

EVANS BANCORP INC
Form 10-Q
November 07, 2006

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**UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q**

(Mark One)

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

For quarterly period ended **September 30, 2006**

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

For the transition period from _____ to _____

Commission file number 0-18539

EVANS BANCORP, INC.

(Exact name of registrant as specified in its charter)

New York

16-1332767

(State of other jurisdiction of incorporation or organization)

(I.R.S. Employer Identification No.)

14 -16 North Main Street, Angola, New York 14006

(Address of principal executive offices) (Zip Code)

(716) 926-2000

(Registrant's telephone number, including area code)

Not applicable

(Former name, former address and former fiscal year, if changed since last report)

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

Indicate by check mark whether the registrant 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 Accelerated filer Non-accelerated filer

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

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

Common Stock, \$.50 par value 2,730,483 shares as of October 31, 2006

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EVANS BANCORP, INC. AND SUBSIDIARIES

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PART I FINANCIAL INFORMATION
 ITEM I FINANCIAL STATEMENTS
 EVANS BANCORP, INC. AND SUBSIDIARIES
 UNAUDITED CONSOLIDATED BALANCE SHEETS
 SEPTEMBER 30, 2006 AND DECEMBER 31, 2005
 (in thousands, except share and per share amounts)

| | September 30, 2006 | December 31, 2005 |
|-----------------------------------------------------------------------------------------------------|--------------------------|-------------------------|
| ASSETS | | |
| Cash and cash equivalents: | | |
| Cash and due from banks | \$ 11,740 | \$ 15,635 |
| Securities: | | |
| Available for sale, at fair value | 136,533 | 155,610 |
| Held to maturity, at amortized cost | 4,294 | 4,342 |
| Loans and leases, net of allowance for loan and lease losses of \$3,680 in 2006 and \$3,211 in 2005 | 275,271 | 256,810 |
| Properties and equipment, net | 8,119 | 8,151 |
| Goodwill | 9,639 | 9,639 |
| Intangible assets | 2,566 | 2,728 |
| Bank-owned life insurance | 9,952 | 9,586 |
| Other assets | 7,340 | 6,045 |
| TOTAL ASSETS | \$ 465,454 | \$ 468,546 |
| LIABILITIES AND STOCKHOLDERS EQUITY | | |
| LIABILITIES | | |
| Deposits: | | |
| Demand | \$ 70,073 | \$ 71,183 |
| NOW | 11,542 | 12,401 |
| Regular savings | 90,085 | 86,558 |
| Muni-vest | 35,362 | 27,521 |
| Time | 152,105 | 139,145 |
| Total deposits | 359,167 | 336,808 |
| Federal funds purchased and agreements to repurchase securities | 9,352 | 8,985 |
| Other short-term borrowings | 14,207 | 34,585 |
| Other liabilities | 7,997 | 6,629 |

| | | |
|--------------------------------|---------|---------|
| Junior subordinated debentures | 11,330 | 11,330 |
| Long-term borrowings | 24,674 | 33,333 |
| | | |
| Total liabilities | 426,727 | 431,670 |

CONTINGENT LIABILITIES AND COMMITMENTS

STOCKHOLDERS EQUITY:

| | | |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------|---------|
| Common stock, \$.50 par value; 10,000,000 shares authorized; 2,745,338 and 2,745,338 shares issued, respectively, and 2,722,401 and 2,729,779 shares outstanding, respectively | 1,373 | 1,373 |
| Capital surplus | 26,179 | 26,155 |
| Retained earnings | 12,991 | 11,087 |
| Accumulated other comprehensive loss, net of tax | (1,323) | (1,387) |
| Less: Treasury stock, at cost (22,937 and 15,559 shares, respectively) | (493) | (352) |
| | | |
| Total stockholders equity | 38,727 | 36,876 |

| | | |
|--------------------------------------------------|-------------------|-------------------|
| TOTAL LIABILITIES AND STOCKHOLDERS EQUITY | \$ 465,454 | \$ 468,546 |
|--------------------------------------------------|-------------------|-------------------|

See Notes to Unaudited Consolidated Financial Statements

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PART I FINANCIAL INFORMATION
 ITEM I FINANCIAL STATEMENTS
 EVANS BANCORP, INC. AND SUBSIDIARIES
 UNAUDITED CONSOLIDATED STATEMENTS OF INCOME
 THREE MONTHS ENDED SEPTEMBER 30, 2006 AND 2005
 (in thousands, except share and per share amounts)

| | Three Months Ended September 30, | |
|----------------------------------------------------------------------|-------------------------------------|--------------|
| | 2006 | 2005 |
| INTEREST INCOME | | |
| Loans | \$ 5,242 | \$ 4,307 |
| Federal funds sold/Interest bearing deposits at other banks | 5 | 13 |
| Securities: | | |
| Taxable | 1,030 | 1,154 |
| Non-taxable | 470 | 478 |
| Total interest income | 6,747 | 5,952 |
| INTEREST EXPENSE | | |
| Deposits | 2,408 | 1,653 |
| Other borrowings | 469 | 368 |
| Junior subordinated debentures | 223 | 173 |
| Total interest expense | 3,100 | 2,194 |
| NET INTEREST INCOME | 3,647 | 3,758 |
| PROVISION FOR LOAN AND LEASE LOSSES | 305 | 215 |
| NET INTEREST INCOME AFTER PROVISION FOR LOAN AND LEASE LOSSES | 3,342 | 3,543 |
| NON-INTEREST INCOME: | | |
| Bank charges | 533 | 558 |
| Insurance service and fees | 1,460 | 1,508 |
| Net gain on sales of securities | 114 | 2 |
| Premium on loans sold | 2 | 4 |
| Bank-owned life insurance | 132 | 96 |
| Life insurance proceeds | | 15 |
| Other | 486 | 322 |
| Total non-interest income | 2,727 | 2,505 |
| NON-INTEREST EXPENSE: | | |
| Salaries and employee benefits | 2,403 | 2,296 |
| Occupancy | 496 | 497 |
| Supplies | 48 | 73 |
| Repairs and maintenance | 140 | 136 |
| Advertising and public relations | 82 | 105 |
| Professional services | 207 | 237 |
| Amortization of intangibles | 141 | 132 |

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| | | |
|-------------------------------------------|-----------|-----------|
| Other Insurance | 79 | 86 |
| Other | 720 | 732 |
| Total non-interest expense | 4,316 | 4,294 |
| INCOME BEFORE INCOME TAXES | 1,753 | 1,754 |
| INCOME TAXES | 471 | 498 |
| NET INCOME | \$ 1,282 | \$ 1,256 |
| Net income per common share-basic | \$ 0.47 | \$ 0.46 |
| Net income per common share-diluted | \$ 0.47 | \$ 0.46 |
| Cash dividends per common share | \$ 0.34 | \$ 0.34 |
| Weighted average number of common shares | 2,724,940 | 2,721,633 |
| Weighted average number of diluted shares | 2,727,307 | 2,724,272 |

See Notes to Unaudited Consolidated Financial Statements

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PART I FINANCIAL INFORMATION
 ITEM I FINANCIAL STATEMENTS
 EVANS BANCORP, INC. AND SUBSIDIARIES
 UNAUDITED CONSOLIDATED STATEMENTS OF INCOME
 NINE MONTHS ENDED SEPTEMBER 30, 2006 AND 2005
 (in thousands, except share and per share amounts)

| | Nine Months Ended September 30, | |
|----------------------------------------------------------------------|------------------------------------|---------------|
| | 2006 | 2005 |
| INTEREST INCOME | | |
| Loans | \$ 14,749 | \$ 11,721 |
| Federal funds sold/Interest bearing deposits at other banks | 35 | 112 |
| Securities: | | |
| Taxable | 3,209 | 3,556 |
| Non-taxable | 1,427 | 1,456 |
| Total interest income | 19,420 | 16,845 |
| INTEREST EXPENSE | | |
| Deposits | 6,429 | 4,502 |
| Other borrowings | 1,509 | 1,154 |
| Junior subordinated debentures | 621 | 474 |
| Total interest expense | 8,559 | 6,130 |
| NET INTEREST INCOME | 10,861 | 10,715 |
| PROVISION FOR LOAN AND LEASE LOSSES | 815 | 554 |
| NET INTEREST INCOME AFTER PROVISION FOR LOAN AND LEASE LOSSES | 10,046 | 10,161 |
| NON-INTEREST INCOME: | | |
| Bank charges | 1,508 | 1,546 |
| Insurance service and fees | 5,147 | 5,084 |
| Net gain on sales of securities | 114 | 107 |
| Premium on loans sold | 6 | 16 |
| Bank-owned life insurance | 365 | 302 |
| Life insurance proceeds | | 95 |
| Other | 1,282 | 890 |
| Total non-interest income | 8,422 | 8,040 |
| NON-INTEREST EXPENSE: | | |
| Salaries and employee benefits | 7,344 | 6,943 |
| Occupancy | 1,529 | 1,485 |
| Supplies | 216 | 270 |
| Repairs and maintenance | 411 | 430 |
| Advertising and public relations | 343 | 378 |
| Professional services | 602 | 785 |
| Amortization of intangibles | 406 | 386 |

