

CASS INFORMATION SYSTEMS INC
Form 10-Q
August 04, 2011

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2011

OR

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

For the transition period from _____ to _____

Commission File No. 000-20827

CASS INFORMATION SYSTEMS, INC.

(Exact name of registrant as specified in its charter)

Missouri
(State or other jurisdiction of incorporation or
organization)

43-1265338
(I.R.S. Employer Identification No.)

13001 Hollenberg Drive
Bridgeton, Missouri
(Address of principal executive offices)

63044
(Zip Code)

(314) 506-5500
(Registrant's telephone number, including area code)

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

Yes X No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes X No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

TABLE OF CONTENTS

| | | |
|---|--|----|
| PART I – Financial Information | | |
| Item 1. | FINANCIAL STATEMENTS | |
| | Consolidated Balance Sheets June 30, 2011 (unaudited) and December 31, 2010 | 3 |
| | Consolidated Statements of Income Three and Six months ended June 30, 2011 and 2010 (unaudited) | 4 |
| | Consolidated Statements of Cash Flows Six months ended June 30, 2011 and 2010 (unaudited) | 5 |
| | Notes to Consolidated Financial Statements (unaudited) | 6 |
| Item 2. | MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS | 15 |
| Item 3. | QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK | 25 |
| Item 4. | CONTROLS AND PROCEDURES | 26 |
| PART II – Other Information– Items 1. – 6. | | 26 |
| SIGNATURES | | 27 |

Forward-looking Statements - Factors That May Affect Future Results

This report may contain or incorporate by reference forward-looking statements made pursuant to the safe harbor provisions of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Although we believe that, in making any such statements, our expectations are based on reasonable assumptions, forward-looking statements are not guarantees of future performance and involve risks, uncertainties, and other factors beyond our control, which may cause future performance to be materially different from expected performance summarized in the forward-looking statements. These risks, uncertainties and other factors are discussed in the section Part I, Item 1A, “Risk Factors” of the Company’s 2010 Annual Report on Form 10-K, filed with the Securities and Exchange Commission (“SEC”), which may be updated from time to time in our future filings with the SEC. We undertake no obligation to publicly update or revise any forward-looking statements to reflect changed assumptions, the occurrence of anticipated or unanticipated events, or changes to future results over time.

Edgar Filing: CASS INFORMATION SYSTEMS INC - Form 10-Q

PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

CASS INFORMATION SYSTEMS, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

(Dollars in Thousands except Share and Per Share Data)

| | June 30, 2011 (Unaudited) | December 31, 2010 |
|--|---------------------------------|----------------------|
| Assets | | |
| Cash and due from banks | \$ 10,489 | \$ 12,277 |
| Interest-bearing deposits in other financial institutions | 78,799 | 67,299 |
| Federal funds sold and other short-term investments | 114,844 | 59,353 |
| Cash and cash equivalents | 204,132 | 138,929 |
| Securities available-for-sale, at fair value | 264,218 | 264,569 |
| Loans | 718,786 | 708,633 |
| Less: Allowance for loan losses | 13,228 | 11,891 |
| Loans, net | 705,558 | 696,742 |
| Premises and equipment, net | 9,740 | 9,617 |
| Investment in bank-owned life insurance | 14,347 | 14,191 |
| Payments in excess of funding | 57,003 | 33,609 |
| Goodwill | 7,471 | 7,471 |
| Other intangible assets, net | 214 | 268 |
| Other assets | 25,015 | 22,639 |
| Total assets | \$ 1,287,698 | \$ 1,188,035 |
| Liabilities and Shareholders' Equity | | |
| Liabilities: | | |
| Deposits: | | |
| Noninterest-bearing | \$ 134,133 | \$ 113,097 |
| Interest-bearing | 387,579 | 405,493 |
| Total deposits | 521,712 | 518,590 |
| Accounts and drafts payable | 600,606 | 516,107 |
| Other liabilities | 13,300 | 11,244 |
| Total liabilities | 1,135,618 | 1,045,941 |
| Shareholders' Equity: | | |
| Preferred stock, par value \$.50 per share; 2,000,000 shares authorized and no shares issued | — | — |
| Common Stock, par value \$.50 per share; 20,000,000 shares authorized and 9,949,324 shares issued at June 30, 2011 and December 31, 2010 | 4,975 | 4,975 |
| Additional paid-in capital | 46,664 | 46,653 |
| Retained earnings | 115,710 | 107,263 |
| Common shares in treasury, at cost (533,767 shares at June 30, 2011 and 561,533 shares at December 31, 2010) | (12,995) | (13,549) |
| Accumulated other comprehensive loss | (2,274) | (3,248) |

Edgar Filing: CASS INFORMATION SYSTEMS INC - Form 10-Q

| | | |
|--|--------------|--------------|
| Total shareholders' equity | 152,080 | 142,094 |
| Total liabilities and shareholders' equity | \$ 1,287,698 | \$ 1,188,035 |

See accompanying notes to unaudited consolidated financial statements.

-3-

CASS INFORMATION SYSTEMS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

(Dollars in Thousands except Per Share Data)

| | Three Months Ended | | Six Months Ended | |
|--|--------------------|-----------|------------------|-----------|
| | June 30, | | June 30, | |
| | 2011 | 2010 | 2011 | 2010 |
| Fee Revenue and Other Income: | | | | |
| Information services payment and processing revenue | \$ 15,219 | \$ 13,533 | \$ 29,566 | \$ 26,278 |
| Bank service fees | 382 | 298 | 734 | 639 |
| Gains on sales of securities | 48 | — | 48 | — |
| Other | 134 | 137 | 267 | 276 |
| Total fee revenue and other income | 15,783 | 13,968 | 30,615 | 27,193 |
| Interest Income: | | | | |
| Interest and fees on loans | 10,129 | 9,871 | 20,382 | 19,298 |
| Interest and dividends on securities: | | | | |
| Taxable | 13 | 11 | 18 | 25 |
| Exempt from federal income taxes | 2,498 | 2,151 | 4,975 | 4,249 |
| Interest on federal funds sold and other short-term investments | 155 | 98 | 324 | 187 |
| Total interest income | 12,795 | 12,131 | 25,699 | 23,759 |
| Interest Expense: | | | | |
| Interest on deposits | 1,125 | 1,199 | 2,331 | 2,375 |
| Net interest income | 11,670 | 10,932 | 23,368 | 21,384 |
| Provision for loan losses | 850 | 1,150 | 1,300 | 2,050 |
| Net interest income after provision for loan losses | 10,820 | 9,782 | 22,068 | 19,334 |
| Total net revenue | 26,603 | 23,750 | 52,683 | 46,527 |
| Operating Expense: | | | | |
| Salaries and employee benefits | 14,146 | 12,683 | 27,852 | 25,173 |
| Occupancy | 557 | 611 | 1,205 | 1,183 |
| Equipment | 848 | 916 | 1,695 | 1,814 |
| Amortization of intangible assets | 27 | 27 | 54 | 54 |
| Other operating | 3,057 | 2,613 | 5,963 | 4,823 |
| Total operating expense | 18,635 | 16,850 | 36,769 | 33,047 |
| Income before income tax expense | 7,968 | 6,900 | 15,914 | 13,480 |
| Income tax expense | 2,229 | 2,000 | 4,456 | 3,831 |
| Net Income | \$ 5,739 | \$ 4,900 | \$ 11,458 | \$ 9,649 |
| Basic Earnings Per Share | .61 | .52 | 1.22 | 1.03 |
| Diluted Earnings Per Share | .61 | .52 | 1.21 | 1.02 |

See accompanying notes to unaudited consolidated financial statements.

