

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

CASS INFORMATION SYSTEMS INC
Form 10-Q
November 08, 2006

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2006

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. 2-80070

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 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

The number of shares outstanding of registrant's only class of stock as of
November 6, 2006: Common stock, par value \$.50 per share - 8,328,476 shares
outstanding.

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

TABLE OF CONTENTS

| | |
|--|----|
| PART I - Financial Information | |
| Item 1. FINANCIAL STATEMENTS | |
| Consolidated Balance Sheets | |
| September 30, 2006 (unaudited) and December 31, 2005 | 3 |
| Consolidated Statements of Income | |
| Three and nine months ended September 30, 2006 and 2005 (unaudited) | 4 |
| Consolidated Statements of Cash Flows | |
| Nine months ended September 30, 2006 and 2005 (unaudited) | 5 |
| Notes to Consolidated Financial Statements (unaudited) | 6 |
| Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS | 13 |
| Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK | 25 |
| Item 4. CONTROLS AND PROCEDURES | 25 |
| PART II - Other Information - Items 1. - 6. | |
| SIGNATURES | |

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. Forward-looking statements are not guarantees of future performance and involve risks, uncertainties, and other factors which may cause future performance to vary from expected performance summarized in the forward-looking statements, including those set forth in this paragraph and in the "Risk Factors" section of the Company's Annual Report on Form 10-K, filed with the Securities and Exchange Commission. Important factors that could cause our actual results, performance, or achievements to be materially different from any future results, performance, or achievements expressed or implied by those statements include, but are not limited to: the failure to successfully execute our corporate plan, the loss of key personnel or inability to attract additional qualified personnel, the loss of key customers, increased competition, the inability to remain current with rapid technological change, risks related to acquisitions, risks associated with business cycles and fluctuations in interest rates, utility and system interruptions or processing errors, rules and regulations governing financial institutions and changes in such rules and regulations, credit risk related to borrowers' ability to repay loans, concentration of loans to certain segments such as commercial enterprises, churches and borrowers in the St. Louis area which creates risks associated with adverse factors that may affect these groups and volatility of the price of our common stock. 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
 (Unaudited)
 (Dollars in Thousands except Share and Per Share Data)

| | September 30 2006 | December 31 2005 |
|---|----------------------|---------------------|
| | ----- | ----- |
| Assets | | |
| Cash and due from banks | \$ 31,533 | \$ 29,561 |
| Federal funds sold and other short-term investments | 188,307 | 120,131 |
| | ----- | ----- |
| Cash and cash equivalents | 219,840 | 149,692 |
| | ----- | ----- |
| Securities available-for-sale, at fair value | 87,871 | 94,859 |
| | ----- | ----- |
| Loans | 520,748 | 529,306 |
| Less: Allowance for loan losses | 5,929 | 6,284 |
| | ----- | ----- |
| Loans, net | 514,819 | 523,022 |
| | ----- | ----- |
| Premises and equipment, net | 13,024 | 11,987 |
| Investment in bank owned life insurance | 11,898 | 11,545 |
| Payments in excess of funding | 13,410 | 7,665 |
| Goodwill | 7,171 | 4,398 |
| Assets related to discontinued operations | 225 | 400 |
| Other intangible assets, net | 1,529 | 935 |
| Other assets | 16,627 | 14,195 |
| | ----- | ----- |
| Total assets | \$ 886,414 | \$ 818,698 |
| | ===== | ===== |
| Liabilities and Shareholders' Equity | | |
| Liabilities: | | |
| Deposits: | | |
| Noninterest-bearing | \$ 100,135 | \$ 116,396 |
| Interest-bearing | 175,053 | 170,602 |
| | ----- | ----- |
| Total deposits | 275,188 | 286,998 |
| Accounts and drafts payable | 514,193 | 445,811 |
| Short-term borrowings | 150 | 188 |
| Subordinated convertible debentures | 3,700 | 3,700 |
| Liabilities related to discontinued operations | 388 | 1,848 |
| Other liabilities | 8,822 | 4,872 |
| | ----- | ----- |
| Total liabilities | 802,441 | 743,417 |
| | ----- | ----- |
| 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; 9,112,484 | | |

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

| | | |
|---|------------|------------|
| and 6,336,593 shares issued at September 30, 2006 | | |
| and December 31, 2005, respectively | 4,556 | 3,168 |
| Additional paid-in capital | 17,756 | 18,326 |
| Retained earnings | 78,820 | 71,506 |
| Common shares in treasury, at cost (784,217 shares at | | |
| September 30, 2006 and 836,457 shares at December 31, 2005) | (17,060) | (17,313) |
| Accumulated other comprehensive loss | (99) | (406) |
| | ----- | ----- |
| Total shareholders' equity | 83,973 | 75,281 |
| | ----- | ----- |
| Total liabilities and shareholders' equity | \$ 886,414 | \$ 818,698 |
| | ===== | ===== |

See accompanying notes to unaudited consolidated financial statements.

-3-

CASS INFORMATION SYSTEMS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)
(Dollars in Thousands except Share and Per Share Data)

| | Three Months Ended September 30 | | Nine Months September |
|--|------------------------------------|----------|--------------------------|
| | 2006 | 2005 | 2006 |
| <hr style="border-top: 1px dashed black;"/> | | | |
| Fee Revenue and Other Income: | | | |
| Information services payment and processing revenue | \$ 10,359 | \$ 9,157 | \$ 29,853 |
| Bank service fees | 341 | 414 | 1,266 |
| Gains on sales of investment securities | -- | -- | -- |
| Other | 228 | 149 | 629 |
| | ----- | ----- | ----- |
| Total fee revenue and other income | 10,928 | 9,720 | 31,748 |
| | ----- | ----- | ----- |
| Interest Income: | | | |
| Interest and fees on loans | 9,331 | 27,169 | 23,598 |
| Interest and dividends on debt and equity securities: | | | |
| Taxable | 262 | 218 | 800 |
| Exempt from federal income taxes | 636 | 347 | 1,910 |
| Interest on federal funds sold and other short-term investments | 2,022 | 1,012 | 4,702 |
| | ----- | ----- | ----- |
| Total interest income | 12,251 | 9,813 | 34,581 |
| | ----- | ----- | ----- |
| Interest Expense: | | | |
| Interest on deposits | 1,729 | 1,178 | 4,457 |
| Interest on short-term borrowings | 2 | 1 | 5 |
| Interest on subordinated convertible debentures | 50 | 50 | 148 |
| | ----- | ----- | ----- |
| Total interest expense | 1,781 | 1,229 | 4,610 |
| | ----- | ----- | ----- |
| Net interest income | 10,470 | 8,584 | 29,971 |

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

| | | | |
|---|----------|----------|-----------|
| Provision for loan losses | 200 | 225 | 500 |
| | ----- | ----- | ----- |
| Net interest income after provision for loan losses | 10,270 | 8,359 | 29,471 |
| | ----- | ----- | ----- |
| Operating Expense: | | | |
| Salaries and employee benefits | 11,136 | 9,600 | 31,673 |
| Occupancy | 522 | 499 | 1,462 |
| Equipment | 732 | 716 | 2,128 |
| Amortization of intangible assets | 70 | 42 | 156 |
| Other operating expense | 2,561 | 2,287 | 7,755 |
| | ----- | ----- | ----- |
| Total operating expense | 15,021 | 13,144 | 43,174 |
| | ----- | ----- | ----- |
| Income before taxes and discontinued operations | 6,177 | 4,935 | 18,045 |
| Income tax expense | 2,205 | 1,670 | 6,397 |
| | ----- | ----- | ----- |
| Net income from continuing operations | 3,972 | 3,265 | 11,648 |
| | ----- | ----- | ----- |
| Loss from discontinued operations before income tax expense | (150) | (259) | (475) |
| Income tax benefit | 62 | 87 | 198 |
| | ----- | ----- | ----- |
| Net loss from discontinued operations | (88) | (172) | (277) |
| | ----- | ----- | ----- |
| Net Income | \$ 3,884 | \$ 3,093 | \$ 11,371 |
| | ===== | ===== | ===== |
| Basic Earnings Per Share: | | | |
| From continuing operations | \$.48 | \$.39 | \$ 1.40 |
| From discontinued operations | (.01) | (.02) | (.03) |
| Basic earnings per share | .47 | .37 | 1.37 |
| Diluted Earnings Per Share: | | | |
| From continuing operations | \$.47 | \$.38 | \$ 1.37 |
| From discontinued operations | (.01) | (.01) | (.03) |
| Diluted earnings per share | .46 | .37 | 1.34 |

See accompanying notes to unaudited consolidated financial statements.

