stock of \$226,000 and common stock of \$1,345,000. During the first quarter, the Company also issued 8,752 shares of treasury stock at fair market value in the aggregate amount of \$250,000. Due to market conditions that have occurred thus far this year, the effect of SFAS No. 115 for the nine month period ended September 30, 1996, was to decrease stockholders' equity, net of tax effect, by \$2,533,000.

The Company's leverage ratio at September 30, 1996 was 7.04 percent, compared to 7.43 percent at December 31, 1995, well above the "well-capitalized" level of 5 percent. The Company's Tier I and total capital ratios under the risk-based capital guidelines were 10.13 percent and 11.10 percent at September 30, 1996 and 11.37 percent and 12.26 percent at December 31, 1995, respectively, which remained above the "well-capitalized" levels of 6 percent (Tier I) and 10 percent (Total Capital).

## RESULTS OF OPERATIONS

### Earnings

Net income for the three and nine month periods ended September 30, 1996, increased \$100,000 or 4.8 percent to \$2.2 million and \$1,275,000 or 24.2 percent to \$6.6 million, compared to the same periods in 1995, respectively. Net income per common and common equivalent share increased to \$.65 per common share and \$1.95 per common share in the quarter and nine months ended September 30, 1996 from \$.63 per common share and \$1.61 per common share recorded in the same periods in 1995. The annualized return on average total assets increased to 1.19 percent for the nine months ended September 30, 1996 from 1.10 percent for the nine months ended September 30, 1995. The overall increase in earnings for both periods reflect higher net interest income resulting from increased volumes and effective leveraging of the balance sheet, offset by a higher loan loss provision, lower service fee income, and higher non-interest expenses to support increased business, while the nine months ended September 30, 1996 was also favorably impacted by a significant reduction in FDIC insurance. The nine month period ended September 30, 1996 is also favorably impacted by higher gains on sales of available for sale securities, while the third quarter of 1995 compared to the third quarter 1996 was also favorably impacted by security gains. A discussion of the factors impacting the changes in the various components of net income follows.

### Net Interest Income

Net interest income, the difference between interest income and interest expense, is a significant

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U.S.B. HOLDING CO., INC.  
MANAGEMENT'S DISCUSSIONS AND ANALYSIS  
OF FINANCIAL CONDITION AND RESULTS OF OPERATION (Cont'd)

### Net Interest Income (Cont'd)

component of the Company's consolidated earnings. For the three month period ended September 30, 1996, net interest income increased 18.0 percent to \$7.6 million from \$6.5 million in the year earlier period. Net interest income increased \$3.2 million or 17.0 percent to \$21.7 million for the nine months ended September 30, 1996, compared to the nine month period ended September 30, 1995. Net interest income increased in both the three and nine month periods ended September 30, 1996, due to volume increases of average earning assets, partially offset by a decrease in the net interest spread. For the three and nine months ended September 30, 1996, the interest spread (yield on earning assets less cost of funds) was 4.11 percent and 4.10 percent, respectively, compared to 4.26 percent and 4.15 percent for the year earlier periods. Yields on interest earning assets decreased during the three and nine month periods ended September 30, 1996, while the cost of funds decreased slightly for both the three and nine months ended September 30, 1996, compared to the same periods in 1995. The cost of funds decreased at a lesser rate compared to the decrease in yield on earning assets, resulting in the negative impact on the net interest spread. The decreases in asset and liability yields were partially as a result of a prime rate and Federal Reserve discount rate decrease which occurred in the first quarter of 1996. The decreases in cost of funds were somewhat offset by higher yielding time deposits due to branch opening promotions and an IRA/Keogh promotion during 1996. In addition, new savings products, "Golden Statement Account" and "Golden Passbook," were introduced during the first and third quarters of 1996, respectively. The new products, which have tiered rates, pay an interest rate which is administratively set of up to 5.00 percent and 5.04 percent for the highest tiers for Golden Statement (\$100,000) and Golden Passbook (\$50,000), respectively. These products are similar to the Liquid Gold product which was discontinued for new deposits in the fourth quarter of 1995. Liquid Gold also pays a tiered rate which is set at the Federal Reserve discount

rate (currently 5 percent) for balances of \$25,000 or more. Increased borrowings to fund growth and effect leverage strategies also resulted in a higher cost of funds, but has the effect of increasing net interest income, while managing interest rate risk.

#### Provision for Loan Losses

The provision for loan losses increased \$325,000 to \$600,000 for the three month period ended September 30, 1996, compared to the same period in 1995 and \$975,000 to \$1,675,000 for the nine months ended September 30, 1996 compared to the year earlier period. Net charge-offs in the first nine months of 1996 totaled \$355,000 relating primarily to real estate loans, compared to \$663,000 of net charge-offs (principally real estate and commercial loans) during the same period in 1995. Nonaccrual loans were \$7.6 million at September 30, 1996, compared to \$4.0 million at December 31, 1995, and \$6.1 million at September 30, 1995. The Bank has approximately \$3.3 million of loans, collateralized by lease receivables, to Bennett Funding Group, a lease finance company, which filed for bankruptcy during the first quarter of 1996. The Bank does not yet know the extent of losses, if any, that will be sustained on these loans. However, based upon Bennett's filing, the loans were placed on nonaccrual status in March 1996. It is the Company's policy to discontinue the accrual of interest on loans when, in the opinion of management, a reasonable doubt exists as to the timely collectibility of the amounts due. Net income is adversely impacted by the level of non-performing assets of the Bank since, in addition to foregone revenue, it must increase the level of provision for loan losses, and incur other costs associated with collections of past due balances.