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| | | |
|-------------------------------------------|-----------|-----------|
| Other Insurance | 256 | 282 |
| Other | 2,179 | 2,122 |
| Total non-interest expense | 13,286 | 13,081 |
| INCOME BEFORE INCOME TAXES | 5,182 | 5,120 |
| INCOME TAXES | 1,423 | 1,427 |
| NET INCOME | \$ 3,759 | \$ 3,693 |
| Net income per common share-basic | \$ 1.38 | \$ 1.36 |
| Net income per common share-diluted | \$ 1.38 | \$ 1.36 |
| Cash dividends per common share | \$ 0.68 | \$ 0.65 |
| Weighted average number of common shares | 2,724,207 | 2,721,955 |
| Weighted average number of diluted shares | 2,726,486 | 2,725,745 |

See Notes to Unaudited Consolidated Financial Statements

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PART I FINANCIAL INFORMATION

ITEM I FINANCIAL STATEMENTS

EVANS BANCORP, INC. AND SUBSIDIARIES

UNAUDITED CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY

NINE MONTHS ENDED SEPTEMBER 30, 2006 AND 2005

(in thousands, except share and per share amounts)

| | Common Stock | Capital Surplus | Retained Earnings | Accumulated Other Comprehensive Income | Treasury Stock | Total |
|-------------------------------------------------------------------------------------------------------------------------------------|-------------------------|----------------------------|------------------------------|-----------------------------------------------------------|---------------------------|--------------|
| Balance, January 1, 2005 | \$ 1,307 | \$ 23,361 | \$ 10,808 | \$ 563 | \$ (565) | \$ 35,474 |
| Comprehensive income: | | | | | | |
| Net Income | | | 3,693 | | | 3,693 |
| Unrealized loss on available-for-sale securities, net of tax effect of \$918 and reclassification adjustment of \$(107) | | | | (1,439) | | (1,439) |
| Total comprehensive income | | | | | | 2,254 |
| Cash dividends (\$0.65 per common share) | | | (1,762) | | | (1,762) |
| Stock options expense | | 148 | | | | 148 |
| Reissued 7,391 shares treasury stock under dividend reinvestment plan | | | 2 | | 176 | 178 |
| Reissued 4,817 shares treasury stock under employee stock purchase plan | | | (23) | | 115 | 92 |
| Reissued 800 shares treasury stock under director stock option plan | | | (2) | | 19 | 17 |
| Purchased 16,400 shares for treasury | | | | | (380) | (380) |
| Balance, September 30, 2005 | \$ 1,307 | \$ 23,509 | \$ 12,716 | \$ (876) | \$ (635) | \$ 36,021 |
| Balance, January 1, 2006 | \$ 1,373 | \$ 26,155 | \$ 11,087 | \$ (1,387) | \$ (352) | \$ 36,876 |
| Comprehensive income: | | | | | | |
| Net Income | | | 3,759 | | | 3,759 |
| | | | | 64 | | 64 |

Unrealized gain on
available-for-sale securities,
net of reclassification
adjustment of \$(114) and
tax effect of (\$41)

Total comprehensive
income

Cash dividends (\$0.68 per
common share)

Stock options expense

Reissued 9,642 shares

treasury stock under
dividend reinvestment plan

Reissued 5,773 shares

treasury stock under
employee stock purchase

plan

Purchased 22,750 shares for
treasury

**Balance, September 30,
2006**

| | | | | | | | | | |
|--|----------|-----------|-----------|----|---------|-------|-------|----|---------|
| | | | | | | | | | |
| | | | | | | | | | 3,823 |
| | | | | | (1,855) | | | | (1,855) |
| | 86 | | | | | | | | 86 |
| | (33) | | | | | 219 | | | 186 |
| | (29) | | | | | | 129 | | 100 |
| | | | | | | (489) | | | (489) |
| | \$ 1,373 | \$ 26,179 | \$ 12,991 | \$ | (1,323) | \$ | (493) | \$ | 38,727 |

See Notes to Unaudited Consolidated Financial Statements

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PART I FINANCIAL INFORMATION
 ITEM I FINANCIAL STATEMENTS
 EVANS BANCORP, INC. AND SUBSIDIARIES
 UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS
 NINE MONTHS ENDED SEPTEMBER 30, 2006 AND 2005
 (in thousands)

| | Nine Months Ended September 30, | |
|---------------------------------------------|------------------------------------|-----------|
| | 2006 | 2005 |
| OPERATING ACTIVITIES: | | |
| Interest received | \$ 19,721 | \$ 16,901 |
| Fees received | 8,054 | 7,314 |
| Interest paid | (8,363) | (5,967) |
| Cash paid to employees and suppliers | (12,073) | (10,913) |
| Income taxes paid | (1,650) | (1,571) |
| Proceeds from sale of loans held for resale | 1,599 | 2,569 |
| Originations of loans held for resale | (1,593) | (2,052) |
| | | |
| Net cash provided by operating activities | 5,695 | 6,281 |
| INVESTING ACTIVITIES: | | |
| Available for sales securities: | | |
| Purchases | (331) | (23,077) |
| Proceeds from sales | 2,086 | 7,067 |
| Proceeds from maturities | 17,312 | 20,545 |
| Held to maturity securities: | | |
| Purchases | (2,104) | (1,891) |
| Proceeds from maturities | 2,048 | 695 |
| Additions to properties and equipment | (588) | (1,119) |
| Increase in loans, net of repayments | (19,400) | (32,205) |
| Proceeds from life insurance | | 665 |
| Acquisitions | (187) | (117) |
| Cash paid on earn-out agreements | (57) | (420) |
| | | |
| Net cash used in investing activities | (1,221) | (29,857) |
| FINANCING ACTIVITIES: | | |
| Proceeds from borrowings | 2,917 | |
| Repayments of short-term borrowings | (28,928) | (15,202) |
| Repayments of long-term borrowings | (2,659) | (9,072) |
| Increase in deposits | 22,359 | 52,947 |
| Dividends paid | (1,855) | (1,762) |
| Purchase of treasury stock | (489) | (380) |
| Re-issuance of treasury stock | 286 | 287 |

| | | |
|-----------------------------------------------------|-----------|-----------|
| Net cash (used in) provided by financing activities | (8,369) | 26,818 |
| Net (decrease) increase in cash and equivalents | (3,895) | 3,242 |
| CASH AND CASH EQUIVALENTS: | | |
| Beginning of period | 15,635 | 8,124 |
| End of period | \$ 11,740 | \$ 11,366 |

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PART I FINANCIAL INFORMATION
 ITEM I FINANCIAL STATEMENTS
 EVANS BANCORP, INC. AND SUBSIDIARIES
 UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS
 NINE MONTHS ENDED SEPTEMBER 30, 2006 AND 2005
 (in thousands)

| | Nine Months Ended September 30, | |
|-----------------------------------------------------------------------------------|------------------------------------|-----------------|
| | 2006 | 2005 |
| RECONCILIATION OF NET INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES: | | |
| Net income | \$ 3,759 | \$ 3,693 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 1,359 | 1,405 |
| Deferred tax benefit | (102) | (109) |
| Provision for loan and lease losses | 815 | 554 |
| Net gain on sales of securities | (114) | (107) |
| Premiums on loans sold | (6) | (16) |
| Stock options expense | 86 | 148 |
| Net change in loans held for resale | | 517 |
| Changes in assets and liabilities affecting cash flow: | | |
| Other assets | (1,286) | (1,001) |
| Other liabilities | 1,184 | 1,197 |
| NET CASH PROVIDED BY OPERATING ACTIVITIES | \$ 5,695 | \$ 6,281 |

See Notes to Unaudited Consolidated Financial Statements

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PART 1 FINANCIAL INFORMATION**ITEM 1 FINANCIAL STATEMENTS****EVANS BANCORP, INC. AND SUBSIDIARIES****NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS****NINE MONTHS ENDED SEPTEMBER 30, 2006 AND 2005****1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

The accounting and reporting policies followed by Evans Bancorp, Inc. (the Company), a financial holding company, and its two direct, wholly-owned subsidiaries: (i) Evans National Bank (the Bank), and its subsidiaries, Evans National Leasing, Inc. (ENL) and Evans National Holding Corp. (ENHC); and (ii) Evans National Financial Services, Inc. (ENFS), and its subsidiary ENB Insurance Agency, Inc. (ENBI) and its subsidiaries, Frontier Claims Services, Inc. (FCS) and ENB Associates Inc. (ENB), in the preparation of the accompanying interim unaudited consolidated financial statements conform with U.S. generally accepted accounting principles and with general practice within the banking industry. Except as the context otherwise requires, the Company and its direct and indirect subsidiaries are collectively referred to in this report as the Company.

The accompanying consolidated financial statements are unaudited. In the opinion of management, all adjustments necessary for a fair presentation of the Company's financial position and results of operations for the interim periods have been made. Such adjustments are of a normal recurring nature.