-4-

CASS INFORMATION SYSTEMS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
(Dollars in Thousands)

| | Nine Months Ended September 30 | |
|---|-----------------------------------|----------|
| | 2006 | 2005 |
| | ----- | ----- |
| Cash Flows From Operating Activities: | | |
| Net income from continuing operations | \$ 11,648 | \$ 8,826 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |

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

| | | |
|--|------------|------------|
| Depreciation and amortization | 1,484 | 1,572 |
| Gains on sales of investment securities | -- | (547) |
| Provision for loan losses | 500 | 625 |
| Amortization of stock bonus awards | 159 | 99 |
| Tax benefit from exercise of stock options and bonuses | -- | 55 |
| Deferred income tax benefit | (1,031) | (688) |
| Increase in income tax liability | 354 | 265 |
| Increase in pension liability | 1,566 | 1,086 |
| Other operating activities, net | (248) | (1,400) |
| Operating activities of discontinued operations | (1,562) | (131) |
| | ----- | ----- |
| Net cash provided by operating activities | 12,870 | 9,762 |
| | ----- | ----- |
| Cash Flows From Investing Activities: | | |
| Proceeds from sales of securities available-for-sale | -- | 12,952 |
| Proceeds from maturities of securities available-for-sale | 65,510 | 57,000 |
| Purchase of securities available-for-sale | (57,860) | (68,854) |
| Net decrease (increase) in loans | 7,703 | (18,769) |
| Increase in payments in excess of funding | (5,745) | (2,989) |
| Purchases of premises and equipment, net | (2,547) | (1,315) |
| Purchase of NTransit, Inc. | (3,172) | -- |
| Investing activities of discontinued operations | -- | (17) |
| | ----- | ----- |
| Net cash provided by (used in) investing activities | 3,889 | (21,992) |
| | ----- | ----- |
| Cash Flows From Financing Activities: | | |
| Net (decrease) increase in noninterest-bearing demand deposits | (16,261) | 4,419 |
| Net decrease in interest-bearing demand and savings deposits | (15,829) | (6,430) |
| Net increase in time deposits | 20,280 | 418 |
| Net increase in accounts and drafts payable | 68,382 | 74,229 |
| Net (decrease) increase in short-term borrowings | (38) | 39 |
| Cash proceeds from exercise of stock options | 330 | 175 |
| Tax benefit from exercise of stock options and bonuses | 64 | -- |
| Cash dividends paid | (2,669) | (2,322) |
| Purchase of common shares for treasury | (870) | (586) |
| | ----- | ----- |
| Net cash provided by financing activities | 53,389 | 69,942 |
| | ----- | ----- |
| Net increase in cash and cash equivalents | 70,148 | 57,712 |
| Cash and cash equivalents at beginning of period | 149,692 | 87,543 |
| | ----- | ----- |
| Cash and cash equivalents at end of period | \$ 219,840 | \$ 145,255 |
| | ===== | ===== |
| Supplemental information: | | |
| Cash paid for interest | \$ 4,287 | \$ 3,418 |
| Cash paid for income taxes | 6,103 | 4,754 |

See accompanying notes to unaudited consolidated financial statements.

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

The accompanying unaudited consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles ("U.S. GAAP") 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. GAAP 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 2005 consolidated financial statements have been reclassified to conform to the 2006 presentation. Such reclassifications have no effect on previously reported net income or shareholders' equity. The Company's bank subsidiary sold the assets of Government e-Management Solutions, Inc. ("GEMS"), its wholly owned subsidiary, on December 30, 2005. The assets, liabilities and results of operations of GEMS have been presented in the accompanying consolidated financial statements as discontinued operations. The Company issued 50% stock dividends on September 15, 2006 and September 15, 2005 and the share and per share information have been restated for all periods presented in the accompanying consolidated financial statements. 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, 2005.

Note 2 - Intangible Assets

The Company accounts for intangible assets in accordance with Statement of Financial Accounting Standards ("SFAS") 142, "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. Intangible assets for the periods ended September 30, 2006 and December 31, 2005 are as follows:

| (In Thousands) | September 30, 2006 | | December 31, 2005 |
|--|--------------------------|-----------------------------|--------------------------|
| | Gross Carrying Amount | Accumulated Amortization | Gross Carrying Amount |
| Assets eligible for amortization: | | | |
| Software | \$ 862 | \$ (359) | \$ 862 |
| Customer List | 750 | (27) | -- |
| Total | 1,612 | (386) | 862 |
| Assets not eligible for amortization: | | | |
| Goodwill | 7,398 | (227)* | 4,625 |
| Minimum pension liability | 303 | -- | 303 |
| Total | 7,701 | (227) | 4,928 |
| Total intangible assets | \$ 9,313 | \$ (613) | \$ 5,790 |

*Amortization through December 31, 2001 prior to adoption of SFAS 142.

Software is amortized over 4-5 years and the customer list that was acquired in the NTransit purchase is amortized over seven years. Goodwill includes \$2,773,000 acquired in the NTransit purchase. The minimum pension liability was recorded in accordance with SFAS 87, "Employers' Accounting for Pensions", which requires the Company to record an additional minimum pension liability by the amount of which the accumulated benefit obligation exceeds the sum of the fair

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

value of plan assets and accrued amount previously recorded and offset this liability by an intangible asset to the extent of previously unrecognized prior service costs. The liability and corresponding intangible asset are adjusted annually.

Amortization of intangible assets amounted to \$156,000 and \$128,000 for the nine-month periods ended September 30, 2006 and 2005, respectively. Estimated amortization of intangibles over the next five years is as follows: \$226,000 in 2006, \$280,000 in 2007 and 2008, \$222,000 in 2009 and \$107,000 in 2010.

Note 3 - Equity Investments in Non-Marketable Securities

Non-marketable equity investments in low-income housing projects are included in other assets on the Company's consolidated balance sheets. The total balance of these investments at September 30, 2006 was \$357,000.

Note 4 - 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, adjusted for the net income effect of the interest expense on the outstanding convertible debentures, by the sum of the

-6-

weighted-average number of common shares outstanding and the weighted-average number of potential common shares outstanding. The calculations of basic and diluted earnings per share for the periods ended September 30, 2006 and 2005 are as follows:

| | Three Months Ended September 30 | | Nine Mo Septe |
|---|------------------------------------|-----------|------------------|
| (Dollars in Thousands except Per Share data) | 2006 | 2005 | 2006 |
| Basic | | | |
| Net income from continuing operations | \$ 3,972 | \$ 3,265 | \$ 11,648 |
| Net loss from discontinued operations | (88) | (172) | (277) |
| Net income | \$ 3,884 | \$ 3,093 | \$ 11,371 |
| Weighted-average common shares outstanding | 8,304,441 | 8,267,733 | 8,311,861 |
| Basic earnings per share from continuing operations | \$.48 | \$.39 | \$ 1.40 |
| Basic earnings per share from discontinued operations | (.01) | (.02) | (.03) |
| Basic earnings per share | \$.47 | \$.37 | \$ 1.37 |
| Diluted | | | |
| Net income from continuing operations | \$ 3,972 | \$ 3,265 | \$ 11,648 |
| Net income effect of 5.33% convertible debentures | 1 28 | 27 | 82 |
| Net income from continuing operations | 4,000 | 3,292 | 11,730 |

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

| | | | |
|--|-----------|-----------|-----------|
| Net loss from discontinued operations | (88) | (172) | (277) |
| Net income | \$ 3,912 | \$ 3,120 | \$ 11,453 |
| Weighted-average common shares outstanding | 8,304,441 | 8,267,733 | 8,311,861 |
| Effect of dilutive stock options and awards | 72,504 | 102,877 | 65,923 |
| Effect of 5.33% convertible debentures | 172,717 | 172,717 | 172,717 |
| Weighted-average common shares outstanding assuming dilution | 8,549,662 | 8,543,327 | 8,550,501 |
| Diluted earnings per share from continuing operations | \$.47 | \$.38 | \$ 1.37 |
| Diluted earnings per share from discontinued operations | (.01) | (.01) | (.03) |
| Diluted earnings per share | \$.46 | \$.37 | \$ 1.34 |

Share and per share data in the schedule above have been restated for the 50% stock dividends issued on September 15, 2006 and September 15, 2005.