CASS INFORMATION SYSTEMS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)
(Dollars in Thousands)

| | Six Months Ended June 30, | |
|--|------------------------------|------------|
| | 2011 | 2010 |
| Cash Flows From Operating Activities: | | |
| Net income | \$ 11,458 | \$ 9,649 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 2,228 | 2,068 |
| Gains on sales of securities | (48) | — |
| Provision for loan losses | 1,300 | 2,050 |
| Stock-based compensation expense | 700 | 746 |
| Decrease in income tax liability | (235) | (1,500) |
| Increase in pension liability | 231 | 397 |
| Other operating activities, net | (996) | 24 |
| Net cash provided by operating activities | 14,638 | 13,434 |
| Cash Flows From Investing Activities: | | |
| Proceeds from sales of securities available-for-sale | 5,405 | — |
| Proceeds from maturities of securities available-for-sale | 7,680 | 1,175 |
| Purchase of securities available-for-sale | (12,342) | (9,324) |
| Net increase in loans | (10,116) | (38,917) |
| Increase in payments in excess of funding | (23,394) | (12,163) |
| Purchases of premises and equipment, net | (1,143) | (529) |
| Net cash used in investing activities | (33,910) | (59,758) |
| Cash Flows From Financing Activities: | | |
| Net increase (decrease) in noninterest-bearing demand deposits | 21,036 | (3,460) |
| Net decrease in interest-bearing demand and savings deposits | (5,972) | (10,912) |
| Net (decrease) increase in time deposits | (11,942) | 40,930 |
| Net increase in accounts and drafts payable | 84,499 | 97,027 |
| Cash dividends paid | (3,011) | (2,629) |
| Distribution of stock awards, net | (249) | (251) |
| Other financing activities, net | 114 | 10 |
| Net cash provided by financing activities | 84,475 | 120,715 |
| Net increase in cash and cash equivalents | 65,203 | 74,391 |
| Cash and cash equivalents at beginning of period | 138,929 | 79,294 |
| Cash and cash equivalents at end of period | \$ 204,132 | \$ 153,685 |
| Supplemental information: | | |
| Cash paid for interest | \$ 2,342 | \$ 2,340 |
| Cash paid for income taxes | 4,135 | 5,350 |

See accompanying notes to unaudited consolidated financial statements.

CASS INFORMATION SYSTEMS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 1 - Basis of Presentation

The accompanying unaudited consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments, consisting of normal recurring accruals, considered necessary for a fair presentation have been included. Certain amounts in the 2010 consolidated financial statements have been reclassified to conform to the 2011 presentation. For further information, refer to the audited consolidated financial statements and related footnotes included in Cass Information System, Inc.'s ("the Company" or "Cass") Annual Report on Form 10-K for the year ended December 31, 2010.

Note 2 – Intangible Assets

The Company accounts for intangible assets in accordance with Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") 350, "Goodwill and Other Intangible Assets," which requires that intangibles with indefinite useful lives be tested annually for impairment and those with finite useful lives be amortized over their useful lives. Details of the Company's intangible assets are as follows:

| | June 30, 2011 | | December 31, 2010 | |
|--|-----------------------|--------------------------|-----------------------|--------------------------|
| | Gross Carrying Amount | Accumulated Amortization | Gross Carrying Amount | Accumulated Amortization |
| (In thousands) | | | | |
| Assets eligible for amortization: | | | | |
| Customer List | \$ 750 | \$ (536) | \$ 750 | \$ (482) |
| Unamortized intangible assets: | | | | |
| Goodwill | 7,698 | (227) | 7,698 | (227) |
| Total intangible assets | \$ 8,448 | \$ (763) | \$ 8,448 | \$ (709) |

The customer list is amortized over seven years. Amortization of intangible assets amounted to \$54,000 for both of the six-month periods ended June 30, 2011 and 2010. Estimated amortization of intangibles over the next five years is as follows: \$107,000 in 2011 and 2012 and \$54,000 in 2013.

Note 3 – Earnings Per Share

Basic earnings per share is computed by dividing net income by the weighted-average number of common shares outstanding. Diluted earnings per share is computed by dividing net income by the sum of the weighted-average number of common shares outstanding and the weighted-average number of potential common shares outstanding. There were no anti-dilutive shares in the three-month and six-month periods ended June 30, 2011 and 2010. The calculations of basic and diluted earnings per share are as follows:

| | Three Months Ended | | Six Months Ended | |
|--|--------------------|-----------|------------------|-----------|
| | June 30, 2011 | 2010 | June 30, 2011 | 2010 |
| (In thousands except share and per share data) | | | | |
| Basic | | | | |
| Net income | \$ 5,739 | \$ 4,900 | \$ 11,458 | \$ 9,649 |
| Weighted-average common shares outstanding | 9,360,724 | 9,334,847 | 9,358,694 | 9,331,789 |
| Basic earnings per share | \$.61 | \$.52 | \$ 1.22 | \$ 1.03 |
| Diluted | | | | |
| Net income | \$ 5,739 | \$ 4,900 | \$ 11,458 | \$ 9,649 |
| Weighted-average common shares outstanding | 9,360,724 | 9,334,847 | 9,358,694 | 9,331,789 |
| Effect of dilutive restricted stock, stock options and stock appreciation rights | 129,376 | 107,759 | 128,111 | 100,165 |

Edgar Filing: CASS INFORMATION SYSTEMS INC - Form 10-Q

| | | | | |
|---|-----------|-----------|-----------|-----------|
| Weighted-average common shares outstanding assuming dilution | 9,490,100 | 9,442,606 | 9,486,805 | 9,431,954 |
| Diluted earnings per share | \$.61 | \$.52 | \$ 1.21 | \$ 1.02 |

-6-

Note 4 – Stock Repurchases

The Company maintains a treasury stock buyback program pursuant to which the Board of Directors has authorized the repurchase of up to 300,000 shares of the Company's common stock. The Company did not repurchase any shares during the six-month periods ended June 30, 2011 and 2010. As of June 30, 2011, 168,000 shares remained available for repurchase under the program. Repurchases are made in the open market or through negotiated transactions from time to time depending on market conditions.

Note 5 – Comprehensive Income

For the three and six-month periods ended June 30, 2011 and 2010, unrealized gains and losses on securities available-for-sale and reclassification adjustments for gains included in net income were the Company's other comprehensive income components. Comprehensive income is summarized as follows:

| (In thousands) | Three Months Ended | | Six Months Ended | |
|---|--------------------|----------|------------------|-----------|
| | June 30, 2011 | 2010 | June 30, 2011 | 2010 |
| Net income | \$ 5,739 | \$ 4,900 | \$ 11,458 | \$ 9,649 |
| Other comprehensive income: | | | | |
| Reclassification adjustments for gains included in net income, net of tax | (31) | — | (31) | — |
| Net unrealized (loss) gain on securities available-for-sale, net of tax | 202 | (813) | 1,005 | 508 |
| Total comprehensive income | \$ 5,910 | \$ 4,087 | \$ 12,432 | \$ 10,157 |

Note 6 – Industry Segment Information

The services provided by the Company are classified into two reportable segments: Information Services and Banking Services. Each of these segments provides distinct services that are marketed through different channels. They are managed separately due to their unique service, processing and capital requirements.

The Information Services segment provides freight, utility and telecommunication invoice processing and payment services to large corporations. The Banking Services segment provides banking services primarily to privately-held businesses and churches.

The Company's accounting policies for segments are the same as those described in the summary of significant accounting policies in the Company's Annual Report on Form 10-K for the year ended December 31, 2010. Management evaluates segment performance based on net income after allocations for corporate expenses and income taxes. Transactions between segments are accounted for at what management believes to be fair value.

All revenue originates from and all long-lived assets are located within North America, and no revenue from any customer of any segment exceeds 10% of the Company's consolidated revenue.

Assets represent actual assets owned by Information Services and there is no allocation methodology used. Loans are sold by Banking Services to Information Services to create liquidity when the Bank's loan-to-deposit ratio is greater than 100%. Segment interest from customers is the actual interest earned on the loans owned by Information Services and Banking Services, respectively.