The results of operations for the three and nine month period ended September 30, 2006 are not necessarily indicative of the results to be expected for the full year. The accompanying unaudited consolidated financial statements should be read in conjunction with the Audited Consolidated Financial Statements and the Notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2005.

2. SECURITIES

Securities which the Company has the positive ability and intent to hold to maturity are stated at amortized cost. Securities which the Company has identified as available-for-sale are stated at fair value with unrealized gains and losses excluded from earnings and reported net of deferred income taxes, in accumulated other comprehensive income (loss), a component of stockholders equity. Available-for-sale securities are net of unrealized losses of \$2.0 million and \$2.1 million as of September 30, 2006 and December 31, 2005, respectively. As of September 30, 2006 and December 31, 2005, the securities portfolio did not contain any other than temporary declines in fair value.

3. ALLOWANCE FOR LOAN AND LEASE LOSSES

The allowance for loan and lease losses represents the amount charged against the Bank's earnings to establish an allowance for probable loan and lease losses based on the Bank's management's evaluation of the loan and lease portfolio. Factors considered by the Bank's management in establishing the allowance include: the collectibility of individual loans and leases, current loan and lease concentrations, charge-off history, delinquent loan and lease percentages, input from regulatory agencies and general economic conditions.

On a quarterly basis, management of the Bank meets to review and determine the adequacy of the allowance for loan and lease losses. In making this determination, the Bank's management analyzes the ultimate collectibility of the loans and leases in its portfolio by incorporating feedback provided by the Bank's

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internal loan staff, an independent internal loan review function and information provided by examinations performed by regulatory agencies.

The analysis of the allowance for loan and lease losses is composed of three components: specific credit allocation, general portfolio allocation and subjectively by determined allocation. The specific credit allocation includes a detailed review of the credit in accordance with the Statement of Financial Accounting Standards (SFAS) No. 114,

Accounting by Creditors for Impairment of a Loan and No. 118, Accounting by Creditors for Impairment of a Loan Income Recognition and Disclosures, and allocation is made based on this analysis. The general portfolio allocation consists of an assigned reserve percentage based on the actual credit rating of the loan or lease.

The subjective portion of the allowance reflects management's evaluation of various conditions, and involves a higher degree of uncertainty because this component of the allowance is not identified with specific problem credits of portfolio segments. The conditions evaluated in connection with this component include the following: industry and regional conditions; seasoning of the loan and lease portfolio and changes in the composition of and growth in the loan and lease portfolio; the strength and duration of the business cycle; existing general economic and business conditions in the lending areas; credit quality trends in nonaccruing loans and leases; historical loan and lease charge-off experience; and the results of bank regulatory examinations.

The following table sets forth information regarding the allowance for loan and lease losses for the nine month periods ended September 30, 2006 and 2005.

Allowance for loan and lease losses

| | Nine months ended September 30, | |
|------------------------------|------------------------------------|----------|
| | 2006 | 2005 |
| | (in thousands) | |
| Beginning balance, January 1 | \$ 3,211 | \$ 2,999 |
| Charge-offs: | | |
| Commercial | (205) | (175) |
| Real estate mortgages | | (2) |
| Installment loans | (42) | (84) |
| Overdrafts | (28) | (23) |
| Direct financing leases | (250) | (50) |
| Total charge-offs | (525) | (334) |
| Recoveries: | | |
| Commercial | 48 | 40 |
| Real estate mortgages | | |
| Installment loans | 61 | 10 |
| Overdrafts | 15 | 6 |
| Direct financing leases | 55 | 51 |
| Total recoveries | 179 | 107 |
| Net charge-offs | (346) | (227) |

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| | | |
|--------------------------------------------------------------------------------------|----------|----------|
| Provision for loan and lease losses | 815 | 554 |
| Ending balance, September 30 | \$ 3,680 | \$ 3,326 |
| Ratio of net charge-offs to average net loans and leases outstanding (annualized) | 0.17% | 0.13% |

Table of Contents**4. PER SHARE DATA**

The common stock per share information is based upon the weighted average number of shares outstanding during each period, retroactively adjusted for stock dividends and stock splits. The Company's potential dilutive securities included 2,367 and 2,279 dilutive shares for the three and nine month periods ended September 30, 2006. There were 2,639 and 3,790 dilutive shares for the three and nine month periods ended September 30, 2005. On August 17, 2006, the Company declared a cash dividend of \$0.34 per share payable on October 2, 2006 to shareholders of record as of September 8, 2006. All September 30, 2005 share and per share amounts have been adjusted to reflect a 5% stock dividend paid in December 2005.

Potential common shares that would have the effect of increasing diluted earnings per share are considered to be anti-dilutive. In accordance with SFAS No. 128, Earnings Per Share, these shares were not included in calculating diluted earnings per share. As of the three and nine month periods ended September 30, 2006, there were approximately 55 thousand shares that are not included in calculating diluted earnings per share because their effect was anti-dilutive. As of the three and nine month periods ended September 30, 2005, there were approximately 42 thousand shares that are not included in calculating diluted earnings per share because their effect was anti-dilutive.

5. TREASURY STOCK

During the quarter ended September 30, 2006 the Company repurchased 4,700 shares of common stock at an average cost of \$21.74 per share, pursuant to the Company's publicly announced common stock repurchase program.

6. SEGMENT INFORMATION

The Company is comprised of two primary business segments, banking and insurance agency activities. The following tables set forth information regarding these segments for the three and nine month periods ended September 30, 2006 and 2005.

Three Months Ended
September 30, 2006
(in thousands)

| | Banking Activities | Insurance Agency Activities | Total |
|-------------------------------------------------------------------------|-------------------------------|--------------------------------------------|--------------|
| Net interest income (expense) | \$ 3,765 | (\$118) | \$ 3,647 |
| Provision for loan and lease losses | 305 | | 305 |
| Net interest income (expense) after provision for loan and lease losses | 3,460 | (118) | 3,342 |
| Non-interest income | 1,267 | | 1,267 |
| Insurance service and fees | | 1,460 | 1,460 |
| Non-interest expense | 3,242 | 1,074 | 4,316 |
| Income before income taxes | 1,485 | 268 | 1,753 |

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| | | | | | |
|--------------|----|-------|----|-----|----------|
| Income taxes | | 363 | | 108 | 471 |
| Net income | \$ | 1,122 | \$ | 160 | \$ 1,282 |

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Nine Months Ended
September 30, 2006
(in thousands)

| | Banking Activities | Insurance Agency Activities | Total |
|-------------------------------------------------------------------------|-------------------------------|--------------------------------------------|--------------|
| Net interest income (expense) | \$ 11,211 | (\$350) | \$ 10,861 |
| Provision for loan and lease losses | 815 | | 815 |
| Net interest income (expense) after provision for loan and lease losses | 10,396 | (350) | 10,046 |
| Non-interest income | 3,275 | | 3,275 |
| Insurance service and fees | | 5,147 | 5,147 |
| Non-interest expense | 9,893 | 3,393 | 13,286 |
| Income before income taxes | 3,778 | 1,404 | 5,182 |
| Income taxes | 861 | 562 | 1,423 |
| Net income | \$ 2,917 | \$ 842 | \$ 3,759 |

Three Months Ended
September 30, 2005
(in thousands)

| | Banking Activities | Insurance Agency Activities | Total |
|-------------------------------------------------------------------------|-------------------------------|--------------------------------------------|--------------|
| Net interest income (expense) | \$ 3,862 | (\$104) | \$ 3,758 |
| Provision for loan and lease losses | 215 | | 215 |
| Net interest income (expense) after provision for loan and lease losses | 3,647 | (104) | 3,543 |
| Non-interest income | 997 | | 997 |
| Insurance service and fees | | 1,508 | 1,508 |
| Non-interest expense | 3,152 | 1,142 | 4,294 |
| Income before income taxes | 1,492 | 262 | 1,754 |
| Income taxes | 393 | 105 | 498 |
| Net income | \$ 1,099 | \$ 157 | \$ 1,256 |

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Nine Months Ended
September 30, 2005
(in thousands)

| | Banking Activities | Insurance Agency Activities | Total |
|-------------------------------------------------------------------------|-------------------------------|--------------------------------------------|--------------|
| Net interest income (expense) | \$ 11,002 | (\$287) | \$ 10,715 |
| Provision for loan and lease losses | 554 | | 554 |
| Net interest income (expense) after provision for loan and lease losses | 10,448 | (287) | 10,161 |
| Non-interest income | 2,956 | | 2,956 |
| Insurance service and fees | | 5,084 | 5,084 |
| Non-interest expense | 9,595 | 3,486 | 13,081 |
| Income before income taxes | 3,809 | 1,311 | 5,120 |
| Income taxes | 903 | 524 | 1,427 |
| Net income | \$ 2,906 | \$ 787 | \$ 3,693 |

7. CONTINGENT LIABILITIES AND COMMITMENTS

The unaudited consolidated financial statements do not reflect various commitments and contingent liabilities, which arise in the normal course of business, and which involve elements of credit risk, interest rate risk and liquidity risk. These commitments and contingent liabilities consist of commitments to extend credit and standby letters of credit. A summary of the Bank's commitments and contingent liabilities at September 30, 2006 and 2005 is as follows:

| | 2006 | 2005 |
|------------------------------|----------------|-------------|
| | (in thousands) | |
| Commitments to extend credit | \$ 60,343 | \$ 62,926 |
| Standby letters of credit | 2,134 | 1,832 |
| Total | \$ 62,477 | \$ 64,758 |

Commitments to extend credit and standby letters of credit include some exposure to credit loss in the event of nonperformance of the customer. The Bank's credit policies and procedures for credit commitments and financial guarantees are the same as those for extensions of credit that are recorded on the Company's unaudited consolidated balance sheets. Because these instruments have fixed maturity dates, and because they may expire without being drawn upon, they do not necessarily represent cash requirements of the Bank. The Bank has not incurred any losses on its commitments during the past two years.