Note 5 - Stock Repurchases

The Company maintains a treasury stock buyback program pursuant to which the Board of Directors has authorized the repurchase of up to 150,000 shares of the Company's Common Stock. The Company repurchased 30,000 and 22,500 shares during the nine months ended September 30, 2006 and 2005, respectively. As of September 30, 2006, 120,000 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 6 - Comprehensive Income

For the nine-month periods ended September 30, 2006 and 2005, unrealized gains and losses on debt and equity securities available-for-sale were the Company's only other comprehensive income component. Comprehensive income for the three and nine month-periods ended September 30, 2006 and 2005 is summarized as follows:

| (In Thousands) | Three Months Ended September 30 | | Nine Months Ended September 30 | |
|---|------------------------------------|----------|-----------------------------------|----------|
| | 2006 | 2005 | 2006 | 2005 |
| Net income from continuing operations | \$ 3,972 | \$ 3,265 | \$11,648 | \$ 8,311 |
| Other comprehensive income: | | | | |
| Net unrealized gain (loss) on securities available-for-sale, net of tax | 793 | (34) | 307 | (1,000) |

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

| | | | | |
|---|----------|----------|----------|------|
| Less: reclassification adjustment for realized gains on sales of securities, available-for-sale, included in net income, net of tax | -- | -- | -- | |
| Total other comprehensive income (loss) | 793 | (34) | 307 | |
| Total comprehensive income from continuing operations | \$ 4,765 | \$ 3,231 | \$11,955 | \$ 8 |

Note 7 - 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, 2005. 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 market value. Information for prior periods has been restated to reflect changes in the composition of the Company's segments.

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

Summarized information about the Company's operations in each industry segment for the three and nine month periods ended September 30, 2006 and 2005, is as follows:

| (In Thousands) | Information Services | Banking Services | Corporate Elimination and Other |
|---|-------------------------|---------------------|---------------------------------------|
| Three Months Ended September 30, 2006: | | | |
| Total Revenues: | | | |
| Revenue from customers | \$ 17,593 | \$ 3,605 | \$ |
| Intersegment revenue | (109) | 921 | (8) |
| Net income from continuing operations | 2,837 | 1,135 | |
| Total assets | 569,760 | 318,136 | (1,4) |
| Goodwill | 7,035 | 136 | |
| Other intangible assets, net | 1,529 | -- | |
| Assets related to discontinued operations | -- | -- | 2 |
| Three Months Ended September 30, 2005: | | | |
| Total Revenues: | | | |
| Revenue from customers | \$ 14,277 | \$ 3,802 | \$ |
| Intersegment revenue | 481 | 358 | (8) |
| Net income from continuing operations | 2,250 | 1,015 | |
| Total assets | 478,215 | 322,065 | (5,0) |

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

| | | | |
|---|-------|-----|-----|
| Goodwill | 4,262 | 153 | |
| Other intangible assets, net | 675 | -- | 3 |
| Assets related to discontinued operations | -- | -- | 4,4 |

Nine Months Ended September 30, 2006:

| | | | |
|---------------------------------------|-----------|-----------|------|
| Total Revenues: | | | |
| Revenue from customers | \$ 49,469 | \$ 11,750 | \$ |
| Intersegment revenue | 778 | 1,633 | (2,4 |
| Net income from continuing operations | 8,267 | 3,381 | |

Nine Months Ended September 30, 2005:

| | | | |
|---------------------------------------|-----------|-----------|------|
| Total Revenues: | | | |
| Revenue from customers | \$ 41,251 | \$ 10,891 | \$ |
| Intersegment revenue | 80 | 1,103 | (1,1 |
| Net income from continuing operations | 5,772 | 3,054 | |

-8-

Note 8 - Loans by Type

| (In Thousands) | September 30, 2006 | December 31, 2005 |
|-----------------------------------|--------------------|-------------------|
| Commercial and industrial | \$ 136,575 | \$ 146,892 |
| Real estate: | | |
| Mortgage | 139,218 | 164,590 |
| Mortgage - Churches & related | 203,713 | 183,964 |
| Construction | 16,661 | 13,052 |
| Construction - Churches & related | 16,134 | 15,118 |
| Industrial revenue bonds | 5,549 | 4,514 |
| Installment | -- | 107 |
| Other | 2,898 | 1,069 |
| Total loans | \$ 520,748 | \$ 529,306 |

Note 9 - 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 and capital 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 September 30, 2006, 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 September 30, 2006, the balances of unused loan commitments, standby and commercial letters of credit were \$18,353,000, \$5,447,000 and \$2,539,000,

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

respectively. Since these 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 and capital lease commitments, time deposits and convertible subordinated debentures at September 30, 2006:

| (Dollars 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 | \$ 4,316 | \$ 645 | \$ 1,186 | \$ 823 | \$ 1,662 |
| Time deposits* | 87,333 | 80,012 | 4,857 | 2,464 | -- |
| Convertible subordinated debentures* | 3,700 | -- | -- | -- | 3,700 |
| Total | \$95,349 | \$80,657 | \$ 6,043 | \$ 3,287 | \$ 5,362 |

* Includes principal payments only.

-9-

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 10 - Stock-Based Compensation

The Company maintains stock-based incentive plans, which permit the awards of shares of restricted common stock and the granting of options to purchase up to 1,039,000 shares of common stock. Restricted shares are amortized to expense over the three-year vesting period. Options currently vest and expire over a period not to exceed seven years. The plans authorize the grant of awards in the form of options intended to qualify as incentive stock options under Section 422 of the Internal Revenue Code, options that do not qualify (non-statutory stock options) and grants of restricted shares of common stock. The Company issues shares out of treasury stock for restricted shares and option exercises.

Prior to fiscal 2006, the Company applied the intrinsic value-based method, as outlined in Accounting Principles Board Opinion ("APB") No. 25, "Accounting for Stock Issued to Employees," and related interpretations, in accounting for stock options granted under these programs. Under the intrinsic value-based method, no compensation expense was recognized if the exercise price of the Company's

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

employee stock options equaled the market price of the underlying stock on the date of the grant. Accordingly, prior to fiscal year 2006, no compensation cost was recognized in the accompanying consolidated statements of income on stock options granted to employees, since all options granted under the Company's share incentive programs had an exercise price equal to the market value of the underlying common stock on the date of the grant.

Effective January 1, 2006, the Company adopted Statement of Financial Accounting Standards No. 123R ("SFAS No. 123R") "Share-based Payment." This statement supersedes APB No. 25. SFAS No. 123R requires that all stock-based compensation be recognized as an expense in the financial statements and that such cost be measured at the fair value of the award. This statement was adopted using the modified prospective method of application, which requires the Company to recognize compensation expense on a prospective basis. Therefore, prior period financial statements have not been restated. Under this method, in addition to reflecting compensation expense for new share-based awards, expense is also recognized to reflect the remaining service period of awards that had been included in pro forma disclosures in prior periods. SFAS No. 123R also requires that excess tax benefits related to stock option exercises be reflected as financing cash inflows instead of operating cash inflows. For the nine months ended September 30, 2006, the only options exercised were incentive stock options that did not generate any excess tax benefits for the Company. As of September 30, 2006, the total unrecognized compensation expense related to non-vested stock options was \$140,000 and the related weighted-average period over which it is expected to be recognized is approximately 5.0 years. As of September 30, 2006, the total unrecognized compensation expense related to non-vested stock awards was \$413,000 and the related weighted-average period over which it is expected to be recognized is approximately 1.5 years.

The disclosures required by SFAS No. 123R are provided in the table below. The Company uses the Black-Scholes option-pricing model to determine the fair value of the stock options at the date of grant. There were 25,227 and 13,242 options granted in the first nine months of 2006 and 2005, respectively. The following table represents the effect on basic and diluted earnings per share for the periods ended September 30, 2005 assuming SFAS 123R had been adopted:

-10-

| (In Thousands except Per Share Data (1)) | Three Months Ended September 30 2005 | Nine Months September 2005 |
|--|--|----------------------------------|
| <hr style="border-top: 1px dashed black;"/> | | |
| Net income from continuing operations | | |
| As reported | \$ 3,265 | \$ 8, |
| Add: Stock-based compensation expense included in reported net income, net of tax | 22 | |
| Less: Stock-based compensation expense determined under the fair-value-based method for all awards, net of tax | (27) | |
| <hr style="border-top: 1px dashed black;"/> | | |
| Pro forma net income from continuing operations | \$ 3,260 | \$ 8, |
| Net income effect of subordinated convertible debentures | 27 | |
| <hr style="border-top: 1px dashed black;"/> | | |
| Pro forma net income from continuing operations assuming dilution | \$ 3,287 | \$ 8, |
| <hr style="border-top: 1px dashed black;"/> | | |
| Net income from continuing operations per common share: | | |

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

| | | | | |
|----------------------|----|-----|----|---|
| Basic, as reported | \$ | .39 | \$ | 1 |
| Basic, pro forma | | .40 | | 1 |
| Diluted, as reported | | .38 | | 1 |
| Diluted, pro forma | | .38 | | 1 |

(1) Per share data has been restated for the 50% stock dividends issued on September 15, 2006 and September 15, 2005.