Edgar Filing: CASS INFORMATION SYSTEMS INC - Form 10-Q

Summarized information about the Company's operations in each industry segment is as follows:

| (In thousands) | Information Services | Banking Services | Corporate, Eliminations and other | Total |
|---|-------------------------|---------------------|---|-----------|
| Three Months Ended June 30, 2011 | | | | |
| Total Net Revenues: | | | | |
| Revenue from customers | \$ 20,690 | \$ 5,913 | \$ — | \$ 26,603 |
| Intersegment revenue | 2,473 | 484 | (2,957) | — |
| Net income | 3,710 | 2,029 | — | 5,739 |
| Goodwill | 7,335 | 136 | — | 7,471 |
| Other intangible assets, net | 214 | — | — | 214 |
| Total assets | 705,956 | 595,471 | (13,729) | 1,287,698 |
| Three Months Ended June 30, 2010 | | | | |
| Total Net Revenues: | | | | |
| Revenue from customers | \$ 18,551 | \$ 5,199 | \$ — | \$ 23,750 |
| Intersegment revenue | 1,984 | 413 | (2,397) | — |
| Net income | 3,353 | 1,547 | — | 4,900 |
| Goodwill | 7,335 | 136 | — | 7,471 |
| Other intangible assets, net | 321 | — | — | 321 |
| Total assets | 630,555 | 521,226 | (6,613) | 1,145,168 |
| Six Months Ended June 30, 2011 | | | | |
| Total Net Revenues: | | | | |
| Revenue from customers | \$ 40,536 | \$ 12,147 | \$ — | \$ 52,683 |
| Intersegment revenue | 5,099 | 941 | (6,040) | — |
| Net income | 7,262 | 4,196 | — | 11,458 |
| Goodwill | 7,335 | 136 | — | 7,471 |
| Other intangible assets, net | 214 | — | — | 214 |
| Total assets | 705,956 | 595,471 | (13,729) | 1,287,698 |
| Six Months Ended June 30, 2010 | | | | |
| Total Net Revenues: | | | | |
| Revenue from customers | \$ 35,779 | \$ 10,748 | \$ — | \$ 46,527 |
| Intersegment revenue | 4,259 | 793 | (5,052) | — |
| Net income | 6,257 | 3,392 | — | 9,649 |
| Goodwill | 7,335 | 136 | — | 7,471 |
| Other intangible assets, net | 321 | — | — | 321 |
| Total assets | 630,555 | 521,226 | (6,613) | 1,145,168 |

Note 7 – Loans by Type

A summary of loan categories by segment and class is as follows:

| (In thousands) | June 30, 2011 | December 31, 2010 |
|---------------------------------|---------------|----------------------|
| Commercial and industrial | \$ 161,099 | \$ 135,061 |
| Real estate: | | |
| Mortgage – Commercial | 134,787 | 151,201 |
| Mortgage – Church & related | 362,711 | 365,378 |
| Construction – Commercial | 15,454 | 18,434 |
| Construction – Church & related | 43,492 | 36,318 |

Edgar Filing: CASS INFORMATION SYSTEMS INC - Form 10-Q

| | | | | |
|--------------------------|----|---------|----|---------|
| Industrial revenue bonds | | 869 | | 1,014 |
| Other | | 374 | | 1,227 |
| Total loans | \$ | 718,786 | \$ | 708,633 |

The following tables present the aging of loans by loan classification at June 30, 2011 and December 31, 2010:

| (In thousands) | 30-59 Days | 60-89 Days | 90 Days and Over | Total Past Due | Current | Total Loans |
|---------------------------------|---------------|---------------|------------------------|----------------------|------------|----------------|
| June 30, 2011 | | | | | | |
| Commercial and industrial | \$ — | \$ 742 | \$ — | \$ 742 | \$ 160,357 | \$ 161,099 |
| Real estate: | | | | | | |
| Mortgage – Commercial | — | 1,059 | 463 | 1,522 | 133,265 | 134,787 |
| Mortgage – Church & related | 656 | — | — | 656 | 362,055 | 362,711 |
| Construction – Commercial | — | — | — | — | 15,454 | 15,454 |
| Construction – Church & related | — | — | — | — | 43,492 | 43,492 |
| Industrial revenue bonds | — | — | — | — | 869 | 869 |
| Other | — | — | — | — | 374 | 374 |
| Total | \$ 656 | \$ 1,801 | \$ 463 | \$ 2,920 | \$ 715,866 | \$ 718,786 |
| December 31, 2010 | | | | | | |
| Commercial and industrial | \$ 105 | \$ — | \$ — | \$ 105 | \$ 134,956 | \$ 135,061 |
| Real estate: | | | | | | |
| Mortgage – Commercial | 145 | — | 490 | 635 | 150,566 | 151,201 |
| Mortgage – Church & related | 1,954 | — | — | 1,954 | 363,424 | 365,378 |
| Construction – Commercial | — | — | — | — | 18,434 | 18,434 |
| Construction – Church & related | — | — | — | — | 36,318 | 36,318 |
| Industrial revenue bonds | — | — | — | — | 1,014 | 1,014 |
| Other | — | — | — | — | 1,227 | 1,227 |
| Total | \$ 2,204 | \$ — | \$ 490 | \$ 2,694 | \$ 705,939 | \$ 708,633 |

Edgar Filing: CASS INFORMATION SYSTEMS INC - Form 10-Q

The following tables present the recorded investment and unpaid principal balance for impaired loans at June 30, 2011 and December 31, 2010:

| (In thousands) | Recorded Investment | Unpaid Principal Balance | Related Allowance for Loan Losses |
|--|---------------------|--------------------------|-----------------------------------|
| June 30, 2011 | | | |
| Commercial and industrial: | | | |
| Nonaccrual | \$ 1,200 | \$ 1,200 | \$ 926 |
| Troubled debt restructurings continuing to accrue interest | 90 | 90 | 45 |
| Real estate – mortgage: | | | |
| Nonaccrual | 2,178 | 2,178 | 130 |
| Troubled debt restructurings continuing to accrue interest | 4,396 | 4,396 | 766 |
| Total impaired loans | \$ 7,864 | \$ 7,864 | \$ 1,867 |
| December 31, 2010 | | | |
| Commercial and industrial: | | | |
| Nonaccrual | \$ 46 | \$ 46 | \$ 4 |
| Real estate – mortgage: | | | |
| Nonaccrual | 519 | 519 | 116 |
| Total impaired loans | \$ 565 | \$ 565 | \$ 120 |

Impaired loans consist primarily of nonaccrual loans, loans greater than 90 days past due and still accruing interest, and troubled debt restructurings continuing to accrue interest. Management measures impairment in accordance with FASB ASC 310, “Allowance for Credit Losses.” At June 30, 2011 and December 31, 2010, all impaired loans were evaluated based on the fair value of the collateral. The fair value of the collateral is based upon an observable market price or current appraised value and therefore, the Company classifies these assets as nonrecurring Level 2. There were no loans delinquent 90 days or more and still accruing interest at June 30, 2011 and December 31, 2010. At June 30, 2011 there were two loans totaling \$4,486,000 classified as troubled debt restructurings, with a total pre-modification loan balance of \$4,486,000. There were no troubled debt restructurings at December 31, 2010. There are two foreclosed loans with a book value of \$1,910,000 which have been reclassified as other real estate owned (included in other assets) as of June 30, 2011 and December 31, 2010.

The following table presents the credit exposure of the loan portfolio by internally assigned credit grade as of June 30, 2011 and December 31, 2010:

| (In thousands) | Commercial and Industrial | Real Estate Mortgage | Real Estate Construction | Other | Total |
|---|---------------------------|----------------------|--------------------------|-----------------|-------------------|
| June 30, 2011 | | | | | |
| Loans subject to normal monitoring ¹ | \$ 156,629 | \$ 468,047 | \$ 58,946 | \$ 1,243 | \$ 684,865 |
| Loans subject to special monitoring²: | | | | | |
| Performing | 3,270 | 27,273 | — | — | 30,543 |
| Nonperforming | 1,200 | 2,178 | — | — | 3,378 |
| Total | \$ 161,099 | \$ 497,498 | \$ 58,946 | \$ 1,243 | \$ 718,786 |
| December 31, 2010 | | | | | |
| Loans subject to normal monitoring ¹ | \$ 130,148 | \$ 495,573 | \$ 54,752 | \$ 2,241 | \$ 682,714 |
| Loans subject to special monitoring²: | | | | | |
| Performing | 4,867 | 20,487 | — | — | 25,354 |
| Nonperforming | 46 | 519 | — | — | 565 |
| Total | \$ 135,061 | \$ 516,579 | \$ 54,752 | \$ 2,241 | \$ 708,633 |

- Loans subject to normal monitoring involve borrowers of acceptable-to-strong credit quality and risk, who have the apparent ability to satisfy their loan obligation.
- Loans subject to special monitoring possess some credit deficiency or potential weakness which requires a high level of management attention.