Certain lending commitments for construction residential mortgage loans are considered derivative instruments under the guidelines of SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities. The changes in the

fair value of these commitments due to interest rate risk are not recorded on the consolidated balance sheets as these derivatives are not considered material.

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The Company is subject to possible litigation proceedings in the normal course of business. As of September 30, 2006, there were no claims pending against the Company that management considered to be material.

8. RECLASSIFICATIONS

Certain reclassifications have been made to the 2005 unaudited consolidated financial statements to conform with the presentation used in 2006.

9. NET PERIODIC BENEFIT COSTS

The Bank has a defined benefit pension plan covering substantially all Company employees. The plan provides benefits that are based on the employees' compensation and years of service. The Bank uses an actuarial method of amortizing prior service cost and unrecognized net gains or losses which result from actual experience and assumptions being different than those that are projected. The amortized method the Bank is using recognizes the prior service cost and net gains or losses over the average remaining service period of active employees.

The Bank also maintains a nonqualified supplemental executive retirement plan covering certain members of the Company's senior management. The Bank uses an actuarial method of amortizing unrecognized net gains or losses which result from actual expense and assumptions being different than those that are projected. The amortization method the Bank uses recognizes the net gains or losses over the average remaining service period of active employees.

The following table represents net periodic benefit costs recognized:
Three months ended September 30,
(in thousands)

| | Pension Benefits | | Supplemental Executive Retirement Plan | |
|------------------------------------|-------------------------|-------|-------------------------------------------------------|-------|
| | 2006 | 2005 | 2006 | 2005 |
| Service cost | \$ 79 | \$ 72 | \$ 29 | \$ 26 |
| Interest cost | 49 | 44 | 38 | 37 |
| Expected return on plan assets | (58) | (48) | | |
| Amortization of prior service cost | (4) | (4) | 14 | 15 |
| Amortization of the net loss | 6 | 1 | 4 | 4 |
| Net periodic benefit cost | \$ 72 | \$ 65 | \$ 85 | \$ 82 |

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Nine months ended September 30,
(in thousands)

| | Pension Benefits | | Supplemental Executive Retirement Plan | |
|------------------------------------|-------------------------|--------|-------------------------------------------------------|--------|
| | 2006 | 2005 | 2006 | 2005 |
| Service cost | \$ 237 | \$ 216 | \$ 87 | \$ 78 |
| Interest cost | 147 | 132 | 114 | 111 |
| Expected return on plan assets | (174) | (144) | | |
| Amortization of prior service cost | (12) | (12) | 42 | 45 |
| Amortization of the net loss | 18 | 3 | 12 | 12 |
| Net periodic benefit cost | \$ 216 | \$ 195 | \$ 255 | \$ 246 |

10. STOCK-BASED COMPENSATION

In December 2004, the Financial Accounting Standards Board (FASB) issued SFAS No. 123 (revised 2004), Share Based Payment (SFAS No. 123(R)). SFAS No. 123(R) supersedes Accounting Principles Board (APB) Opinion No. 25, Accounting for Stock Issued to Employees, and amends SFAS No. 95, Statement of Cash Flows. Generally, the fair value approach in SFAS No. 123(R) is similar to the fair value approach described in SFAS No. 123. In 2005, the Company used the Black-Scholes-Merton formula to estimate the fair value of stock options granted to employees. The Company adopted SFAS No. 123(R), using the modified-prospective method, beginning January 1, 2006. Based on the terms of its equity compensation plans, the adoption of SFAS No. 123(R) did not require the Company to record a cumulative effect of adjustment. The Company also elected to continue to estimate the fair value of stock options using the Black-Scholes-Merton formula.

In the first nine months of 2006, because the fair value recognition provisions of SFAS No. 123, Stock-Based Compensation, and SFAS No. 123(R) were materially consistent under the Company's valuation of its equity plans, the adoption of SFAS No. 123(R) did not have a significant impact on the Company's financial position or the Company's results of operations. Further, the Company believes the adoption of SFAS No. 123(R) will not have a material impact on the Company's future stock-based compensation expense.

Under the Company's 1999 Employee Stock Option and Long-Term Incentive Plan, as amended (the Option Plan), the Company may grant options to its officers, directors and key employees for up to 289,406 shares of common stock (as adjusted for stock dividends). Under the Option Plan, the exercise price of each option is not to be less than 100% of the market price of the Company's stock on the date of grant and an option's maximum term is ten years. The Company normally issues shares out of its treasury for any options exercised. The options have vesting schedules from 1 year through 9 years. At September 30, 2006, there were a total of 196,970 shares available for grant under the Option Plan.

As of December 31, 2005 there were 88,577 stock options outstanding under the Option Plan with a weighted-average exercise price of \$21.32. During the three and nine month period ended September 30, 2006 there were no options granted, exercised, or expired. During the three and nine month periods ended September 30, 2006 there were 6,520 options forfeited at a weighted average exercise price of \$20.94. At September 30, 2006 there were 82,057 stock options outstanding under the Option Plan with a weighted-average exercise price of \$21.35, with no intrinsic value, and a weighted-average remaining contractual term of 7.8 years.

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At September 30, 2006 there were 39,752 options exercisable at a weighted average exercise price of \$21.77, with no intrinsic value, and a weighted-average remaining contractual term of 7.64 years.

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On February 18, 2003, the Board of Directors of the Company adopted the Evans Bancorp, Inc. Employee Stock Purchase Plan (the Purchase Plan). As of September 30, 2006, there were 84,090 shares of common stock available to issue to its full-time employees, nearly all of whom are eligible to participate. Under the terms of the Purchase Plan, employees can choose each year to have up to 15% of their annual base earnings withheld to purchase the Company's common stock. The Company grants options on January 1 and July 1 of each year during the term of the Purchase Plan. The purchase price of the stock is 85% of the lower of its price on the grant date or the exercise date. Compensation cost is recognized for the fair value of the employees' purchase rights, which was estimated using the Black-Scholes-Merton model.

As of September 30, 2006, there was approximately \$153 thousand of total unrecognized compensation cost related to nonvested share-based compensation arrangements granted under the Company's equity plans. That cost is expected to be recognized over a weighted-average period of 2.0 years. This expected cost does not include the impact of any future stock-based compensation awards. The compensation cost charged against income for those plans was \$26 thousand and \$86 thousand for the three and nine month periods ended September 30, 2006, respectively, and \$52 thousand and \$148 thousand for the same periods of 2005.

11. RECENT ACCOUNTING PRONOUNCEMENTS

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements which is effective for fiscal years beginning after November 15, 2007 and for interim periods within those years. This statement defines fair value, establishes a framework for measuring fair value and expands the related disclosure requirements. We are currently evaluating the potential impact of this statement.

In September 2006, the FASB issued SFAS No. 158, Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans an amendment of FASB Statements No. 87, 88, 106 and 132(R) (SFAS 158). This statement requires balance sheet recognition of the overfunded or underfunded status of pension and postretirement benefit plans. Under SFAS 158, actuarial gains and losses, prior service costs or credits, and any remaining transition assets or obligations that have not been recognized under previous accounting standards must be recognized as a component of other comprehensive income on the Statement of Stockholders' Equity, net of tax effects, until they are amortized as a component of net periodic benefit cost. In addition, the measurement date, the date at which plan assets and the benefit obligation are measured, is required to be the company's fiscal year end. This statement is effective for public entities for fiscal years ending after December 15, 2006. We are currently evaluating the potential impact of this statement.

In September 2006, the SEC staff issued Staff Accounting Bulletin (SAB) No. 108, Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements (SAB 108). SAB 108 was issued in order to eliminate the diversity of practice in how public companies quantify misstatements of financial statements, including misstatements that were not material to prior years' financial statements. We will initially apply the provisions of SAB 108 in connection with the preparation of our annual financial statements for the year ending December 31, 2006. We are currently evaluating the potential impact of SAB 108 may have on our financial position and results of operations.