Following are the assumptions used to estimate the fair value of option grants during the three and nine-month periods ended September 30, 2006 and 2005:

| | Three Months Ended | | |
|-------------------------|--------------------|------|--------|
| | September 30 | | |
| | 2006 | 2005 | 2006 |
| Risk-free interest rate | -- | -- | 4.37% |
| Expected life | -- | -- | 7 yrs. |
| Expected volatility | -- | -- | 5.00% |
| Expected dividend yield | -- | -- | 1.88% |

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 options 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 options using average monthly closing market prices of the Company's stock. The expected dividend yield is determined based on the Company's current rate of annual dividends.

Under the treasury stock method, outstanding stock options are dilutive when the average market price of the Company's common stock, when combined with the effect of any unamortized compensation expense, exceeds the option price during a period. In addition, proceeds from the assumed exercise of dilutive options along with the related tax benefit are assumed to be used to repurchase common shares at the average market price of such stock during the period. Anti-dilutive shares are those option shares with exercise prices in excess of the current market value.

A summary of the Company's stock option activity for the three and nine-month periods ended September 30, 2006 is shown below.

| | Shares | Weighted-Average Exercise Price | Average Remaining Contractual Term Years |
|----------------------------------|-----------|---------------------------------|--|
| Outstanding at December 31, 2005 | 209,851 | \$ 10.67 | |
| Granted | 25,227 | 22.73 | |
| Exercised | (134,724) | 9.72 | |
| Forfeited or expired | -- | -- | |
| Outstanding at June 30, 2006 | 100,354 | 15.03 | |
| Granted | -- | -- | |
| Exercised | (5,505) | 9.56 | |

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

| | | | | |
|-----------------------------------|--------|---------|-------|-------|
| Forfeited or expired | -- | -- | | |
| | ----- | ----- | | |
| Outstanding at September 30, 2006 | 94,849 | 15.34 | 4.56 | \$ |
| | ===== | ===== | ===== | ===== |
| Exercisable at September 30, 2006 | 2,399 | \$ 9.95 | 3.09 | \$ |
| | ===== | ===== | ===== | ===== |

-11-

The total intrinsic value of options exercised during the three and nine-month periods ended September 30, 2006 was \$105,000 and \$1,728,000, respectively. The total intrinsic value of options exercised during the three and nine-month periods ended September 30, 2005 was \$103,000 and \$216,000, respectively. The Company does not anticipate any additional options will be exercised during 2006.

A summary of the activity of the non-vested shares during the nine-month period ended September 30, 2006 is shown below. There was no activity for the three-month period ended September 30, 2006.

| | Shares | Weighted-Average Grant Date Fair Value |
|----------------------------------|-----------|--|
| ----- | | |
| Non-vested at December 31, 2005 | 168,047 | \$ 1.82 |
| Granted | 25,229 | 3.25 |
| Vested | (100,826) | 1.68 |
| Forfeited | -- | -- |
| ----- | | |
| Non-vested at September 30, 2006 | 92,450 | \$ 2.37 |
| ===== | | |

The weighted-average grant date fair value of options granted during the nine-month period ended September 30, 2006 was \$3.25.

Note 11 - 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 for 2005 and an estimate for 2006:

| (In Thousands) | Estimated 2006 | Actual 2005 |
|--|----------------|-------------|
| ----- | | |
| Service cost - benefits earned during the year | \$ 1,554 | \$ 1,292 |
| Interest cost on projected benefit obligation | 1,565 | 1,384 |
| Expected return on plan assets | (1,603) | (1,312) |
| Net amortization | 270 | 109 |
| ----- | | |

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

Net periodic pension cost \$ 1,786 \$ 1,473

Pension costs recorded to expense were \$586,000 and \$346,000 for the three-month periods ended September 30, 2006 and 2005 ("Third Quarter of 2006 and 2005", respectively). Pension costs recorded to expense were \$1,339,000 and \$1,039,000 for the first nine-month periods ending September 30, 2006 and 2005 ("First Nine Months of 2006 and 2005", respectively). The Company has not made any contribution to the plan during the nine-month period ended September 30, 2006, but is expecting to contribute approximately \$3,200,000 in 2006.

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 2005 and an estimate for 2006:

| (In Thousands) | Estimated 2006 | Actual 2005 |
|--|-------------------|----------------|
| ===== | | |
| Service cost - benefits earned during the year | \$ 43 | \$ (34) |
| Interest cost on projected benefit obligation | 149 | 161 |
| Net amortization | 112 | 64 |
| ----- | | |
| Net periodic pension cost | \$ 304 | \$ 191 |
| ----- | | |

Pension costs recorded to expense were \$163,000 and \$49,000 for the Third Quarter of 2006 and 2005, respectively, and were \$258,000 and \$143,000 for the First Nine Months of 2006 and 2005, respectively.

-12-

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

Overview

Cass Information Systems, Inc. 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 includes 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 stores 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 provide Internet-based tools for analytical processing. The Company also, through Cass Commercial Bank ("the Bank"), its St. Louis, Missouri-based bank subsidiary, provides banking services in the St. Louis metropolitan area, Orange County, California and other selected cities in the United States. In

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

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 that can vary greatly. In addition, the degree of automation such as electronic data interchange ("EDI"), 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 account balances that are 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 expense on its deposits. The Bank also assesses fees on other services such as cash management services.

Industry-wide factors that impact the Company include the acceptance by large corporations of the outsourcing of 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. The general level of interest rates also has a significant effect on the revenue of the Company.

On December 30, 2005, the Company's bank subsidiary sold the operating assets of its wholly-owned subsidiary, GEMS, to N. Harris Computer Corporation. The assets, liabilities and operating results of GEMS have been reclassified as discontinued operations for all periods. GEMS developed and sold proprietary financial, human resource and revenue management software to government entities. GEMS was acquired on January 2, 2001 when the Company's bank subsidiary foreclosed on the operating assets of a software company in order to protect its financial interests.

On July 7, 2006, the Company acquired 100% of the stock of NTransit, Inc., a company whose service provides auditing and expense management of parcel shipments. While this acquisition does not meet the Regulation S-X criteria of a significant business combination, it positions the Company to expand its offerings in the specialized service and expertise in parcel shipping, which is a unique segment of the transportation industry that has experienced tremendous growth in recent years.

Currently, management views Cass' major opportunity and challenge as the continued expansion of its payment and information processing service offerings

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

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. This trend has been positive over the past years and management anticipates that this should continue in 2006. The general level of interest rates, particularly short-term interest rates, began to increase in 2004 and continued through the first nine months of 2006. If rates continue to rise, the positive impact on net interest income and net earnings will continue. Conversely, if rates decline there will be a negative impact. Management intends to continue to refine its risk management practices, monitor and manage the quality of the loan portfolio and maintain a strong financial and liquidity position.

Critical Accounting Policies

The Company has prepared the consolidated financial information in this report in accordance with U.S. GAAP. In preparing the consolidated financial statements in accordance with U.S. GAAP, 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 our business operations are discussed in the "Provision and Allowance for Loan Losses" section of this report.

Impairment of Assets. The Company periodically evaluates certain long-term assets such as intangible assets including goodwill, foreclosed assets, internally developed software and investments in private equity securities 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. Assets held for sale are carried at the lower of cost or fair value less costs to sell. 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 Company accounts for income taxes in accordance with SFAS No. 109, "Accounting for Income Taxes," which establishes financial accounting and reporting standards for the effect of 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, changes in tax laws or interpretations thereof. In addition, the Company is

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

subject to the continuous examination of its income tax returns by the Internal Revenue Service and other taxing authorities. A change in the assessment of the outcomes of such matters could materially impact its consolidated financial statements.

Results of Operations

The following paragraphs more fully discuss the results of operations and changes in financial condition for the Third Quarter of 2006 compared to the Third Quarter of 2005 and the First Nine Months of 2006 compared to the First Nine Months of 2005. 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 the Company's 2005 Annual Report on Form 10-K. Results of operations for the Third Quarter of 2006 are not necessarily indicative of the results to be attained for any other period.