Edgar Filing: CASS INFORMATION SYSTEMS INC - Form 10-Q

The following table provides information regarding the changes in the allowance for loan losses by segment from December 31, 2010 to June 30, 2011:

| (In thousands) | December 31, 2010 | Charge -Offs | Recoveries | Provision | June 30, 2011 |
|----------------------------|-------------------------|-----------------|------------|-----------|------------------|
| Commercial and industrial | \$ 2,728 | — | \$ 36 | \$ 1,040 | \$ 3,804 |
| Real estate - mortgage | 8,491 | — | 1 | 230 | 8,722 |
| Real estate - construction | 656 | — | — | 40 | 696 |
| Other | 16 | — | — | (10) | 6 |
| Total | \$ 11,891 | — | \$ 37 | \$ 1,300 | \$ 13,228 |

Note 8 – Commitments and Contingencies

In the normal course of business, the Company is party to activities that contain credit, market and operational risks that are not reflected in whole or in part in the Company's consolidated financial statements. Such activities include traditional off-balance sheet credit-related financial instruments and commitments under operating leases. These financial instruments include commitments to extend credit, commercial letters of credit and standby letters of credit. The Company's maximum potential exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit, commercial letters of credit and standby letters of credit is represented by the contractual amounts of those instruments. At June 30, 2011 and December 31, 2010, no amounts have been accrued for any estimated losses for these instruments.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commercial and standby letters of credit are conditional commitments issued by the Company or its subsidiaries to guarantee the performance of a customer to a third party. These off-balance sheet financial instruments generally have fixed expiration dates or other termination clauses and may require payment of a fee. At June 30, 2011, the balance of unused loan commitments, standby and commercial letters of credit were \$16,451,000, \$21,752,000 and \$4,030,000, respectively. Since some of the financial instruments may expire without being drawn upon, the total amounts do not necessarily represent future cash requirements. Commitments to extend credit and letters of credit are subject to the same underwriting standards as those financial instruments included on the consolidated balance sheets. The Company evaluates each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary upon extension of the credit, is based on management's credit evaluation of the borrower. Collateral held varies, but is generally accounts receivable, inventory, residential or income-producing commercial property or equipment. In the event of nonperformance, the Company or its subsidiaries may obtain and liquidate the collateral to recover amounts paid under its guarantees on these financial instruments.

The following table summarizes contractual cash obligations of the Company related to operating lease commitments and time deposits at June 30, 2011:

| (In thousands) | Amount of Commitment Expiration per Period | | | | |
|-----------------------------|--|---------------------|--------------|--------------|-----------------|
| | Total | Less than 1 Year | 1-3 Years | 3-5 Years | Over 5 Years |
| Operating lease commitments | \$ 2,579 | \$ 608 | \$ 1,032 | \$ 592 | \$ 347 |
| Time deposits | 145,176 | 126,877 | 15,678 | 2,621 | — |
| Total | \$ 147,755 | \$ 127,485 | \$ 16,710 | \$ 3,213 | \$ 347 |

The Company and its subsidiaries are involved in various pending legal actions and proceedings in which claims for damages are asserted. Management, after discussion with legal counsel, believes the ultimate resolution of these legal actions and proceedings will not have a material effect upon the Company's consolidated financial position or results of operations.

Note 9 – Stock-Based Compensation

In 2007, the Board and the Company's shareholders approved the 2007 Omnibus Incentive Stock Plan (the "Omnibus Plan"). The Omnibus Plan permits the issuance of up to 880,000 shares of the Company's common stock in the form of stock options, stock appreciation rights ("SARs"), restricted stock, restricted stock units and performance awards. The Company issues shares out of treasury stock for these awards. During the six months ended June 30, 2011, 26,017 restricted shares and 75,016 SARs were granted under the Omnibus Plan.

Edgar Filing: CASS INFORMATION SYSTEMS INC - Form 10-Q

The Company also maintains its other stock-based incentive plans for the restricted common stock previously awarded and the options previously issued and still outstanding. These plans have been superseded by the Omnibus Plan and accordingly, any available restricted stock and stock option grants not yet issued have been cancelled.

Restricted Stock

Restricted shares are amortized to expense over the three-year vesting period. As of June 30, 2011, the total unrecognized compensation expense related to non-vested common stock was \$1,287,000 and the related weighted-average period over which it is expected to be recognized is approximately 1.5 years.

Following is a summary of the activity of the restricted stock:

| | Six Months Ended | |
|------------------------------|------------------|------------|
| | June 30, 2011 | |
| | Shares | Fair Value |
| Balance at December 31, 2010 | 50,271 | \$ 28.51 |
| Granted | 26,017 | 36.35 |
| Vested | (28,580) | 28.43 |
| Balance at June 30, 2011 | 47,708 | \$ 32.84 |

Stock Options

Stock options vest and expire over a period not to exceed seven years. As of June 30, 2011, the total unrecognized compensation expense related to non-vested stock options was \$22,000, and the related weighted-average period over which it is expected to be recognized is approximately 1.6 years. Following is a summary of the activity of the stock options during the six-month period ended June 30, 2011:

| | Shares | Weighted-Average Exercise Price | Average Remaining Contractual Term Years | Aggregate Intrinsic Value (In thousands) |
|----------------------------------|---------|---------------------------------|--|--|
| Outstanding at December 31, 2010 | 36,628 | \$ 18.36 | 1.56 | \$ 717 |
| Exercised | (6,584) | 14.47 | | |
| Outstanding at June 30, 2011 | 30,044 | 19.21 | 1.29 | \$ 557 |
| Exercisable at June 30, 2011 | 26,704 | \$ 19.03 | 1.26 | \$ 500 |

The total intrinsic value of options exercised was \$156,000 and \$60,000 for the six-month periods ended June 30, 2011 and 2010, respectively. Following is a summary of the activity of the non-vested stock options during the six-month period ended June 30, 2011:

| | Shares | Weighted-Average Grant Date Fair Value |
|---------------------------------|---------|--|
| Non-vested at December 31, 2010 | 12,440 | \$ 2.94 |
| Vested | (9,100) | 2.93 |
| Non-vested at June 30, 2011 | 3,340 | \$ 2.95 |

SARs

SARs vest over a three-year period, with one-third of the shares vesting and becoming exercisable each year on the anniversary date of the grant, and they expire 10 years from the original grant date. As of June 30, 2011, the total unrecognized compensation expense was \$902,000 and the related weighted-average period over which it is expected to be recognized is 1.4 years. Following is a summary of the activity of the Company's SARs program for the six-month period ended June 30, 2011:

| | Weighted-Average | Average Remaining | Aggregate Intrinsic |
|--|------------------|-------------------|---------------------|
|--|------------------|-------------------|---------------------|

Edgar Filing: CASS INFORMATION SYSTEMS INC - Form 10-Q

| | Shares | Exercise Price | Contractual Term Years | Value (In thousands) |
|----------------------------------|----------|----------------|------------------------|----------------------|
| Outstanding at December 31, 2010 | 241,755 | \$ 27.34 | 7.38 | \$ 2,562 |
| Granted | 75,016 | 36.24 | | |
| Exercised | (14,396) | 12.20 | | |
| Outstanding at June 30, 2011 | 302,375 | \$ 29.55 | 7.93 | \$ 2,481 |
| Exercisable at June 30, 2011 | 171,158 | \$ 27.47 | 4.07 | \$ 1,762 |