ITEM 2 MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This Quarterly Report on Form 10-Q may contain certain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the Securities Act), and Section 21E of the Securities Exchange

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Act of 1934, as amended (the Exchange Act), that involve substantial risks and uncertainties. When used in this report, or in the documents incorporated by reference herein, the words anticipate, believe, estimate, expect, intend, may, plan, seek, and similar expressions identify such forward-looking statements. These forward-looking statements include statements regarding the Company's business plans, prospects, growth and operating strategies, statements regarding the asset quality of the Company's loan and investment portfolios, and estimates of the Company's risks and future costs and benefits.

These forward-looking statements are based largely on the expectations of the Company's management and are subject to a number of risks and uncertainties, including but not limited to general economic conditions, either nationally or in the Company's market areas, that are worse than expected; increased competition among depository or other financial institutions; inflation and changes in the interest rate environment that reduce the Company's margins or reduce the fair value of financial instruments; changes in laws or government regulations affecting financial institutions, including changes in regulatory fees and capital requirements; the Company's ability to enter new markets successfully and capitalize on growth opportunities; the Company's ability to successfully integrate acquired entities; changes in accounting pronouncements and practices, as adopted by financial institution regulatory agencies, the Financial Accounting Standards Board and the Public Company Accounting Oversight Board; changes in consumer spending, borrowing and saving habits; changes in the Company's organization, compensation and benefit plans; and other factors discussed elsewhere in this Report on Form 10-Q, as well as in the Company's periodic reports filed with the Securities and Exchange Commission (the SEC). Many of these factors are beyond the Company's control and are difficult to predict.

Because of these and other uncertainties, the Company's actual results, performance or achievements could differ materially from those contemplated, expressed or implied by the forward-looking statements contained herein.

Forward-looking statements speak only as of the date they are made. The Company undertakes no obligation, to publicly update or revise forward-looking information, whether as a result of new, updated information, future events or otherwise.

APPLICATION OF CRITICAL ACCOUNTING ESTIMATES

The Company's Unaudited Consolidated Financial Statements are prepared in accordance with U.S. generally accepted accounting principles and follow general practices within the industries in which it operates. Application of these principles requires management to make estimates, assumptions and judgments that affect the amounts reported in the Company's Unaudited Consolidated Financial Statements and Notes. These estimates, assumptions and judgments are based on information available as of the date of the Unaudited Consolidated Financial Statements. Accordingly, as this information changes, the Unaudited Consolidated Financial Statements could reflect different estimates, assumptions and judgments. Certain policies inherently have a greater reliance on the use of estimates, assumptions and judgments, and as such, have a greater possibility of producing results that could be materially different than originally reported. Estimates, assumptions and judgments are necessary when assets and liabilities are required to be recorded at fair value, when a decline in the value of an asset not carried on the financial statements at fair value warrants an impairment write-down or valuation reserve to be established, or when an asset or liability needs to be recorded contingent upon a future event. Carrying assets and liabilities at fair value inherently results in more financial statement volatility. The fair values and the information used to record valuation adjustments for certain assets and liabilities are based either on quoted market prices or are provided by other third-party sources, when available. When third-party information is not available, valuation adjustments are estimated in good faith by management primarily through the use of internal cash flow modeling techniques.

The most significant accounting policies followed by the Company are presented in Note 1 to the Audited Consolidated Financial Statements included in Item 8 in its Annual Report on Form 10-K. These policies, along with the disclosures presented in the other Notes to the Company's Audited Consolidated Financial Statements contained in its Annual Report on Form 10-K and in this financial review, provide information on how significant assets and liabilities are valued in the Company's Unaudited Consolidated Financial Statements and how those values are determined.

Based on the valuation techniques used and the sensitivity of financial statement amounts to the methods, assumptions and estimates underlying those amounts, management has identified the determination of the allowance for loan and lease losses and valuation of goodwill to be the accounting areas that require the most subjective or

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complex judgments, and as such, could be most subject to revision as new information becomes available.

Allowance for Loan and Lease Losses

The allowance for loan and lease losses represents management's estimate of probable losses in the Bank's loan and lease portfolio. Determining the amount of the allowance for loan and lease losses is considered a critical accounting estimate because it requires significant judgment on the part of management and the use of estimates related to the amount and timing of expected future cash flows on impaired loans and leases, estimated losses on pools of homogeneous loans and leases based on historical loss experience and consideration of current economic trends and conditions, all of which may be susceptible to significant change. The loan and lease portfolio also represents the largest asset type on the Unaudited Consolidated Balance Sheets. Note 1 to the Audited Consolidated Financial Statements included in Item 8 in its Annual Report on Form 10-K describes the methodology used to determine the allowance for loan and lease losses.

Goodwill

The amount of goodwill reflected in the Company's Unaudited Consolidated Financial Statements is required to be tested by management for impairment on at least an annual basis. The test for impairment of goodwill on the identified reporting unit is considered a critical accounting estimate because it requires judgment on the part of management and the use of estimates related to the growth assumptions and market multiples used in the valuation model.

ANALYSIS OF FINANCIAL CONDITION**Loan and Lease Activity**

Total gross loans and leases grew to \$279.0 million at September 30, 2006, reflecting a \$6.0 million or 2.2% increase from June 30, 2006 and an \$18.9 million or 7.3% increase from December 31, 2005. Gross loans and leases are net of \$6.8 million, \$6.3 million and \$4.0 million unearned income on direct financing leases as of September 30, 2006, June 30, 2006 and December 31, 2005, respectively. Commercial loans and leases totaled \$193.5 million at September 30, 2006, reflecting a \$3.5 million or 1.9% increase from June 30, 2006 and a \$10.9 million or 6.0% increase from December 31, 2005. Growth in direct financing leases of \$2.3 million or 9.0% and commercial real estate loans of \$1.9 million or 1.4%, offset by decreases in commercial installment loans of \$1.3 million or 6.8%, were largely responsible for the increase from June 30, 2006. Growth in direct financing leases of \$10.8 million or 63.8%, and commercial real estate loans of \$1.8 million or 1.3%, offset by decreases in commercial installment loans of \$1.3 million or 6.8%, were largely responsible for the increase from December 31, 2005.

Consumer loans totaled \$84.8 million at September 30, 2006, reflecting a \$2.4 million or 2.9% increase from June 30, 2006 and a \$7.8 million or 10.4% increase from December 31, 2005. Consumer real estate loans increased \$1.9 million or 4.3% from June 30, 2006 and \$6.7 million or 16.5% from December 31, 2005. The Bank continues to sell certain fixed rate residential mortgages originated below a designated interest level to the Federal National Mortgage Association (FNMA), while maintaining the servicing rights for those mortgages. During the three month period ended September 30, 2006, the Bank sold mortgages to FNMA totaling \$0.9 million, as compared to \$0.8 million during the three month period ended September 30, 2005. During the nine month period ended September 30, 2006, the Bank sold mortgages to FNMA totaling \$1.6 million, as compared to \$2.6 million during the nine month period ended September 30, 2005. At September 30, 2006, the Bank had a loan servicing portfolio principal balance of \$28.2 million upon which it earns servicing fees, as compared to \$28.6 million at June 30, 2006, and \$28.8 million at December 31, 2005.

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Loan and Lease Portfolio Composition

The following table presents selected information on the composition of the Company's loan and lease portfolio in dollar amounts and in percentages as of the dates indicated.

| | September 30, 2006 (in thousands) | Percentage | December 31, 2005 (in thousands) | Percentage |
|------------------------------------------|-----------------------------------------|---------------|----------------------------------------|---------------|
| Commercial Loans and Leases | | | | |
| Real Estate | \$ 137,198 | 49.2% | \$ 135,425 | 52.1% |
| Installment | 17,332 | 6.2% | 18,588 | 7.1% |
| Direct Financing Leases | 27,748 | 9.9% | 16,945 | 6.5% |
| Lines of Credit | 11,207 | 4.1% | 11,603 | 4.5% |
| Cash Reserve | 42 | 0.0% | 38 | 0.0% |
| Total Commercial Loans and Leases | 193,527 | 69.4% | 182,599 | 70.2% |
| Consumer Loans | | | | |
| Real Estate | 47,266 | 16.9% | 40,586 | 15.6% |
| Home Equity | 34,478 | 12.4% | 33,114 | 12.7% |
| Installment | 2,412 | 0.9% | 2,254 | 0.9% |
| Overdrafts | 159 | 0.1% | 219 | 0.1% |
| Credit Card | 304 | 0.1% | 307 | 0.1% |
| Other | 132 | 0.0% | 288 | 0.1% |
| Total Consumer Loans | 84,751 | 30.4% | 76,768 | 29.5% |
| Net Deferred Costs & Unearned Discounts | 673 | 0.2% | 654 | 0.3% |
| Total Loans and Leases | 278,951 | 100.0% | 260,021 | 100.0% |
| Allowance for Loan and Lease Losses | (3,680) | | (3,211) | |
| Loans and Leases, net | \$ 275,271 | | \$ 256,810 | |

Net loan and lease charge-offs were \$229 thousand in the three month period ended September 30, 2006 as compared to net charge-offs of \$55 thousand in the same period of 2005. Net charge-offs were \$346 thousand for the nine month period ended September 30, 2006 as compared to \$227 thousand in the same period of 2005.