-14-

Net Income

The following table summarizes the Company's operating results:

| (Dollars in Thousands except Per Share Data) | Three Months Ended September 30 | | | % | Nine Se |
|--|------------------------------------|----------|--|--------|------------|
| | 2006 | 2005 | | Change | 2006 |
| Net income | \$ 3,884 | \$ 3,093 | | 25.6% | \$ 11,371 |
| Net income from continuing operations | \$ 3,972 | \$ 3,265 | | 21.7% | \$ 11,648 |
| Diluted earnings per share | \$.46 | \$.37 | | 24.3% | \$ 1.34 |
| Diluted earnings per share from continuing operations | \$.47 | \$.38 | | 23.7% | \$ 1.37 |
| Return on average assets | 1.80% | 1.57% | | -- | 1.84% |
| Return on average equity | 19.12% | 16.88% | | -- | 19.45% |

Fee Revenue and Other Income from Continuing Operations

The Company's fee revenue is derived mainly from freight 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 for the three and nine-month periods ended September 30, 2006 and 2005 were as follows:

| (In Thousands) | Three Months Ended September 30 | | | % | Ni |
|----------------|------------------------------------|------|--|--------|------|
| | 2006 | 2005 | | Change | 2006 |

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

| | | | | |
|--|-------------|-------------|-------|--------------|
| Freight Core Invoice Transaction Volume* | 6,154 | 5,815 | 5.8% | 18,311 |
| Freight Invoice Dollar Volume | \$3,648,694 | \$3,111,175 | 17.3% | \$10,722,994 |
| Utility Transaction Volume | 1,701 | 1,421 | 19.7% | 4,797 |
| Utility Transaction Dollar Volume | \$1,538,628 | \$1,148,438 | 34.0% | \$ 4,188,578 |
| Payment and Processing Fees | \$ 10,359 | \$ 9,157 | 13.1% | \$ 29,853 |

*Core invoices exclude parcel shipments.

Third Quarter of 2006 compared to Third Quarter of 2005:

Freight transaction volume for the Third Quarter of 2006 increased mainly due to increased activity with existing accounts and a growing customer base. Total dollar volume processed by this division also increased during this period due to the increased activity and larger average freight charges. The increase in transaction and dollar volume from utility transactions increased primarily due to new customers as the growth of this division continues. These increases in transaction volume, combined with the expansion of the customer base in the telecom division, drove the 13% increase in processing fees.

Bank service fees decreased \$73,000 or 18%. This decrease was due primarily to the fact that service fees decrease as the credit allowance for non-interest bearing deposits increases with the general level of interest rates. There were no gains from the sale of securities in the Third Quarter of 2006 and the Third Quarter of 2005. Other income increased \$79,000 in the Third Quarter of 2006.

First Nine Months of 2006 compared to First Nine Months of 2005:

Freight and Utility transaction volume and dollar volume increased for the First Nine Months of 2006 compared to 2005 due to the same factors discussed above for the Third Quarter.

Bank service fees increased \$107,000 or 9%. This increase was due primarily to a penalty charged for the early withdrawal of a certificate of deposit by one large bank customer during the First Quarter of 2006. There were no gains from the sale of securities in the First Nine Months of 2006 compared to a net gain of \$547,000 during the First Nine Months of 2005. Other income increased \$137,000 in the First Nine Months of 2006.

-15-

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 for the three and nine-month periods ended September 30, 2006 and 2005:

| (Dollars in Thousands) | Three Months Ended September 30 | | | Nin 2006 |
|------------------------|------------------------------------|------|-------------|-------------|
| | 2006 | 2005 | % Change | |
| | | | | |

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

| | | | | |
|--------------------------------------|------------|------------|-------|------------|
| Average earnings assets | \$ 774,293 | \$ 700,442 | 10.5% | \$ 751,769 |
| Net interest income* | 10,842 | 8,798 | 23.2% | 31,093 |
| Net interest margin* | 5.56% | 4.98% | -- | 5.53% |
| Yield on earning assets* | 6.47% | 5.68% | -- | 6.35% |
| Rate on interest bearing liabilities | 3.83% | 2.61% | -- | 3.44% |

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

Third Quarter of 2006 compared to Third Quarter of 2005:

The increase in net interest income was primarily due to a significant increase in earning assets and an increase in yields on earning assets that exceeded the counteracting effect of increases in rates paid on deposit accounts. The increase in earning assets was funded by an increase in accounts and drafts payable due to the increase in dollar volume processed that exceeded a decrease in bank deposits. This decrease was caused mainly by management's decision to reduce the balances of higher-cost funding. Yields on earning assets and rates paid on deposit accounts both increased as the general level of interest rates increased. However, as the balances of earning assets greatly exceed the balances of interest-bearing deposits, the net effect on net interest margin was positive.

Total average loans increased \$14,688,000 or 3% to \$527,784,000. This increase was attributable to new business relationships and was funded by the increase in accounts and drafts payable. Total average investment in debt and equity securities increased \$23,012,000 or 35% to \$88,734,000 as the Company invested a portion of the increase in payables. Total average federal funds sold and other short-term investments increased \$36,151,000 or 30% to \$157,775,000. This increase provides additional liquidity to the Company. For more information on the changes in net interest income please refer to the tables that follow.

First Nine Months of 2006 compared to First Nine Months of 2005:

The increase in net interest income was primarily due to a significant increase in earning assets and an increase in yields on earning assets that exceeded the counteracting effect of increases in rates paid on deposit accounts. The increase in earning assets was funded by an increase in accounts and drafts payable due to the increase in dollar volume processed that exceeded a decrease in bank deposits. This decrease was caused mainly by management's decision to reduce the balances of higher-cost funding. Yields on earning assets and rates paid on deposit accounts both increased as the general level of interest rates increased. However, as the balances of earning assets greatly exceed the balances of interest-bearing deposits, the net effect on net interest margin was positive.

Total average loans increased \$18,297,000 or 4% to \$528,250,000. This increase was attributable to new business relationships and was funded by the increase in accounts and drafts payable. Total average investment in debt and equity securities increased \$25,256,000 or 38% to \$91,672,000 as the Company invested a portion of the increase in payables. Total average federal funds sold and other short-term investments increased \$26,124,000 or 25% to \$131,847,000. This increase provides additional liquidity to the Company. For more information on the changes in net interest income please refer to the tables that follow.

The Company is positively affected by increases in the level of interest rates due to the fact that its rate-sensitive assets significantly exceed its rate-sensitive liabilities. This is primarily due to the noninterest-bearing liabilities generated by the Company in the form of accounts and drafts payable. Changes in interest rates will affect some earning assets such as federal funds sold and floating rate loans immediately and some earning assets, such as fixed

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

rate loans and municipal bonds, over time.

-16-

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

The following table shows 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.

| (Dollars in Thousands) | Third Quarter 2006 | | | Thi |
|---|--------------------|-------------------------|-------------|-------------------|
| | Average Balance | Interest Income/Expense | Yield/Rate | Average Balance |
| Assets (1) | | | | |
| Earning assets: | | | | |
| Loans (2,3): | | | | |
| Taxable | \$ 522,439 | \$ 9,273 | 7.04% | \$ 508,263 |
| Tax-exempt (4) | 5,345 | 88 | 6.53 | 4,833 |
| Debt and equity securities (5): | | | | |
| Taxable | 22,600 | 263 | 4.62 | 28,724 |
| Tax-exempt (4) | 66,134 | 978 | 5.87 | 36,998 |
| Federal funds sold and other short-term investments | 157,775 | 2,022 | 5.08 | 121,624 |
| Total earning assets | 774,293 | 12,624 | 6.47 | 700,442 |
| Nonearning assets: | | | | |
| Cash and due from banks | 29,914 | | | 30,398 |
| Premises and equipment, net | 12,886 | | | 11,242 |
| Bank owned life insurance | 11,818 | | | 11,351 |
| Goodwill and other intangibles | 5,269 | | | 5,479 |
| Other assets | 26,355 | | | 22,630 |
| Assets related to discontinued operations | 396 | | | 6,128 |
| Allowance for loan losses | (6,313) | | | (6,063) |
| Total assets | \$ 854,618 | | | \$ 781,607 |
| Liabilities And Shareholders' Equity (1) | | | | |
| Interest-bearing liabilities: | | | | |
| Interest-bearing demand deposits | \$ 63,845 | \$ 429 | 2.67% | \$ 74,360 |
| Savings deposits | 26,338 | 201 | 3.03 | 29,602 |
| Time deposits of \$100 or more | 61,631 | 762 | 4.91 | 42,697 |
| Other time deposits | 28,845 | 338 | 4.65 | 36,497 |
| Total interest-bearing deposits | 180,659 | 1,730 | 3.80 | 183,156 |
| Short-term borrowings | 197 | 2 | 4.03 | 134 |
| Subordinated debentures | 3,700 | 50 | 5.36 | 3,700 |
| Total interest-bearing | | | | |

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

| | | | | |
|--|------------|-----------|-------|------------|
| liabilities | 184,556 | 1,782 | 3.83 | 186,990 |
| Noninterest-bearing liabilities: | | | | |
| Demand deposits | 98,542 | | | 103,996 |
| Accounts and drafts payable | 481,988 | | | 409,026 |
| Other liabilities | 8,664 | | | 7,149 |
| Liabilities related to discontinued operations | 242 | | | 1,779 |
| ----- | | | | |
| Total liabilities | 773,992 | | | 708,940 |
| Shareholders' equity | 80,626 | | | 72,667 |
| Total liabilities and shareholders' equity | \$ 854,618 | | | \$ 781,607 |
| ----- | | | | |
| Net interest income | | \$ 10,842 | | |
| Interest spread | | | 2.64% | |
| Net interest margin | | | 5.56 | |
| ===== | | | | |

- Balances shown are daily averages.
- 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 2005 Consolidated Financial Statements, filed with the Company's 2005 Annual Report on Form 10-K.
- Interest income on loans includes net loan fees of \$55,000 and \$45,000 for the Third Quarter of 2006 and 2005, respectively.
- Interest income is presented on a tax-equivalent basis assuming a tax rate of 35%. The tax-equivalent adjustment was approximately \$373,000 and \$214,000 for the Third Quarter of 2006 and 2005, respectively.
- For purposes of these computations, yields on investment securities are computed as interest income divided by the average amortized cost of the investments.