-11-

Edgar Filing: CASS INFORMATION SYSTEMS INC - Form 10-Q

Following is a summary of the activity of the non-vested SARs during the six-month period ended June 30, 2011:

| | Shares | Weighted Average Grant Date Fair Value |
|---------------------------------|----------|---|
| Non-vested at December 31, 2010 | 141,201 | \$ 27.18 |
| Granted | 75,016 | 36.24 |
| Vested | (85,000) | 27.36 |
| Non-vested at June 30, 2011 | 131,217 | \$ 32.28 |

The Company uses the Black-Scholes pricing model to determine the fair value of the SARs at the date of grant. Following are the assumptions used to estimate the per-share fair value of SARs granted:

| | Six Months Ended June 30, | |
|-------------------------|------------------------------|--------|
| | 2011 | 2010 |
| Risk free interest rate | 2.70% | 3.33% |
| Expected life | 7 yrs. | 7 yrs. |
| Expected volatility | 27.86% | 30.00% |
| Expected dividend yield | 1.77% | 1.86% |

The risk-free interest rate is based on the zero-coupon U.S. Treasury yield for the period equal to the expected life of the SARs at the time of the grant. The expected life was derived using the historical exercise activity. The Company uses historical volatility for a period equal to the expected life of the rights using average monthly closing market prices of the Company's stock as reported on The Nasdaq Global Market. The expected dividend yield is based on the Company's current rate of annual dividends.

Note 10 – Defined Pension Plans

The Company has a noncontributory defined benefit pension plan, which covers most of its employees. The Company accrues and makes contributions designed to fund normal service costs on a current basis using the projected unit credit with service proration method to amortize prior service costs arising from improvements in pension benefits and qualifying service prior to the establishment of the plan over a period of approximately 30 years. Disclosure information is based on a measurement date of December 31 of the corresponding year. The following table represents the components of the net periodic pension costs:

| (In thousands) | Estimated | Actual |
|--|-----------|----------|
| | 2011 | 2010 |
| Service cost – benefits earned during the year | \$ 2,079 | \$ 1,771 |
| Interest cost on projected benefit obligation | 2,457 | 2,290 |
| Expected return on plan assets | (3,314) | (2,440) |
| Net amortization | 642 | 616 |
| Net periodic pension cost | \$ 1,864 | \$ 2,237 |

Pension costs recorded to expense related to the noncontributory defined benefit pension plan were \$466,000 and \$542,000 for the three-month periods ended June 30, 2011 and 2010, respectively, and totaled \$932,000 and \$1,084,000 for the six-month periods ended June 30, 2011 and 2010, respectively. The Company made a contribution of \$450,000 to the plan during the three-month period ended June 30, 2011, for a total of \$900,000 for the six-month period ending June 30, 2011 and expects to contribute at least an additional \$900,000 in 2011.

In addition to the above funded benefit plan, the Company has an unfunded supplemental executive retirement plan which covers key executives of the Company. This is a noncontributory plan in which the Company and its subsidiaries make accruals designed to fund normal service costs on a current basis using the same method and criteria as its defined benefit plan. The following table represents the components of the net periodic pension costs for 2010 and an estimate for 2011:

Estimated Actual

Edgar Filing: CASS INFORMATION SYSTEMS INC - Form 10-Q

| (In thousands) | 2011 | 2010 |
|--|--------|--------|
| Service cost – benefits earned during the year | \$ 90 | \$ 78 |
| Interest cost on projected benefit obligation | 295 | 315 |
| Net amortization | 249 | 258 |
| Net periodic pension cost | \$ 634 | \$ 651 |

-12-

Edgar Filing: CASS INFORMATION SYSTEMS INC - Form 10-Q

Pension costs recorded to expense related to the unfunded supplemental executive retirement plan were \$159,000 and \$168,000 for the three-month periods ended June 30, 2011 and 2010, respectively, and were \$317,000 and \$330,000 for the six-month periods ended June 30, 2011 and 2010, respectively.

Note 11 – Income Taxes

As of June 30, 2011, the Company’s unrecognized tax benefits were approximately \$2,155,000, of which \$1,671,000 would, if recognized, affect the Company’s effective tax rate. As of December 31, 2010, the Company’s unrecognized tax benefits were approximately \$1,877,000, of which \$1,465,000 would, if recognized, affect the Company’s effective tax rate. During the next twelve months, the Company may realize a reduction of its unrecognized tax benefits of approximately \$451,000 due to the lapse of federal and state statutes of limitations.

The Company recognizes interest and penalties related to uncertain tax positions in income tax expense. The Company had \$135,000 and \$106,000 of gross interest accrued as of June 30, 2011 and December 31, 2010, respectively. There were no penalties for unrecognized tax benefits accrued at June 30, 2011 and December 31, 2010.

The Company is subject to income tax in the U.S. federal jurisdiction and numerous state jurisdictions. U.S. federal income tax returns for tax years 2007 through 2009 remain subject to examination by the Internal Revenue Service. In addition, the Company is subject to state tax examinations for the tax years 2006 through 2009.

Note 12 – Investment Securities Available for Sale

Investment securities available-for-sale are recorded at fair value on a recurring basis. The Company’s investment securities available-for-sale are measured at fair value using Level 2 valuations. The market evaluation utilizes several sources which include “observable inputs” rather than “significant unobservable inputs” and therefore falls into the Level 2 category. The amortized cost, gross unrealized gains, gross unrealized losses and fair value of investment securities are summarized as follows:

| (In thousands) | June 30, 2011 | | | |
|----------------------------------|----------------|------------------------|-------------------------|------------|
| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
| State and political subdivisions | \$ 254,080 | \$ 10,953 | \$ 815 | \$ 264,218 |

| (In thousands) | December 31, 2010 | | | |
|----------------------------------|-------------------|------------------------|-------------------------|------------|
| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
| State and political subdivisions | \$ 255,929 | \$ 9,829 | \$ 1,189 | \$ 264,569 |

The fair values of securities with unrealized losses are as follows:

| (In thousands) | June 30, 2011 | | | | | |
|----------------------------------|----------------------|-------------------|----------------------|-------------------|----------------------|-------------------|
| | Less than 12 months | | 12 months or more | | Total | |
| | Estimated fair value | Unrealized losses | Estimated fair value | Unrealized losses | Estimated Fair value | Unrealized losses |
| State and political subdivisions | \$ 40,163 | \$ 815 | \$ — | \$ — | \$ 40,163 | \$ 815 |

| (In thousands) | December 31, 2010 | | | | | |
|----------------------------------|----------------------|-------------------|----------------------|-------------------|----------------------|-------------------|
| | Less than 12 months | | 12 months or more | | Total | |
| | Estimated fair value | Unrealized losses | Estimated fair value | Unrealized losses | Estimated Fair value | Unrealized losses |
| State and political subdivisions | \$ 40,163 | \$ 815 | \$ — | \$ — | \$ 40,163 | \$ 815 |

Edgar Filing: CASS INFORMATION SYSTEMS INC - Form 10-Q

| (In thousands) | fair value | losses | fair value | losses | Fair value | losses |
|----------------------------------|------------|----------|------------|--------|------------|----------|
| State and political subdivisions | \$ 53,741 | \$ 1,189 | \$ — | \$ — | \$ 53,741 | \$ 1,189 |

-13-

Edgar Filing: CASS INFORMATION SYSTEMS INC - Form 10-Q

There were 47 securities (none greater than 12 months) in an unrealized loss position as of June 30, 2011. There were 61 securities (none greater than 12 months) in an unrealized loss position as of December 31, 2010. All unrealized losses were reviewed to determine whether the losses were other than temporary. Management believes that all unrealized losses are temporary since they were market driven, and the Company has the ability and intent to hold these securities until recovery.