Non-performing loans and leases, defined as accruing loans and leases greater than 90 days past due and non-accrual loans and leases, totaled 0.24% of total loans and leases outstanding at September 30, 2006 as compared to 0.37% at June 30, 2006 and 0.72% at December 31, 2005. The allowance for loan and lease losses totaled \$3.7 million or 1.32% of total loans and leases outstanding at September 30, 2006 as compared to \$3.6 million or 1.32% of total loans and leases at June 30, 2006 and \$3.2 million or 1.23% of total loans and leases outstanding at December 31, 2005.

The adequacy of the Company's allowance for loan and lease losses is reviewed quarterly by the Company's management with consideration given to loan and lease concentrations, charge-off history, delinquent

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loan and lease percentages, and general economic conditions. Management believes the allowance for loan and lease losses is adequate for losses from existing loans and leases.

The following table sets forth information regarding non-performing loans and leases as of the dates specified.

| | September 30, 2006 | December 31, 2005 |
|---------------------------------------------------------------------------------|-----------------------------------|------------------------------|
| | (in thousands) | |
| Non-accruing loans and leases: | | |
| Mortgage loans on real estate Residential 1-4 family | \$ | \$ |
| Commercial and multi-family | 151 | 600 |
| Construction | | |
| Second mortgages | | |
| Home equity lines of credit | | |
| Total mortgage loans on real estate | 151 | 600 |
| Direct financing leases | | |
| Commercial loans | 445 | 1,175 |
| Consumer installment loans | | |
| Personal | | |
| Credit cards | | |
| Other | | |
| Total consumer installment loans | | |
| Total non-accruing loans and leases | \$ 596 | \$ 1,775 |
| Accruing loans and leases 90+ days past due | 81 | 95 |
| Total non-performing loans and leases | 677 | 1,870 |
| Total non-performing loans and leases as a percentage of total assets | 0.15% | 0.41% |
| Total non-performing loans and leases as a percentage of total loans and leases | 0.24% | 0.72% |

For the three and nine month periods ended September 30, 2006, gross interest income that would have been reported on non-accruing loans and leases had they been current, was \$15 thousand and \$69 thousand, respectively. For the three and nine month periods ended September 30, 2005, gross interest income that would have been reported on non-accruing loans and leases had they been current, was \$34 thousand and \$101 thousand, respectively. There was no interest income included in net income for the three and nine month periods ended September 30, 2006 and 2005 on non-accruing loans and leases. Non-accruing commercial loans declined \$0.7 million from December 31, 2005 due mainly to a \$0.5 million recovery on collateral for one significant non-accrual loan in the first quarter of 2006. Non-accruing commercial mortgage loans on real estate declined \$0.4 million from December 31, 2005 due mainly to \$0.3 million in payoffs in the first quarter of 2006 and \$0.1 million in payoffs in the third quarter of 2006.

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Investing Activities

Total securities declined to \$140.8 million at September 30, 2006, reflecting a \$7.3 million or 4.9% decrease from June 30, 2006, and a \$19.1 million or 12.0% decrease from December 31, 2005. The decline in the securities portfolio was due in part to available funds being used for increased lending. The Company monitors extension and prepayment risk in the portfolio to limit potential exposures. Management believes the average expected life of the portfolio is 3.3 years as of September 30, 2006, as compared to 3.7 years as of June 30, 2006 and 3.5 years as of December 31, 2005. Available-for-sale securities with a total fair value of \$130.3 million at September 30, 2006 were pledged as collateral to secure public deposits and for other purposes required or permitted by law.

Funding Activities

Total deposits at September 30, 2006 were \$359.2 million, reflecting a \$16.2 million or 4.7% increase from June 30, 2006 and a \$22.4 million or 6.6% increase from December 31, 2005. These increases were mainly attributable to increases in time deposits of \$13.3 million or 9.6% and \$13.0 million or 9.3% from June 30, 2006 and December 31, 2005, respectively. In the third quarter, the Bank has chosen to increase non-core funding in time deposits in place of short-term borrowings due to favorable rate and maturity considerations. Based on such, short-term borrowings from other correspondent banks and the Federal Home Loan Bank of New York at September 30, 2006 declined \$18.0 million or 55.8% from June 30, 2006 and \$22.9 million or 61.7% from December 31, 2005. Demand deposits at September 30, 2006 were \$70.1 million, reflecting a \$1.9 million or 2.8% increase from June 30, 2006 but a \$1.1 million or 1.6% decrease from December 31, 2005. Savings deposits at September 30, 2006 were \$90.1 million, reflecting a \$0.3 million or 0.4% increase from June 30, 2006 and a \$3.5 million or 4.1% increase from December 31, 2005. Additionally, due to municipal tax collections in the first and third quarters of 2006, munivest balances and securities sold under agreements to repurchase at September 30, 2006 were \$35.4 million and \$9.4 million, respectively. These are increases of \$0.7 million or 2.0% and \$3.4 million or 57.6% from June 30, 2006, and \$7.8 million or 28.5% and \$2.9 million or 45.3% from December 31, 2005 for munivest and securities sold under agreements to repurchase, respectively.

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ANALYSIS OF RESULTS OF OPERATIONS**Average Balance Sheet**

The following tables present the significant categories of the assets and liabilities of the Company, interest income and interest expense, and the corresponding yields earned and rates paid for the periods indicated. The assets and liabilities are presented as daily averages. The average loan and lease balances include both performing and non-performing loans and leases. Investments are included at amortized cost. Yields are presented on a non-tax-equivalent basis.

| | Three Months Ended September 30, 2006 | | | Three Months Ended September 30, 2005 | | |
|---------------------------------------|----------------------------------------------------------------------|--------------------------------------|------------------------|----------------------------------------------------------------------|--------------------------------------|------------------------|
| | Average Outstanding Balance (dollars in thousands) | Interest Earned/ Paid | Yield/ Rate | Average Outstanding Balance (dollars in thousands) | Interest Earned/ Paid | Yield/ Rate |
| ASSETS | | | | | | |
| Interest-earning assets: | | | | | | |
| Loans and leases, net | \$ 272,492 | \$ 5,242 | 7.69% | \$ 245,346 | \$ 4,307 | 7.02% |
| Taxable securities | 100,440 | 1,030 | 4.10% | 124,928 | 1,154 | 3.69% |
| Tax-exempt securities | 43,570 | 470 | 4.31% | 45,917 | 478 | 4.16% |
| Federal funds sold | 514 | 5 | 3.89% | 2,770 | 13 | 1.88% |
| Total interest-earning assets | 417,016 | 6,747 | 6.47% | 418,961 | 5,952 | 5.68% |
| Non interest-earning assets: | | | | | | |
| Cash and due from banks | 12,584 | | | 10,207 | | |
| Premises and equipment, net | 8,172 | | | 8,284 | | |
| Other assets | 29,645 | | | 26,083 | | |
| Total Assets | \$ 467,417 | | | \$ 463,535 | | |
| LIABILITIES & STOCKHOLDERS | | | | | | |
| EQUITY | | | | | | |
| Interest-bearing liabilities: | | | | | | |
| NOW | \$ 11,952 | \$ 6 | 0.20% | \$ 12,443 | \$ 5 | 0.16% |
| Regular savings | 89,868 | 272 | 1.21% | 93,774 | 200 | 0.85% |
| Muni-Vest savings | 34,293 | 385 | 4.49% | 50,318 | 380 | 3.02% |
| Time deposits | 152,207 | 1,745 | 4.59% | 135,560 | 1,068 | 3.15% |
| Other borrowed funds | 45,680 | 452 | 3.96% | 44,873 | 356 | 3.17% |
| Junior subordinated debentures | 11,330 | 223 | 7.87% | 11,330 | 173 | 6.11% |
| Securities sold U/A to repurchase | 8,564 | 17 | 0.79% | 6,070 | 12 | 0.79% |
| | 353,894 | \$ 3,100 | 3.50% | 354,368 | \$ 2,194 | 2.48% |

Total interest-bearing liabilities

Noninterest-bearing liabilities:

| | | |
|-----------------|--------|--------|
| Demand deposits | 66,430 | 64,900 |
| Other | 9,255 | 7,362 |

| | | |
|-------------------|------------|------------|
| Total liabilities | \$ 429,579 | \$ 426,630 |
|-------------------|------------|------------|

| | | |
|---------------------|--------|--------|
| Stockholders equity | 37,838 | 36,905 |
|---------------------|--------|--------|

| | | |
|------------------------------|------------|------------|
| Total Liabilities and Equity | \$ 467,417 | \$ 463,535 |
|------------------------------|------------|------------|

| | | |
|-----------------------|----------|----------|
| Net interest earnings | \$ 3,647 | \$ 3,758 |
|-----------------------|----------|----------|

| | | |
|--------------------------------------|-------|-------|
| Net yield on interest earning assets | 3.50% | 3.59% |
|--------------------------------------|-------|-------|

| | | |
|----------------------|-------|-------|
| Interest rate spread | 2.97% | 3.20% |
|----------------------|-------|-------|