-17-

| (Dollars in Thousands) | First Nine Months of 2006 | | | First Ni |
|---|---------------------------|-------------------------|------------|-----------------|
| | Average Balance | Interest Income/Expense | Yield/Rate | Average Balance |
| ===== | | | | |
| Assets (1) | | | | |
| Earning assets: | | | | |
| Loans (2,3): | | | | |
| Taxable | \$ 522,940 | \$ 26,994 | 6.90% | \$ 505,072 |
| Tax-exempt (4) | 5,310 | 268 | 6.75 | 4,881 |
| Debt and equity securities (5): | | | | |
| Taxable | 25,506 | 800 | 4.19 | 28,681 |
| Tax-exempt (4) | 66,166 | 2,939 | 5.94 | 37,735 |
| Federal funds sold and other short-term investments | 131,847 | 4,702 | 4.77 | 105,723 |
| ----- | | | | |
| Total earning assets | 751,769 | 35,703 | 6.35 | 682,092 |
| Nonearning assets: | | | | |

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

| | | | | |
|---|-------------------|------------------|-------------|-------------------|
| Cash and due from banks | 28,921 | | | 27,144 |
| Premises and equipment, net | 12,506 | | | 11,252 |
| Bank owned life insurance | 11,702 | | | 11,240 |
| Goodwill and other intangibles | 5,287 | | | 5,525 |
| Other assets | 23,067 | | | 22,231 |
| Assets related to discontinued operations | 6,164 | | | 233 |
| Allowance for loan losses | (6,265) | | | (5,996) |
| Total assets | \$ 827,220 | | | \$ 759,652 |
| Liabilities And Shareholders' Equity (1) | | | | |
| Interest-bearing liabilities: | | | | |
| Interest-bearing demand deposits | \$ 71,612 | \$ 1,282 | 2.39% | \$ 81,150 |
| Savings deposits | 22,444 | 420 | 2.50 | 25,948 |
| Time deposits of \$100 or more | 50,909 | 1,778 | 4.67 | 45,825 |
| Other time deposits | 30,551 | 977 | 4.28 | 36,717 |
| Total interest-bearing deposits | 175,516 | 4,457 | 3.40 | 189,640 |
| Short-term borrowings | 166 | 5 | 4.03 | 166 |
| Subordinated debentures | 3,700 | 148 | 5.35 | 3,700 |
| Total interest-bearing liabilities | 179,382 | 4,610 | 3.44 | 193,506 |
| Noninterest-bearing liabilities: | | | | |
| Demand deposits | 99,104 | | | 100,049 |
| Accounts and drafts payable | 462,314 | | | 386,097 |
| Other liabilities | 7,575 | | | 7,156 |
| Liabilities related to discontinued operations | 662 | | | 1,872 |
| Total liabilities | 749,037 | | | 688,680 |
| Shareholders' equity | 78,183 | | | 70,972 |
| Total liabilities and shareholders' equity | \$ 827,220 | | | \$ 759,652 |
| Net interest income | | \$ 31,093 | | |
| Interest spread | | | 2.91% | |
| Net interest margin | | | 5.53 | |

- Balances shown are daily averages.
- 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 2005 Consolidated Financial Statements, filed with the Company's 2005 Annual Report on Form 10-K.
- Interest income on loans includes net loan fees of \$164,000 and \$113,000 for the First Nine Months of 2006 and 2005, respectively.
- Interest income is presented on a tax-equivalent basis assuming a tax rate of 35%. The tax-equivalent adjustment was approximately \$1,122,000 and \$655,000 for the First Nine Months of 2006 and 2005, respectively.
- 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

Analysis of Net Interest Income Changes

The following table presents the changes in interest income and expense between periods due to changes in volume and interest rates. That portion of the change in interest attributable to the combined rate/volume variance has been allocated to rate and volume changes in proportion to the absolute dollar amounts of the change in each.

| (In Thousands) | Third Quarter 2006 Over 2005 | | |
|--|---------------------------------|----------|----------|
| | Volume | Rate | Total |
| Increase (decrease) in interest income: | | | |
| Loans (1,2): | | | |
| Taxable | \$ 233 | \$ 855 | \$ 1,088 |
| Tax-exempt (3) | 8 | 2 | 10 |
| Debt and equity securities: | | | |
| Taxable | (54) | 99 | 45 |
| Tax-exempt (3) | 431 | 13 | 444 |
| Federal funds sold and other short-term investments | 359 | 651 | 1,010 |
| Total interest income | 977 | 1,620 | 2,597 |
| Interest expense on: | | | |
| Interest-bearing demand deposits | (55) | 129 | 74 |
| Savings deposits | (16) | 82 | 66 |
| Time deposits of \$100 or more | 199 | 194 | 393 |
| Other time deposits | (76) | 95 | 19 |
| Short-term borrowings | 1 | -- | 1 |
| Subordinated debentures | -- | -- | -- |
| Total interest expense | 53 | 500 | 553 |
| Net interest income | \$ 924 | \$ 1,120 | \$ 2,044 |

1. Average balances include nonaccrual loans.
2. Interest income includes net loan fees.
3. Interest income is presented on a tax-equivalent basis assuming a tax rate of 35%.

| (In Thousands) | First Nine Months 2006 Over 2005 | | |
|--|-------------------------------------|----------|----------|
| | Volume | Rate | Total |
| Increase (decrease) in interest income: | | | |
| Loans (1,2): | | | |
| Taxable | \$ 852 | \$ 2,697 | \$ 3,549 |
| Tax-exempt (3) | 21 | 12 | 33 |
| Debt and equity securities: | | | |
| Taxable | (72) | 279 | 207 |
| Tax-exempt (3) | 1,262 | 35 | 1,297 |
| Federal funds sold and other short-term investments | 660 | 1,782 | 2,442 |
| Total interest income | 2,723 | 4,805 | 7,528 |
| Interest expense on: | | | |
| Interest-bearing demand deposits | (137) | 348 | 211 |

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

| | | | |
|--------------------------------|----------|----------|----------|
| Savings deposits | (48) | 148 | 100 |
| Time deposits of \$100 or more | 128 | 597 | 725 |
| Other time deposits | (158) | 293 | 135 |
| Short-term borrowings | -- | 2 | 2 |
| Subordinated debentures | -- | -- | -- |
| Total interest expense | (215) | 1,388 | 1,173 |
| ----- | | | |
| Net interest income | \$ 2,938 | \$ 3,417 | \$ 6,355 |
| ===== | | | |

4. Average balances include nonaccrual loans.
5. Interest income includes net loan fees.
6. Interest income is presented on a tax-equivalent basis assuming a tax rate of 35%.

-19-

Provision and Allowance for Loan Losses

An important determinant of the Company's operating results is the provision for loan losses and the level of loans charged off. There was a \$200,000 and \$225,000 provision made for loan losses during the Third Quarter of 2006 and the Third Quarter of 2005, respectively. There was a \$500,000 and \$625,000 provision made for loan losses during the First Nine Months of 2006 and the First Nine Months of 2005, respectively. As discussed below, the Company continually analyzes the outstanding loan portfolio based on the performance, financial condition and collateralization of the credits. There was \$583,000 of net loan charge-offs in the Third Quarter of 2006 and \$3,000 of recoveries in the Third Quarter 2005. There was \$855,000 of net loan charge-offs in the First Nine Months of 2006 and \$425,000 in the First Nine Months 2005.