The amortized cost and fair value of investment securities by contractual maturity are shown in the following table. Expected maturities may differ from contractual maturities because borrowers have the right to prepay obligations with or without prepayment penalties.

| (In thousands) | June 30, 2011 | |
|------------------------------------|-------------------|------------|
| | Amortized Cost | Fair Value |
| Due in 1 year or less | \$ 14,362 | \$ 14,567 |
| Due after 1 year through 5 years | 38,718 | 41,212 |
| Due after 5 years through 10 years | 96,902 | 104,003 |
| Due after 10 years | 104,098 | 104,436 |
| Total | \$ 254,080 | \$ 264,218 |

There were no securities pledged to secure public deposits and for other purposes at June 30, 2011.

Proceeds from sales of investment securities classified as available for sale were \$4,904,000 and \$0 for the three months ended June 30, 2011 and 2010, respectively, and were \$5,405,000 and \$0 for the six months ended June 30, 2011 and 2010, respectively. Gross realized gains were \$48,000 and \$0 for the three months ended June 30, 2011 and 2010, respectively, and were \$48,000 and \$0 for the six months ended June 30, 2011 and 2010, respectively.

Note 13 – Fair Value of Financial Instruments

Following is a summary of the carrying amounts and fair values of the Company's financial instruments:

| (In thousands) | June 30, 2011 | | December 31, 2010 | |
|-----------------------------------|--------------------|--------------|--------------------|--------------|
| | Carrying Amount | Fair Value | Carrying Amount | Fair Value |
| Balance sheet assets: | | | | |
| Cash and cash equivalents | \$ 204,132 | \$ 204,132 | \$ 138,929 | \$ 138,929 |
| Investment securities | 264,218 | 264,218 | 264,569 | 264,569 |
| Loans, net | 705,558 | 712,111 | 696,742 | 710,294 |
| Accrued interest receivable | 5,866 | 5,866 | 5,857 | 5,857 |
| Total | \$ 1,179,774 | \$ 1,186,327 | \$ 1,106,097 | \$ 1,119,649 |
| Balance sheet liabilities: | | | | |
| Deposits | \$ 521,712 | \$ 521,712 | \$ 518,590 | \$ 518,590 |
| Accounts and drafts payable | 600,606 | 600,606 | 516,107 | 516,107 |
| Short-term borrowings | — | — | 9 | 9 |
| Accrued interest payable | 197 | 197 | 208 | 208 |
| Total | \$ 1,122,515 | \$ 1,122,515 | \$ 1,034,914 | \$ 1,034,914 |

The following methods and assumptions were used to estimate the fair value of each class of financial instruments for which it is practicable to estimate that value:

Cash and Other Short-term Instruments – For cash and cash equivalents, accrued interest receivable, accounts and drafts payable, short-term borrowings and accrued interest payable, the carrying amount is a reasonable estimate of fair value because of the demand nature or short maturities of these instruments.

Edgar Filing: CASS INFORMATION SYSTEMS INC - Form 10-Q

Loans – The fair value of loans is estimated by discounting the future cash flows using the current rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities.

Deposits – The fair value of demand deposits, savings deposits and certain money market deposits is the amount payable on demand at the reporting date. The fair value of fixed-maturity certificates of deposit is estimated using the rates currently offered for deposits of similar remaining maturities. The fair value estimates above do not include the benefit that results from the low-cost funding provided by the deposit liabilities compared to the cost of borrowing funds in the market or the benefit derived from the customer relationship inherent in existing deposits.

-14-

Note 14 – Subsequent Events

In accordance with FASB ASC 855, “Subsequent Events,” the Company has evaluated subsequent events after the consolidated balance sheet date of June 30, 2011 and there were no events identified that would require additional disclosures to prevent the Company’s consolidated financial statements from being misleading.

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

Overview

Cass provides payment and information processing services to large manufacturing, distribution and retail enterprises from its processing centers in St. Louis, Missouri, Columbus, Ohio, Boston, Massachusetts, Greenville, South Carolina and Wellington, Kansas. The Company’s services include freight invoice rating, payment processing, auditing, and the generation of accounting and transportation information. Cass also processes and pays utility invoices, which include electricity, gas and telecommunications expenses and is a provider of telecom expense management solutions. Cass extracts, stores, and presents information from freight, utility and telecommunication invoices, assisting its customers’ transportation, energy and information technology managers in making decisions that will enable them to improve operating performance. The Company receives data from multiple sources, electronic and otherwise, and processes the data to accomplish the specific operating requirements of its customers. It then provides the data in a central repository for access and archiving. The data is finally transformed into information through the Company’s databases that allow client interaction as required and provides Internet-based tools for analytical processing. The Company also, through Cass Commercial Bank, its St. Louis, Missouri based bank subsidiary (the “Bank”), provides banking services in the St. Louis metropolitan area, Orange County, California and other selected cities in the United States. In addition to supporting the Company’s payment operations, the Bank provides banking services to its target markets, which include privately-owned businesses and churches and church-related ministries.

The specific payment and information processing services provided to each customer are developed individually to meet each customer’s requirements, which can vary greatly. In addition, the degree of automation such as electronic data interchange, imaging, and web-based solutions varies greatly among customers and industries. These factors combine so that pricing varies greatly among the customer base. In general, however, Cass is compensated for its processing services through service fees and investment of account balances generated during the payment process. The amount, type and calculation of service fees vary greatly by service offering, but generally follow the volume of transactions processed. Interest income from the balances generated during the payment processing cycle is affected by the amount of time Cass holds the funds prior to payment and the dollar volume processed. Both the number of transactions processed and the dollar volume processed are therefore key metrics followed by management. Other factors will also influence revenue and profitability, such as changes in the general level of interest rates, which have a significant effect on net interest income. The funds generated by these processing activities are invested in overnight investments, investment grade securities and loans generated by the Bank. The Bank earns most of its revenue from net interest income, or the difference between the interest earned on its loans and investments and the interest paid on its deposits and other borrowings. The Bank also assesses fees on other services such as cash management services.

Industry-wide factors that impact the Company include the willingness of large corporations to outsource key business functions such as freight, utility and telecommunication payment and audit. The benefits that can be achieved by outsourcing transaction processing and the management information generated by Cass’ systems can be influenced by factors such as the competitive pressures within industries to improve profitability, the general level of transportation costs, deregulation of energy costs and consolidation of telecommunication providers. Economic factors that impact the Company include the general level of economic activity that can affect the volume and size of invoices processed, the ability to hire and retain qualified staff, and the growth and quality of the loan portfolio. As lower levels of economic activity are encountered the number and total dollar amount of transactions processed by the Company may decline, thereby reducing fee revenue, interest income, and possibly liquidity. Conversely, improving economic conditions will tend to increase fee revenue, interest income and liquidity. The general level of interest rates also has a significant effect on the revenue of the Company. As discussed in greater detail in Item 7A, “Quantitative and Qualitative Disclosures about Market Risk,” in the Company’s 2010 Annual Report on Form 10-K, a decline in the general level of interest rates can have a negative impact on net interest income.

Currently, management views Cass' major opportunity as the continued expansion of its payment and information processing service offering and customer base. Management intends to accomplish this by maintaining the Company's lead in applied technology, which when combined with the security and processing controls of the Bank, makes Cass unique in the industry.

Critical Accounting Policies

The Company has prepared the consolidated financial statements in this report in accordance with the FASB Accounting Standards Codification ("ASC"). In preparing the consolidated financial statements, management makes estimates and assumptions that affect the reported amount of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenses during the reporting period. These estimates have been generally accurate in the past, have been consistent and have not required any material changes. There can be no assurances that actual results will not differ from those estimates. Certain accounting policies that require significant management estimates and are deemed critical to our results of operations or financial position have been discussed with the Audit Committee of the Board of Directors and are described below.

Allowance for Loan Losses. The Company performs periodic and systematic detailed reviews of its loan portfolio to assess overall collectability. The level of the allowance for loan losses reflects management's estimate of the collectability of the loan portfolio. Although these estimates are based on established methodologies for determining allowance requirements, actual results can differ significantly from estimated results. These policies affect both segments of the Company. The impact and associated risks related to these policies on the Company's business operations are discussed in the "Provision and Allowance for Loan Losses" section of this report. The Company's estimates have been materially accurate in the past, and accordingly, we expect to continue to utilize the present processes.