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| | Nine Months Ended September 30, 2006 | | | Nine Months Ended September 30, 2005 | | |
|---------------------------------------|-------------------------------------------------------------|-----------------------------|----------------|-------------------------------------------------------------|-----------------------------|----------------|
| | Average Outstanding Balance (dollars in thousands) | Interest Earned/ Paid | Yield/ Rate | Average Outstanding Balance (dollars in thousands) | Interest Earned/ Paid | Yield/ Rate |
| ASSETS | | | | | | |
| Interest-earning assets: | | | | | | |
| Loans and leases, net | \$ 264,863 | \$ 14,749 | 7.42% | \$ 231,629 | \$ 11,721 | 6.75% |
| Taxable securities | 106,730 | 3,209 | 4.01% | 127,436 | 3,556 | 3.72% |
| Tax-exempt securities | 44,726 | 1,427 | 4.25% | 45,850 | 1,456 | 4.23% |
| Time deposits other banks | | | 0.00% | 287 | 3 | 1.39% |
| Federal funds sold | 958 | 35 | 4.87% | 6,801 | 109 | 2.14% |
| Total interest-earning assets | 417,277 | 19,420 | 6.21% | 412,003 | 16,845 | 5.45% |
| Non interest-earning assets: | | | | | | |
| Cash and due from banks | 12,428 | | | 10,191 | | |
| Premises and equipment, net | 8,174 | | | 8,214 | | |
| Other assets | 28,892 | | | 25,738 | | |
| Total Assets | \$ 466,771 | | | \$ 456,146 | | |
| LIABILITIES & STOCKHOLDERS | | | | | | |
| EQUITY | | | | | | |
| Interest-bearing liabilities: | | | | | | |
| NOW | \$ 11,726 | \$ 16 | 0.18% | \$ 12,056 | \$ 16 | 0.18% |
| Regular savings | 88,951 | 679 | 1.02% | 96,221 | 613 | 0.85% |
| Muni-Vest savings | 37,181 | 1,173 | 4.21% | 54,974 | 1,103 | 2.68% |
| Time deposits | 148,160 | 4,561 | 4.10% | 123,559 | 2,770 | 2.99% |
| Other borrowed funds | 50,275 | 1,464 | 3.88% | 48,607 | 1,118 | 3.07% |
| Junior subordinated debentures | 11,330 | 621 | 7.31% | 11,330 | 474 | 5.58% |
| Securities sold U/A to repurchase | 7,670 | 45 | 0.78% | 6,235 | 36 | 0.77% |
| Total interest-bearing liabilities | 355,293 | \$ 8,559 | 3.21% | 352,982 | \$ 6,130 | 2.32% |
| Noninterest-bearing liabilities: | | | | | | |
| Demand deposits | 66,130 | | | 60,843 | | |

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| | | |
|--------------------------------------|------------|------------|
| Other | 7,961 | 6,265 |
| Total liabilities | \$ 429,384 | \$ 420,090 |
| Stockholders equity | 37,387 | 36,056 |
| Total Liabilities and Equity | \$ 466,771 | \$ 456,146 |
| Net interest earnings | \$ 10,861 | \$ 10,715 |
| Net yield on interest earning assets | 3.47% | 3.47% |
| Interest rate spread | 3.00% | 3.13% |

Net Income

Net income was \$1.3 million or \$0.47 per basic and diluted share for the three months ended September 30, 2006, as compared to \$1.3 million or \$0.46 per basic and diluted share for the same period in 2005. Net income represented a return on average assets of 1.10% and 1.08% for the three month periods ended September 30, 2006 and 2005, respectively. The return on average equity was 13.55% and 13.61% for the three month periods ended September 30, 2006 and 2005, respectively.

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On a year-to-date basis, net income was \$3.8 million or \$1.38 per basic and diluted share for the nine months ended September 30, 2006, as compared to \$3.7 million or \$1.36 per basic and diluted share for the same period in 2005. Net income represented a return on average assets of 1.07% and 1.07% for the nine month periods ended September 30, 2006 and 2005, respectively. The return on average equity was 13.41% and 13.65% for the nine month periods ended September 30, 2006 and 2005, respectively.

Operating Results

Net interest income for the three month period ended September 30, 2006 was \$3.6 million, a decrease of \$0.1 million from the same period in 2005. Net interest income for the nine month period ended September 30, 2006 was 10.9 million, an increase of \$0.1 million from the same period in 2005. Significant growth in the Bank's loan and lease portfolio along with higher yields on loans and leases increased interest income in 2006 over 2005. Offsetting this increased interest income was increased interest expense on time deposits and short-term borrowings in the three and nine month periods ended September 30, 2006. Additionally, in the three and nine months ended September 30, 2005, the Company benefited from \$0.1 million in negotiated incremental interest income from a commercial loan paid off in 2005.

The net interest margin for the three and nine month periods ended September 30, 2006 was 3.50% and 3.47%, respectively, as compared to 3.59% and 3.47% for the same periods in 2005. The return on interest earning assets increased 79 basis points and 76 basis points in the three and nine month periods ended September 30, 2006, respectively mainly due to higher rates on loans and leases and a greater concentration of growth in leases, which tend to have higher rates. Interest free funds also contributed 53 basis points and 47 basis points in the three and nine month periods ended September 30, 2006, respectively, due to an increase in average demand deposits, compared to a 39 basis point and 34 basis point contribution in the same periods of 2005. This strong growth of loans and leases and demand deposits was offset by an increase in the Bank's cost of interest-bearing liabilities, which increased to 3.50% and 3.21% in the three and nine month periods ended September 30, 2006, respectively, from 2.48% and 2.32% in the same periods of 2005. The rise in short-term interest rates on federal funds purchased and time deposits, as a result of the Federal Reserve Bank Open Market Committee's policy decisions, were the primary drivers of this increase in cost of funds.

The provision for loan and lease losses for the three and nine month periods ended September 30, 2006 increased to \$305 thousand and \$815 thousand, respectively, from \$215 thousand and \$554 thousand for the same periods in 2005. The increase was a result of continued consumer and commercial loan and lease growth, particularly the Bank's expanding direct financing lease portfolio, through Evans National Leasing, which tends to have a higher credit risk than consumer loans and commercial loans collateralized by real estate.

Non-interest income was \$2.7 million for the three month period ended September 30, 2006, an increase of \$0.2 million or 8.9% from the same period in 2005. Non-interest income was \$8.4 million for the nine month period ended September 30, 2006, an increase of \$0.4 million or 4.8% from the same period of 2005. Gains on sales of securities of \$0.1 million, fee income on the expanding loan and lease portfolio, including \$0.1 million in commercial prepayment penalties, along with increased ATM and interchange fee revenue from an increased ATM network contributed to the increased non-interest income in the three and nine month periods ended September 30, 2006. In the nine month period ended September 30, 2006, increased insurance fee revenue of \$0.1 million was primarily the result of increased profit sharing revenue at ENBI in the first quarter of 2006. Partially offsetting these increases was a \$0.1 million decrease in life insurance proceeds which were received in the nine months ended September 2005, but not 2006.

Non interest expense was \$4.3 million for three month period ended September 30, 2006, which is comparable to the \$4.3 million in the same period of 2005. Non interest expense was \$13.3 million for nine month period ended September 30, 2006, an increase of \$0.2 million or 1.6% from the same period in 2005. Salary and employee benefit expense for the three and nine month periods ended September 30, 2006 increased \$0.1 million and \$0.4 million, respectively, from the same periods in 2005, due to Company growth, and merit pay increases awarded in early 2006. Occupancy, supplies, repair and maintenance, advertising, professional services, other insurance, and other miscellaneous expenses were relatively flat with or decreased during the three and nine month periods ended

September 30, 2006, due to cost cutting initiatives implemented during this difficult interest rate environment.

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Income tax expense totaled \$471 thousand and \$1.4 million for the three and nine month periods ended September 30, 2006, respectively, compared to \$498 and \$1.4 million for the same periods in 2005. The effective tax rate for the three and nine month periods ended September 30, 2006 was 26.9% and 27.5%, respectively, compared to 28.4% and 27.9% for the same periods in 2005. The decrease in effective tax rate in 2006 is primarily due to the higher composition of tax advantaged banking division income in the three and nine months ended September 30, 2006.

CAPITAL

The Bank has consistently maintained regulatory capital ratios at, or above, federal well capitalized standards. Equity as a percentage of assets was 8.1% at September 30, 2006, 8.0% at June 30, 2006 and 7.9% December 31, 2005. Book value per common share was \$14.23 at September 30, 2006, compared to \$13.65 at June 30, 2006 and \$13.51 at December 31, 2005. Total stockholders equity was \$38.7 million at September 30, 2006, up from \$37.2 million at June 30, 2006 and \$36.9 million at December 31, 2005. The increase is primarily attributable to net income of \$1.3 million and \$3.8 million in the three and nine month periods ended September 30, 2006, offset by \$1.0 million and \$1.9 million in dividends in the three and nine month periods ended September 30, 2006 and a decrease in unrealized losses in the investment portfolio of \$1.2 million in the three month period ended September 30, 2006.