The allowance for loan losses at September 30, 2006 was \$5,929,000 and at December 31, 2005 was \$6,284,000. The ratio of allowance for loan losses to total loans outstanding at September 30, 2006 was 1.14%, compared to 1.19% at December 31, 2005. Nonperforming loans were \$954,000 or .18% of total loans at September 30, 2006 compared to \$1,464,000 or .28% of total loans at December 31, 2005.

At September 30, 2006, nonperforming loans, which are also considered impaired, consisted of \$954,000 in non-accrual loans as shown in the following table. This total consists of three loans that relate to businesses that are for sale or are in process of liquidation. Nonperforming loans at December 31, 2005 consisted of \$983,000 in non-accrual loans and \$481,000 in loans that were still accruing interest although past due for over 90 days. Total nonperforming loans decreased \$180,000 from September 30, 2005 to September 30, 2006.

In addition to the nonperforming loans discussed above, at September 30, 2006, approximately \$5,868,000 of loans not included in the table below were identified by management as having potential credit problems. They may also be classified for regulatory purposes. These loans are excluded from the table due to the fact they are current under the original terms of the loans; however, circumstances have raised doubts as to the ability of the borrowers to comply with the current loan repayment terms. Included in this balance is \$3,795,000 related to one borrower that was renegotiated several years ago and although current under the new terms of the contract, management believes, due to the financial condition of the borrower, there still remains risk as to the collectability of all amounts under the loan agreement. The remaining loans are closely monitored by management and have specific reserves established for the estimated loss exposure.

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

The allowance for loan losses has been established and is maintained to absorb probable losses in the loan portfolio. An ongoing assessment of risk of loss is performed to determine if the current balance of the allowance is adequate to cover probable losses in the portfolio. A charge or credit is made to expense to cover any deficiency or reduce any excess. The current methodology employed to determine the appropriate allowance consists of two components, specific and general. The Company develops specific valuation allowances on commercial, real estate, and construction loans based on individual review of these loans and an estimate of the borrower's ability to repay the loan given the availability of collateral, other sources of cash flow and collection options available. The general component relates to all other loans, which are evaluated based on loan grade. The loan grade assigned to each loan is typically evaluated on an annual basis, unless circumstances require interim evaluation. The Company assigns a reserve amount consistent with each loan's rating category. The reserve amount is based on derived loss experience over prescribed periods. In addition to the amounts derived from the loan grades, a portion is added to the general reserve to take into account other factors including national and local economic conditions, downturns in specific industries including loss in collateral value, trends in credit quality at the Company and the banking industry, and trends in risk rating changes. As part of their examination process, federal and state agencies review the Company's methodology for maintaining the allowance for loan losses and the balance in the account. These agencies may require the Company to increase the allowance for loan losses based on their judgments and interpretations about information available to them at the time of their examination.

-20-

Summary of Asset Quality

| (Dollars in Thousands) | Three Months Ended September 30 | | Nine Se |
|--|------------------------------------|------------|------------|
| | 2006 | 2005 | 2006 |
| Allowance at beginning of period | \$ 6,312 | \$ 6,009 | \$ 6,28 |
| Provision charged to expense | 200 | 225 | 50 |
| Loans charged off | 586 | -- | 86 |
| Recoveries on loans previously charged off | 3 | 3 | |
| Net loans charged-off (recovered) | 583 | (3) | 85 |
| Allowance at end of period | \$ 5,929 | \$ 6,237 | \$ 5,92 |
| Loans outstanding: | | | |
| Average | \$ 527,784 | \$ 513,096 | \$ 528,25 |
| September 30 | 520,748 | 518,792 | 520,74 |
| Ratio of allowance for loan losses to loans outstanding: | | | |
| Average | 1.12% | 1.22% | 1.1 |
| September 30 | 1.14 | 1.20 | 1.1 |
| Nonperforming loans: | | | |
| Nonaccrual loans | \$ 954 | \$ 1,111 | \$ 95 |
| Loans past due 90 days or more | -- | 23 | - |
| Renegotiated loans | -- | -- | - |

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

| | | | | | | |
|--|----|------|----|-------|----|----|
| Total non performing loans | \$ | 954 | \$ | 1,134 | \$ | 95 |
| Foreclosed assets | | -- | | -- | | -- |
| <hr style="border-top: 1px dashed black;"/> | | | | | | |
| Nonperforming loans as percentage of average loans | | .18% | | .22% | | .1 |
| <hr style="border-top: 1px dashed black;"/> | | | | | | |

The Bank had no properties carried as other real estate owned as of September 30, 2006 and 2005 and December 31, 2005.

Operating Expense from Continuing Operations

Total operating expense for the Third Quarter of 2006 increased \$1,877,000 or 14% to \$15,021,000 compared to the Third Quarter of 2005 due primarily to expenses related to the 13% growth in processing activity. Total operating expense for the First Nine Months of 2006 increased \$4,404,000 or 11% to \$43,174,000 compared to the First Nine Months of 2005 due primarily to expenses related to the 13% growth in processing activity.

Salaries and benefits expense for the Third Quarter of 2006 increased \$1,536,000 or 16% to \$11,136,000 compared to the Third Quarter of 2005 and increased \$3,393,000 or 12% to \$31,673,000 for the First Nine Months of 2006 compared to the First Nine Months of 2005 primarily due to additional headcount to service new transaction business, an increase in pension expense for both of the Company's plans and an increase in bonuses related to the earnings increase over the comparable period last year.

Occupancy expense for the Third Quarter of 2006 increased \$23,000 or 5% to \$522,000 from the Third Quarter of 2005 and increased \$19,000 or 1% from the First Nine Months of 2005 compared to the First Nine Months of 2006.

Equipment expense for the Third Quarter of 2006 increased \$16,000 or 2% compared to the Third Quarter of 2005 due to additional depreciation on asset purchases and decreased \$18,000 from the First Nine Months of 2005 compared to the First Nine Months of 2006 mainly due to the amortization of internally developed software that was fully amortized in the Fourth Quarter of 2005.

Amortization of intangible assets for the Third Quarter and the First Nine Months of 2006 increased \$28,000 or 67% compared to the Third Quarter of 2005 and 22% compared to the First Nine Months of 2005 due to the amortization of the customer list acquired with the NTransit purchase in July, 2006.

Other operating expense for the Third Quarter of 2006 increased \$274,000, or 12% compared to the Third Quarter of 2005 and increased \$982,000 or 15% from the First Nine Months of 2005 compared to the First Nine Months of 2006. The increases were due to increases in outside services expense and expenses related to the Bank's 100th year anniversary celebrations.

Income tax expense for the Third Quarter of 2006 increased \$535,000 or 32% compared to the Third Quarter of 2005 and increased \$1,851,000 or 41% for the First Nine Months of 2006 compared to the First Nine Months of 2005. The effective tax rate was 35.7% and 33.8% for the Third Quarter of 2006 and for the Third Quarter of 2005, respectively, and was 35.4% and 34.0% for the First Nine Months of 2006 and 2005, respectively. The increase in the effective tax rate was due to an increase in the Company's federal statutory tax rate in 2006 to 35% versus 34% in 2005.

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

Total assets at September 30, 2006 were \$886,414,000, an increase of \$67,716,000, or 8% from December 31, 2005. The most significant changes in asset balances during this period was an increase of \$68,176,000 or 57% in federal funds sold and other short-term investments. Changes in federal funds sold and other short-term investments reflect the Company's daily liquidity position and are affected by the changes in the other asset balances, deposits and accounts and draft payable balances.

Total liabilities were \$802,441,000, an increase of \$59,024,000, or 8% from December 31, 2005. Total deposits at September 30, 2006 were \$275,188,000, a decrease of \$11,810,000 or 4%. Accounts and drafts payable were \$514,193,000, an increase of \$68,382,000 or 15%. Total shareholders' equity at September 30, 2006 was \$83,973,000, an increase of \$8,692,000 or 12% increase from December 31, 2005.

Deposits in the First Nine Months of 2006 decreased as customers moved funds into other higher-yielding investments. Accounts and drafts payable will fluctuate from period-end to period-end due to the payment processing cycle, which results in lower balances on days when checks clear and higher balances on days when checks are issued. For this reason, average balances are a more meaningful measure of accounts and drafts payable (for average balances refer to the tables under the "Distribution of Assets, Liabilities and Stockholders' Equity; Interest Rate and Interest Differential" section of this report).

The increase in total shareholders' equity for the First Nine Months of 2006 resulted from net income of \$11,371,000, cash received on the exercise of stock options of \$330,000, \$64,000 tax benefit on stock and option awards, \$159,000 from the amortization of stock bonus awards, an increase in other comprehensive income of \$307,000, offset by dividends paid of \$2,669,000 (\$.16 per share) and the purchase of common shares for treasury of \$870,000.