Impairment of Assets. The Company periodically evaluates certain long-term assets such as intangible assets including goodwill, foreclosed assets and assets held for sale for impairment. Generally, these assets are initially recorded at cost, and recognition of impairment is required when events and circumstances indicate that the carrying amounts of these assets will not be recoverable in the future. If impairment occurs, various methods of measuring impairment may be called for depending on the circumstances and type of asset, including quoted market prices, estimates based on similar assets, and estimates based on valuation techniques such as discounted projected cash flows. The Company had no impairment of goodwill and intangible assets for the three or six-month periods ended June 30, 2011 or for the fiscal year ended December 31, 2010, and management does not anticipate any future impairment loss. Investment securities available-for-sale are measured at fair value as calculated by an independent research firm. The market evaluation utilizes several sources which include "observable inputs" rather than "significant unobservable inputs." These policies affect both segments of the Company and require significant management assumptions and estimates that could result in materially different results if conditions or underlying circumstances change.

Income Taxes. The objectives of accounting for income taxes are to recognize the amount of taxes payable or refundable for the current year and deferred tax liabilities and assets for the future tax consequences of events that have been recognized in an entity's financial statements or tax returns. Judgment is required in addressing the future tax consequences of events that have been recognized in the Company's financial statements or tax returns such as the realization of deferred tax assets or changes in tax laws or interpretations thereof. In addition, the Company is subject to the continuous examination of its income tax returns by the Internal Revenue Service and other taxing authorities. In accordance with FASB ASC 740, "Income Taxes," the Company has unrecognized tax benefits related to tax positions taken or expected to be taken. See Note 11 to the financial statements.

Pension Plans. The amounts recognized in the consolidated financial statements related to pension plans are determined from actuarial valuations. Inherent in these valuations are assumptions, including expected return on plan assets, discount rates at which the liabilities could be settled at December 31, 2010, rate of increase in future compensation levels and mortality rates. These assumptions are updated annually and are disclosed in Note 10 to the consolidated financial statements filed with the Company's Annual Report on Form 10-K for the year ended December 31, 2010. There have been no significant changes in the Company's long-term rate of return assumptions for the past three fiscal years ended December 31 and management believes they are not reasonably likely to change in the future. Pursuant to FASB ASC 715, "Compensation - Retirement Benefits," the Company has recognized the funded status of its defined benefit postretirement plan in its balance sheet and has recognized changes in that funded status through comprehensive income. The funded status is measured as the difference between the fair value of the plan assets and the projected benefit obligation as of the date of its fiscal year-end.

Results of Operations

The following paragraphs more fully discuss the results of operations and changes in financial condition for the three-month period ended June 30, 2011 (“Second Quarter of 2011”) compared to the three-month period ended June 30, 2010 (“Second Quarter of 2010”) and the six-month period ended June 30, 2011 (“First Half of 2011”) compared to the six-month period ended June 30, 2010 (“First Half of 2010”). The following discussion and analysis should be read in conjunction with the consolidated financial statements and related notes and with the statistical information and financial data appearing in this report, as well as in the Company’s 2010 Annual Report on Form 10-K. Results of operations for the Second Quarter of 2011 are not necessarily indicative of the results to be attained for any other period.

Net Income

The following table summarizes the Company’s operating results:

| (In thousands except per share data) | Second Quarter of | | | First Half of | | |
|--------------------------------------|-------------------|----------|-------------|---------------|----------|-------------|
| | 2011 | 2010 | % Change | 2011 | 2010 | % Change |
| Net income | \$ 5,739 | \$ 4,900 | 17.1% | \$ 11,458 | \$ 9,649 | 18.7% |
| Diluted earnings per share | \$.61 | \$.52 | 17.3% | \$ 1.21 | \$ 1.02 | 18.6% |
| Return on average assets | 1.83% | 1.77% | — | 1.85% | 1.78% | — |
| Return on average equity | 15.53% | 14.62% | — | 15.87% | 14.66% | — |

Fee Revenue and Other Income

The Company’s fee revenue is derived mainly from transportation and utility processing and payment fees. As the Company provides its processing and payment services, it is compensated by service fees which are typically calculated on a per-item basis and by the accounts and drafts payable balances generated in the payment process which can be used to generate interest income. Processing volumes related to fees and accounts and drafts payable were as follows:

| (In thousands except per share data) | Second Quarter of | | | First Half of | | |
|--------------------------------------|-------------------|--------------|-------------|---------------|--------------|-------------|
| | 2011 | 2010 | % Change | 2011 | 2010 | % Change |
| Freight Core Invoice Transaction | | | | | | |
| Volume* | 7,486 | 6,716 | 11.5% | 14,156 | 12,733 | 11.2% |
| Freight Invoice Dollar Volume | \$ 5,260,144 | \$ 4,193,903 | 25.4% | \$ 9,829,074 | \$ 7,962,844 | 23.4% |
| Utility Transaction Volume | 3,340 | 3,045 | 9.7% | 6,698 | 6,100 | 9.8% |
| Utility Transaction Dollar Volume | \$ 2,559,095 | \$ 2,451,775 | 4.4% | \$ 5,248,330 | \$ 5,059,874 | 3.7% |
| Payment and Processing Fees | \$ 15,219 | \$ 13,533 | 12.5% | \$ 29,566 | \$ 26,278 | 12.5% |

* Core invoices exclude parcel shipments.

Second Quarter of 2011 compared to Second Quarter of 2010:

Transportation and utility transaction volumes were up 12% and 10%, respectively, and dollar volumes were up 25% and 4%, respectively, due to new business and improved activity for existing customers.

Bank service fees increased \$84,000, or 28%, due to an increase in letter of credit fees offset by a slight decline in account analysis fees. There were \$48,000 gains on sales of securities in the Second Quarter of 2011.

First Half of 2011 compared to First Half of 2010:

Transportation and utility transaction volumes were up 11% and 10%, respectively, and dollar volumes were up 23% and 4%, respectively, due to new business and improved activity for existing customers.

Edgar Filing: CASS INFORMATION SYSTEMS INC - Form 10-Q

Bank service fees increased \$95,000, or 15%, due to increased letter of credit fees and commission and exchange fees offset by a decrease in account analysis fees as more customers chose to pay for services with compensating balances rather than fees. There were \$48,000 gains on sales of securities in the First Half of 2011.

-17-

Net Interest Income

Net interest income is the difference between interest earned on loans, investments, and other earning assets and interest expense on deposits and other interest-bearing liabilities. Net interest income is a significant source of the Company's revenues. The following table summarizes the changes in net interest income and related factors:

| (In thousands) | Second Quarter of | | | First Half of | | |
|--------------------------------------|-------------------|--------------|-------------|---------------|--------------|-------------|
| | 2011 | 2010 | % Change | 2011 | 2010 | % Change |
| Average earnings assets | \$ 1,146,708 | \$ 1,017,818 | 12.7% | \$ 1,148,130 | \$ 1,001,350 | 14.7% |
| Average interest-bearing liabilities | 395,590 | 334,879 | 18.1% | 402,293 | 329,098 | 22.2% |
| Net interest income* | 13,018 | 12,103 | 7.6% | 26,051 | 23,698 | 9.9% |
| Net interest margin* | 4.55% | 4.77% | | 4.58% | 4.77% | |
| Yield on earning assets* | 4.95% | 5.24% | | 4.99% | 5.25% | |
| Rate on interest-bearing liabilities | 1.14% | 1.44% | | 1.17% | 1.46% | |

* Presented on a tax-equivalent basis assuming a tax rate of 35%.

Second Quarter of 2011 compared to Second Quarter of 2010:

Second Quarter 2011 average earning assets increased 13% compared to the same period in the prior year (see discussion in the following paragraphs). The yield on earning assets and the tax equivalent net interest margin both decreased in 2011 as the general level of interest rates declined; however, the significant increase in average earning assets caused net interest income to increase 8% on a tax equivalent basis.