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#### U.S.B. HOLDING CO., INC. MANAGEMENT'S DISCUSSIONS AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATION (Cont'd)

##### Provision for Loan Losses (Cont'd)

An evaluation of the quality of the loan portfolio is performed by management on an ongoing basis as an integral part of the loan function, which includes the identification of past due loans, the recognition of the current economic environment and the review of the historical loan experience. Management has taken a prudent and cautious position in evaluating various business and economic uncertainties in relation to the Company's loan portfolio and believes that the allowance for loan losses at September 30, 1996 reflects the risk elements inherent in the total loan portfolio at this time. The changes in the provision charged to income and the allowance for loan losses reflects such uncertainties on an ever increasing loan portfolio. There is no assurance that the Company will not be required to make future adjustments to the allowance in response to changing economic conditions or regulatory examinations.

##### Non-Interest Income

Non-interest income for the three months ended September 30, 1996 decreased to \$854,000 from \$1,040,000 in the same period of 1995. For the nine months ended September 30, 1996, non-interest income was \$3,062,000, which represented a 8.5 percent increase, or \$239,000, over the same period in 1995. The third quarter decrease is related to higher gains on securities transactions (\$140,000) in the three month period ended September 1995, and lower service charges and fees (\$60,000). The increase in non-interest income for the nine months ended September 30, 1996, compared to 1995, resulted from an increase in the gains on securities transactions (\$468,000), which offset decreases in gains/losses on loans held for sale (\$82,000), and service charges income (\$143,000). The relationship of non-interest income to non-interest expenses was 18.7 percent and 23.3 percent for the three and nine months periods ended September 30, 1996 compared to 25.1 percent and 21.8 percent for the three and nine month periods ended September 30, 1995, respectively.

The net gain on securities transactions of \$592,000 for the nine month period ended September 30, 1996, was a result of activity that occurred in the securities portfolio, while maintaining the overall yield and quality of the portfolio. During the first half of 1996, the Bank sold approximately \$46.5 million of securities, principally callable U.S. Government agencies (\$12.0 million), U.S. Treasuries (\$20.0 million), mortgage-backed securities (\$10.0 million), and corporate bonds (\$4.5 million). The U.S. Government agencies were sold because of the expectation that they would be called this year, while the remaining securities were sold to take advantage of market conditions. The net gain on securities transactions of \$124,000 for the nine months ended September 30, 1995, was a result of sales of mortgage-backed securities during the third quarter to increase yield and shorten maturity, and of callable U.S. Government agencies which likely would have been called during the remainder of 1995 and January, 1996.

The net loss of \$68,000 during the nine months ended September 30, 1996 for loans held for sale principally resulted from the write-down of loans (\$78,000)

previously held for sale which were transferred to the held to maturity portfolio. These loans were transferred at the lower of cost or fair value. The net gain on loans held for sale in the first nine months of 1995 of \$14,000 was principally due to the sale of \$2.7 million of fixed rate residential mortgages.

U.S.B. HOLDING CO., INC.  
MANAGEMENT'S DISCUSSIONS AND ANALYSIS  
OF FINANCIAL CONDITION AND RESULTS OF OPERATION (Cont'd)

Non-Interest Income (Cont'd)

Service charges decreased \$60,000 and \$143,000 in the three and nine month periods ended September 30, 1996, respectively, compared to the prior year. Although there were more deposit accounts in 1996 compared to 1995, lower insufficient funds charges and increased competition impacted the level of fees charged.

Other income, which consists of credit card fees, loan servicing income, wire transfer fees, safe deposit, and other fees, remained relatively flat for each period, as growth in credit card revenue was offset by lower fees in other categories.

Non-Interest Expenses

Non-interest expenses increased \$432,000 to \$4,569,000 and \$187,000 to \$13,127,000 for the three and nine month periods ended September 30, 1996, respectively, from the comparable periods in 1995. The primary reasons for these increases result from an increase in salaries and other operating costs to support growth offset by an employee settlement and higher branch charge-offs in the nine month period ended September 30, 1995 and lower FDIC Insurance premium for the nine months ended September 30, 1996. The following discusses each component of non-interest expense.

Salaries and benefits are the largest component of non-interest expense. Increases of \$339,000 and \$954,000 occurred during the three and nine month periods ended September 30, 1996, respectively, compared to the previous year, which represented increases of 14.9 percent and 14.7 percent, respectively. Full-time equivalent employees of 221 at September 30, 1996 represented an increase from 207 full-time equivalent employees at September 30, 1995. The salary increases occurred due to additional personnel necessary for the Bank to accommodate the increases in both deposits and loans and their related services, the opening of two new branches in 1996, and annual merit increases. These increases were partially offset by the decrease in Royal personnel as Royal was sold on December 31, 1995.