LIQUIDITY

The Bank utilizes cash flows from the investment portfolio and federal funds sold balances to manage the liquidity requirements related to loan demand and deposit fluctuations. The Bank also has many borrowing options. As a member of the Federal Home Loan Bank (FHLB) the Bank is able to borrow funds at competitive rates. Advances of up to \$45.0 million can be drawn on the FHLB via an Overnight Line of Credit Agreement between the Bank and the FHLB. An amount equal to 25% of the Bank s total assets could be borrowed through the advance programs under certain qualifying circumstances. The Bank also has the ability to purchase up to \$14.0 million in federal funds from its correspondent banks. By placing sufficient collateral in safekeeping at the Federal Reserve Bank, the Bank could also borrow at the discount window. Additionally, the Company has access to capital markets as a funding source.

Cash flows from the Bank s investment portfolio are laddered, so that securities mature at regular intervals, to provide funds from principal and interest payments at various times as liquidity needs may arise. Contractual maturities are also laddered, with consideration as to the volatility of market prices, so that securities are available-for-sale from time-to-time without the need to incur significant losses. At September 30, 2006, approximately 7.1% of the Bank s securities had contractual maturity dates of one year or less and approximately 34.2% had maturity dates of five years or less. Available assets of \$141.2 million, less public and purchased funds of \$170.1 million, resulted in a long-term liquidity ratio of 83% at September 30, 2006, versus 76% at June 30, 2006 and 90% at December 31, 2005.

The Company s liquidity needs can also be met by more aggressively pursuing municipal deposits, which are normally awarded on the basis of competitive bidding. The Company believes that the Bank maintains a sufficient level of U.S. government and government agency securities and New York State municipal bonds that can be pledged as collateral for these deposits.

ITEM 3 QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Additional information responsive to this Item is contained in the Liquidity section of Management s Discussion and Analysis of Financial Condition and Results of Operations, which information is incorporated herein by reference.

Market risk is the risk of loss from adverse changes in market prices and/or interest rates of the Bank s financial instruments. The primary market risk the Company is exposed to is interest rate risk. The core banking activities of lending and deposit-taking expose the Bank to interest rate risk, which occurs when assets and liabilities reprice at different times and by different amounts as interest rates change. As a result, net interest income earned by

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the Bank is subject to the effects of changing interest rates. The Bank measures interest rate risk by calculating the variability of net interest income in the future periods under various interest rate scenarios using projected balances for interest-earning assets and interest-bearing liabilities. Management's philosophy toward interest rate risk management is to limit the variability of net interest income to changes in net interest rates. The balances of financial instruments used in the projections are based on expected growth from forecasted business opportunities, anticipated prepayments of loans, and investment securities and expected maturities of investment securities, loans and deposits. Management supplements the modeling technique described above with analysis of market values of the Bank's financial instruments and changes to such market values given changes in the interest rates.

The Bank's Asset Liability Committee, which includes members of senior management, monitors the Bank's interest rate sensitivity with the aid of a computer model that considers the impact of ongoing lending and deposit taking activities, as well as interrelationships in the magnitude and timing of the repricing of financial instruments, including the effect of changing interest rates on expected prepayments and maturities. When deemed prudent, management has taken actions, and intends to do so in the future, to mitigate exposure to interest rate risk through the use of on- or off-balance sheet financial instruments. Possible actions include, but are not limited to, changing the pricing of loan and deposit products, and modifying the composition of interest-earning assets and interest-bearing liabilities, and other financial instruments used for interest rate risk management purposes.

The following table demonstrates the possible impact of changes in interest rates on the Bank's net interest income over a 12 month period of time:

**SENSITIVITY OF NET INTEREST INCOME
TO CHANGES IN INTEREST RATES**

| | Calculated (decrease) increase in projected annual net interest income (in thousands) | |
|---------------------------|------------------------------------------------------------------------------------------------|----------------------|
| | September 30, 2006 | December 31, 2005 |
| Changes in interest rates | | |
| +200 basis points | (679) | (777) |
| +100 basis points | (338) | (386) |
| -100 basis points | 313 | 337 |
| -200 basis points | 449 | 542 |

Many assumptions were utilized by management to calculate the impact that changes in the interest rates may have on the Bank's net interest income. The more significant assumptions related to the rate of prepayments of mortgage-related assets, loan and deposit volumes and pricing, and deposit maturities. The Bank assumed immediate changes in rates including 200 basis point rate changes. In the event that the 200 basis point rate changes cannot be achieved, the applicable rate changes are limited to lesser amounts such that interest rates cannot be less than zero. These assumptions are inherently uncertain and, as a result, the Bank cannot precisely predict the impact of changes in interest rates on net interest income. Actual results may differ significantly due to the timing, magnitude, and frequency of interest rate changes in market conditions and interest rate differentials (spreads) between maturity/repricing categories, as well as any actions such as those previously described, which management may take to counter such changes. In light of the uncertainties and assumptions associated with the process, the amounts presented in the table and changes in such amounts are not considered significant to the Bank's projected net interest income.

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**ITEM 4 CONTROLS AND PROCEDURES
DISCLOSURE CONTROLS AND PROCEDURES**

The Company's management, with the participation of the Company's principal executive officer and principal financial officer, evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act). Based on that evaluation, the Company's principal executive and principal financial officers concluded that the Company's disclosure controls and procedures as of September 30, 2006 (the end of the period covered by this Report) have been designed and are functioning effectively to provide reasonable assurance that the information required to be disclosed by the Company in its reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms.

CHANGES IN INTERNAL CONTROL OVER FINANCIAL REPORTING

No changes in the Company's internal control over financial reporting were identified in the fiscal quarter ended September 30, 2006 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II OTHER INFORMATION**ITEM 2 UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS****Issuer Purchases of Equity Securities**

The following table includes all Company repurchases of its common stock, \$0.50 par value, made on a monthly basis during the period covered by this Report, including those made pursuant to publicly announced plans or programs.

| Period | Total number of shares purchased | Average price paid per share | Total number of shares purchased as part of publicly announced plans or programs | Maximum number of shares that may yet be purchased under the plans or programs |
|---------------------------------------------------------------|-------------------------------------------|---------------------------------------|----------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------|
| July 2006 (July 1, 2006 through July 31, 2006) | 1,200 | \$ 23.12 | 1,200 | 52,215 |
| August 2006 (August 1, 2006 through August 31, 2006) | 1,700 | \$ 21.37 | 1,700 | 50,515 |
| September 2006 (September 1, 2006 through September 30, 2006) | 1,800 | \$ 21.19 | 1,800 | 48,715 |
| Total | 4,700 | \$ 21.74 | 4,700 | |

All of the foregoing shares were purchased in open market transactions. On August 18, 2005, the Company announced that its Board of Directors authorized a common stock repurchase program, pursuant to which the Company may repurchase of up to 75,000 shares of the Company's common stock over the next two years, unless the program is terminated earlier. The Company did not make any repurchases during the quarter ended September

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30, 2006 other than pursuant to this publicly announced program, and there were no other publicly announced plans or programs outstanding during the quarter ended September 30, 2006.

ITEM 5 OTHER INFORMATION

Departure of Directors or Principal Officers; Election of Directors; Appointment of Principal Officers

Mr. James Tilley, president & chief executive officer of the Company was appointed by the Company's board of directors on November 2, 2006 to serve as the treasurer and principal financial officer of the Company until such time as the successor for Mark DeBacker, the Company's former treasurer and principal financial officer, has been identified, and is duly qualified and elected.

Amendments to Articles of Incorporation or Bylaws; Change in Fiscal Year

On November 2, 2006, the Board of Directors of the Company approved an amendment to the Company's bylaws to permit the issuance of shares of the Company's capital stock in book-entry form (uncertified form); specifically, Article VI, Section 601 and Section 602 of the Bylaws was amended. A copy of the Company's Bylaws as amended is attached as Exhibit 3.2.1 to this for 10Q and is incorporated herein by reference.

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| ITEM 6 EXHIBITS | | |
| Exhibit No. | Name | Page No. |
| 3.2.1 | Amended Bylaws of the Company | 30 |
| 31.1 | Certification of Principal Executive Officer pursuant to section 302 of The Sarbanes-Oxley Act of 2002. | 39 |
| 31.2 | Certification of the Principal Financial Officer pursuant to section 302 of The Sarbanes-Oxley Act of 2002. | 40 |
| 32.1 | Certification of Principal Executive Officer pursuant to 18 USC Section 1350 Chapter 63 of Title 18, United States Code, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. | 41 |
| 32.2 | Certification of Principal Financial Officer pursuant to 18 USC Section 1350 Chapter 63 of Title 18, United States Code, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. | 42 |

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SIGNATURES

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

Evans Bancorp, Inc.

DATE

November 7, 2006

/s/ James Tilley

James Tilley
President and CEO
(On Behalf of the Registrant and
as Principal Executive Officer)

DATE

November 7, 2006

/s/ James Tilley

James Tilley
Treasurer
(Principal Financial Officer)

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|-------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------|
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