Total average loans increased \$35,385,000, or 5%, to \$710,399,000 for the Second Quarter of 2011 as compared to the Second Quarter of 2010. This increase was attributable to the continuing successful marketing efforts by the Company's lending staff. Average investment securities increased \$40,291,000, or 18%, to \$258,653,000, as the Company took advantage of buying opportunities in the market.

Total average interest-bearing deposits for the Second Quarter of 2011 increased \$60,725,000, or 18%, to \$395,590,000 compared to the Second Quarter of 2010, primarily due to customers transferring funds from lower-yielding investments at other institutions. Average accounts and drafts payable increased \$56,546,000, or 11%, as freight and utility payment processing activities increased.

First Half of 2011 compared to First Half of 2010:

First Half of 2011 average earning assets increased 15% compared to the same period in the prior year (see discussion in the following paragraphs). The yield on earning assets and the tax equivalent net interest margin both decreased in 2011 as the general level of interest rates declined; however, the significant increase in average earning assets caused net interest income to increase 10% on a tax equivalent basis.

Total average loans increased \$46,259,000, or 7%, to \$708,064,000 for the First Half of 2011 as compared to the First Half of 2010. This increase was attributable to the continuing successful marketing efforts by the Company's lending staff. Average investment securities increased \$42,188,000, or 20%, to \$258,025,000, as the Company took advantage of buying opportunities in the market.

Total average interest-bearing deposits for the First Half of 2011 increased \$73,221,000, or 22%, to \$402,292,000 compared to the First Half of 2010, primarily due to customers transferring funds from lower-yielding investments at other institutions. Average accounts and drafts payable increased \$57,182,000, or 11%, as freight and utility payment processing activities increased.

For more information on the changes in net interest income, please refer to the tables that follow.

Edgar Filing: CASS INFORMATION SYSTEMS INC - Form 10-Q

Distribution of Assets, Liabilities and Shareholders' Equity; Interest Rate and Interest Differential

The following tables show the condensed average balance sheets for each of the periods reported, the tax-equivalent interest income and expense on each category of interest-earning assets and interest-bearing liabilities, and the average yield on such categories of interest-earning assets and the average rates paid on such categories of interest-bearing liabilities for each of the periods reported.

| (In thousands) | Second Quarter of 2011 | | | Second Quarter of 2010 | | |
|--|------------------------|-------------------------|-------------|------------------------|-------------------------|-------------|
| | Average Balance | Interest Income/Expense | Yield/Rate | Average Balance | Interest Income/Expense | Yield/Rate |
| Assets¹ | | | | | | |
| Earning assets | | | | | | |
| Loans^{2, 3}: | | | | | | |
| Taxable | \$ 709,509 | \$ 10,126 | 5.72% | \$ 672,465 | \$ 9,848 | 5.87% |
| Tax-exempt ⁴ | 890 | 5 | 2.25 | 2,549 | 36 | 5.66 |
| Investment securities⁵: | | | | | | |
| Taxable | 1,002 | 13 | 5.20 | 890 | 11 | 4.96 |
| Tax-exempt ⁴ | 257,651 | 3,844 | 5.98 | 217,472 | 3,309 | 6.10 |
| Interest-bearing deposits in other financial institutions | | | | | | |
| | 87,364 | 83 | .38 | 16,770 | 13 | .31 |
| Federal funds sold and other short-term investments | | | | | | |
| | 90,292 | 72 | .32 | 107,672 | 85 | .32 |
| Total earning assets | 1,146,708 | 14,143 | 4.95 | 1,017,818 | 13,302 | 5.24 |
| Non-earning assets | | | | | | |
| Cash and due from banks | 12,755 | | | 10,394 | | |
| Premise and equipment, net | 9,743 | | | 10,039 | | |
| Bank owned life insurance | 14,376 | | | 13,857 | | |
| Goodwill and other intangibles | 7,701 | | | 7,808 | | |
| Other assets | 80,353 | | | 62,031 | | |
| Allowance for loan losses | (12,537) | | | (9,116) | | |
| Total assets | \$ 1,259,099 | | | \$ 1,112,831 | | |
| Liabilities and Shareholders' Equity¹ | | | | | | |
| Interest-bearing liabilities | | | | | | |
| Interest-bearing demand deposits | | | | | | |
| | \$ 219,745 | \$ 552 | 1.01% | \$ 162,721 | \$ 495 | 1.22% |
| Savings deposits | 23,584 | 58 | .99 | 23,996 | 71 | 1.19 |
| Time deposits >= \$100 | 53,045 | 177 | 1.34 | 55,682 | 215 | 1.55 |
| Other time deposits | 99,216 | 338 | 1.37 | 92,466 | 418 | 1.81 |
| Total interest-bearing deposits | 395,590 | 1,125 | 1.14 | 334,865 | 1,199 | 1.44 |
| Short-term borrowings & other | — | — | — | 14 | — | — |
| Total interest bearing liabilities | 395,590 | 1,125 | 1.14 | 334,879 | 1,199 | 1.44 |
| Non-interest bearing liabilities | | | | | | |
| Demand deposits | 127,383 | | | 110,343 | | |
| Accounts and drafts payable | 573,659 | | | 517,113 | | |
| Other liabilities | 14,204 | | | 16,025 | | |
| Total liabilities | 1,110,836 | | | 978,360 | | |
| Shareholders' equity | 148,263 | | | 134,471 | | |
| Total liabilities and | | | | | | |

Edgar Filing: CASS INFORMATION SYSTEMS INC - Form 10-Q

| | | | | | |
|----------------------|----|-----------|--------|-----------|--------|
| shareholders' equity | \$ | 1,259,099 | \$ | 1,112,831 | |
| Net interest income | | \$ | 13,018 | \$ | 12,103 |
| Net interest margin | | | 4.55% | | 4.77% |
| Interest spread | | | 3.81 | | 3.80 |

1. Balances shown are daily averages.
2. For purposes of these computations, nonaccrual loans are included in the average loan amounts outstanding. Interest on nonaccrual loans is recorded when received as discussed further in Note 1 to the Company's 2010 consolidated financial statements, filed with the Company's 2010 Annual Report on Form 10-K.
3. Interest income on loans includes net loan fees of \$140,000 and \$92,000 for the Second Quarter of 2011 and 2010, respectively.
4. Interest income is presented on a tax-equivalent basis assuming a tax rate of 35%. The tax-equivalent adjustment was approximately \$1,348,000 and \$1,171,000 for the Second Quarter of 2011 and 2010, respectively.
5. For purposes of these computations, yields on investment securities are computed as interest income divided by the average amortized cost of the investments.

Edgar Filing: CASS INFORMATION SYSTEMS INC - Form 10-Q

| (In thousands) | First Half of 2011 | | | First Half of 2010 | | |
|--|--------------------|--------------------------------|----------------|--------------------|--------------------------------|----------------|
| | Average Balance | Interest Income/ Expense | Yield/ Rate | Average Balance | Interest Income/ Expense | Yield/ Rate |
| Assets¹ | | | | | | |
| Earning assets | | | | | | |
| Loans^{2, 3}: | | | | | | |
| Taxable | \$ 707,136 | \$ 20,375 | 5.81% | \$ 659,216 | \$ 19,250 | 5.89% |
| Tax-exempt ⁴ | 928 | 11 | 2.39 | 2,589 | 74 | 5.76 |
| Investment securities⁵: | | | | | | |
| Taxable | 965 | 18 | 3.76 | 841 | 25 | 5.99 |
| Tax-exempt ⁴ | 257,060 | 7,654 | 6.00 | 214,996 | 6,537 | 6.13 |
| Interest-bearing deposits in other financial institutions | | | | | | |
| | 74,821 | 149 | .40 | 19,075 | 26 | .27 |
| Federal funds sold and other short-term investments | | | | | | |
| | 107,220 | 175 | .33 | 104,633 | 161 | .31 |
| Total earning assets | | | | | | |