These changes also occurred because of an increase in incentive compensation programs which are based upon the Company's net income and overall financial performance, higher payroll taxes during 1996 due to the higher salary base and increases in other employee benefit programs such as medical coverage, tuition reimbursement, and training.

The changes in the other components of non-interest expenses for the three and nine month periods ended September 30, 1996 compared to September 30, 1995, were due to the following:

- o Decrease of \$14,000 (1.6%) and an increase of \$86,000 (3.5%), respectively, in occupancy and equipment expense were due principally to maintenance expenses associated with the severe winter of 1996, an increase in maintenance contracts relating to the Bank's branch and computer related equipment, and additional rental expense associated with new branch openings in 1996 offset by a decrease in expenses due to the sale of Royal on December 31, 1995.

U.S.B. HOLDING CO., INC.  
MANAGEMENT'S DISCUSSIONS AND ANALYSIS  
OF FINANCIAL CONDITION AND RESULTS OF OPERATION (Cont'd)

Non-Interest Expenses (Cont'd)

- o Increases of \$54,000 (24.7%) and \$59,000 (9.0%), respectively, in advertising and business development. The increases reflect advertising and promotion of new deposit products and new branches and increased business development activities.
- o Increases of \$43,000 (19.8%) and \$65,000 (9.5%), respectively, in

professional fees. The increases relate to examination fees for the New York State Department of Banking examination which took place during the second quarter of 1996 and professional fees associated with loan collections, foreclosures and other litigation.

- o Increases of \$2,000 (1.4%) and \$28,000 (6.6%), respectively, in communications were due to an increase in postage and telephone expenses that arose as a result of higher postal volume, the new branch additions, transfer of credit card operations from Maryland to New York, and upgrading of data lines throughout the Bank.
- o Decrease of \$3,000 (3.2%) and increase of \$41,000 (16.9%), respectively, in stationery and printing. The overall increase occurred due to increased loan and deposit volume, and growth of the credit card operation which offset the decrease caused by the sale of Royal.
- o Increase of \$2,000 and decrease of \$604,000 (100%), respectively, in FDIC insurance premiums as the Bank Insurance Fund reached its required level of 1.25 percent of insured deposits in 1995, resulting in a refund of the third quarter premium in 1995, and a decrease in the annual FDIC premium for the Bank to \$2,000 annually.
- o Increases of \$9,000 (2.6%) and decreases of \$442,000 (31.8%) in other expenses. The decrease was due to higher 1995 second quarter expenses resulting from a settlement with a former executive officer of the Company and higher branch charge-offs. In addition, there has been a reduction in 1996 foreclosure related expenses compared to the 1995 periods, lower amortization of intangible assets due to intangible assets becoming fully amortized in 1995, offset by an increase in credit card expenses in 1996 due to the growth of this program.

#### Income Taxes

The effective tax rates for the three month periods ended September 30, 1996 and 1995 were 34.7 percent and 33.3 percent, respectively, while the effective tax rates for the nine month periods ended September 30, 1996 and 1995 were 34.4 percent and 31.9 percent, respectively. The increase in the overall effective tax rate in 1996 reflects a lower percent of non-taxable security income due to maturities of these securities, while total assets have increased significantly during 1996. The purchases of tax-exempt securities are dependent upon their availability in the marketplace and the yield of such securities on a tax equivalent basis, compared to other securities of equivalent credit risks and maturity.

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#### PART II - OTHER INFORMATION

##### Item 6. Exhibits and Reports on Form 8-K

- (a) Exhibit XI - Statement re: Computation of Earnings Per Share
- (b) Reports on Form 8-K. None were filed during the quarter ended September 30, 1996.

#### SIGNATURES

Pursuant to the requirements of the Securities and Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized, on November 13, 1996.

U.S.B. HOLDING CO., INC.

/s/ Thomas E. Hales  
-----  
Thomas E. Hales  
Chairman of the Board, President  
Chief Executive Officer and Director

/s/ Steven T. Sabatini  
-----  
Steven T. Sabatini  
Executive Vice President Finance,  
Chief Financial Officer and  
Assistant Secretary  
(Principal Financial and  
Accounting Officer)

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EXHIBIT XI  
U.S.B. HOLDING CO., INC.  
COMPUTATION OF EARNINGS PER SHARE

FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 1996

	Three Months Ended September	Nine Months Ended September 30, 1996
-----		
(000's, Except Share Data)		
Weighted average number of common shares outstanding	3,084,521	3,081,484
Assuming exercise of options reduced by the number of shares which could have been purchased with the proceeds from exercise of such options	163,766	160,750
	-----	-----
Weighted average common and common equivalent shares	3,248,287	3,242,234
	-----	-----
Net income	\$ 2,175	\$ 6,550
Less: Preferred stock dividend requirements	71	226
	-----	-----
Net income available to common shareholders	\$ 2,104	\$ 6,324
	=====	=====
Net income per common and common equivalent share	\$ 0.65	\$ 1.95
	=====	=====

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