Liquidity and Capital Resources

The balance of liquid assets consists of cash and cash equivalents, which include cash and due from banks, federal funds sold and money market funds, and was \$219,840,000 at September 30, 2006, an increase of \$70,148,000 or 47% from December 31, 2005. At September 30, 2006, these assets represented 25% of total assets. These funds are the Company's and its subsidiaries' primary source of liquidity to meet future expected and unexpected loan demand, depositor withdrawals or reductions in accounts and drafts payable.

Secondary sources of liquidity include the investment portfolio and borrowing lines. Total investment in securities was \$87,871,000 at September 30, 2006, a decrease of \$6,988,000 from December 31, 2005. These assets represented 10% of total assets at September 30, 2006. Of this total, 75% were state and political subdivision securities, 19% were U.S. Treasury securities, 5% were U.S. government agencies and 1% was other securities. Of the total portfolio, 20% mature in one year, 22% mature in one to five years, and 58% mature in five or more years. During the Third Quarter of 2006 the Company did not sell any securities.

The Bank has unsecured lines of credit at correspondent banks to purchase federal funds up to a maximum of \$29,000,000. Additionally, the Bank maintains a line of credit at unaffiliated financial institutions in the maximum amount of \$57,962,000 collateralized by U.S. Treasury and agency securities and commercial and residential mortgage loans.

The deposits of the Company's banking subsidiary have historically been stable, consisting of a sizable volume of core deposits related to customers that utilize other commercial products of the Bank. The accounts and drafts payable generated by the Company has also historically been a stable source of funds.

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

Net cash flows provided by operating activities were \$12,870,000 for the First Nine Months of 2006 compared with \$9,762,000 for the First Nine Months of 2005. This increase is attributable to the increase in net income from continuing operations of \$2,822,000, the absence of a gain on sales of investment securities in 2006 compared to \$547,000 in 2005, offset by a decrease of \$1,431,000 in operating activities related to discontinued operations plus the other normal fluctuations in asset and liability accounts. Net cash flows from investing and financing activities fluctuate greatly as the Company actively manages its investment and loan portfolios. Customer activity influences changes in deposits and accounts and drafts payable balances. Other causes for the changes in these account balances are discussed earlier in this report. Due to the daily fluctuations in these account balances, the analysis of changes in average balances, also discussed earlier in this report, can be more indicative of underlying activity than the period-end balances used in the statements of cash flows. Management anticipates that cash and cash equivalents, maturing investments and cash from operations will continue to be sufficient to fund the Company's operations and capital expenditures in 2006.

-22-

The Company faces market risk to the extent that its net interest income and fair market value of equity are affected by changes in market interest rates. For information regarding the market risk of the Company's financial instruments, see Item 3. "QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK".

Risk-based capital guidelines require the Company to meet a minimum total capital ratio of 8.0% of which at least 4.0% must consist of Tier 1 capital. Tier 1 capital generally consists of (a) common shareholders' equity (excluding the unrealized market value adjustments on the available-for-sale securities), (b) qualifying perpetual preferred stock and related surplus subject to certain limitations specified by the FDIC, (c) minority interests in the equity accounts of consolidated subsidiaries less (d) goodwill, (e) mortgage servicing rights within certain limits and (f) any other intangible assets and investments in subsidiaries that the FDIC determines should be deducted from Tier 1 capital. The FDIC also requires a minimum leverage ratio of 3.0%, defined as the ratio of Tier 1 capital less purchased mortgage servicing rights to total assets, for banking organizations deemed the strongest and most highly rated by banking regulators. A higher minimum leverage ratio is required of less highly-rated banking organizations. Total capital, a measure of capital adequacy, includes Tier 1 capital, allowance for loan losses, and debt considered equity for regulatory capital purposes.

The Company and the Bank continue to exceed all regulatory capital requirements, as evidenced by the following capital amounts and ratios at September 30, 2006 and December 31, 2005:

| September 30, 2006 (Dollars In Thousands) | Amount | Ratio |
|---|-----------|--------|
| ===== | | |
| Total capital (to risk-weighted assets) | | |
| Cass Information Systems, Inc. | \$ 85,067 | 13.32% |
| Cass Commercial Bank | 42,933 | 14.92 |
| Tier I capital (to risk-weighted assets) | | |
| Cass Information Systems, Inc. | \$ 75,438 | 11.81% |
| Cass Commercial Bank | 38,699 | 13.45 |
| Tier I capital (to average assets) | | |
| Cass Information Systems, Inc. | \$ 75,438 | 8.91% |
| Cass Commercial Bank | 38,699 | 11.58 |
| ===== | | |

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

| December 31, 2005 (Dollars In Thousands) | Amount | Ratio |
|--|-----------|--------|
| ===== | | |
| Total capital (to risk-weighted assets) | | |
| Cass Information Systems, Inc. | \$ 80,066 | 12.80% |
| Cass Commercial Bank | 42,597 | 14.64 |
| Tier I capital (to risk-weighted assets) | | |
| Cass Information Systems, Inc. | \$ 70,082 | 11.21% |
| Cass Commercial Bank | 38,251 | 13.15 |
| Tier I capital (to average assets) | | |
| Cass Information Systems, Inc. | \$ 70,082 | 8.52% |
| Cass Commercial Bank | 38,251 | 11.16 |
| ===== | | |

Stock Dividend

The Company paid a 50% stock dividend on September 15, 2006, to shareholders of record at the close of trading September 1, 2006. Shareholders received one additional share of the Company's stock for each two shares owned.

Inflation

The Company's assets and liabilities are primarily monetary, consisting of cash, cash equivalents, securities, loans, payables and deposits. Monetary assets and liabilities are those that can be converted into a fixed number of dollars. The Company's consolidated balance sheet reflects a net positive monetary position (monetary assets exceed monetary liabilities). During periods of inflation, the holding of a net positive monetary position will result in an overall decline in the purchasing power of a company. Management believes that replacement costs of equipment, furniture, and leasehold improvements will not materially affect operations. The rate of inflation does affect certain expenses, such as those for employee compensation, which may not be readily recoverable in the price of the Company's services.

-23-

Impact of New Accounting Pronouncements

In November 2005, the Financial Accounting Standards Board ("FASB") issued FASB Staff Position ("FSP") FAS 115-1 and 124-1, "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments." The guidance addresses the determination of when an investment is considered impaired, whether that impairment is other than temporary, and the measurement of an impairment loss. The FSP also includes accounting considerations subsequent to the recognition of an other-than-temporary impairment and requires certain disclosures about unrealized losses that have not been recognized as other-than-temporary impairments. The guidance in this FSP amends FASB Statement No. 115, "Accounting for Certain Investments in Debt and Equity Securities," and adds a footnote to APB Opinion No. 18, "The Equity Method of Accounting for Investments in Common Stock." The guidance in this FSP nullifies certain requirements of the Emerging Issues Task Force ("EITF"), Issue No. 03-1, "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments," and supersedes EITF Abstracts, Topic D-44, "Recognition of Other-Than-Temporary Impairment upon the Planned Sale of a Security Whose Cost Exceeds Fair Value." The Company applied this guidance effective January 1, 2006 and there was no material impact on its consolidated financial statements.

In December 2004, the FASB issued SFAS No. 123 (Revised 2004), "Share-Based Payment". This Statement addresses the accounting for transactions in which an entity exchanges its equity instruments for goods or services. The Statement

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

eliminates the ability to account for share-based compensation transactions using APB Opinion No. 25, "Accounting for Stock Issued to Employees", and generally requires instead that such transactions be accounted for using a fair-value based method. For public entities, the cost of employee services received in exchange for an award of equity instruments, such as stock options, will be measured based on the grant-date fair value of those instruments, and that cost will be recognized over the period during which an employee is required to provide service in exchange for the award (usually the vesting period). This Statement was adopted by the Company on January 1, 2006. The implementation of SFAS No. 123R did not have a material effect on the Company's financial condition or results of operations. See Note 10 to the financial statements.

In May 2005, the FASB issued SFAS No. 154 "Accounting Changes and Error Corrections" as a replacement of APB Opinion No. 20 and FASB Statement No. 3. This Statement applies to all voluntary changes in accounting principles and changes required by an accounting pronouncement in the unusual instance that the pronouncement does not include specific transition provisions. This Statement carries forward without change the guidance contained in APB Opinion No. 20 for reporting the correction of an error in previously issued financial statements and a change in accounting estimate. This Statement also carries forward the guidance in APB Opinion No. 20 requiring justification of a change in accounting principle on the basis of preferability. This Statement was adopted by the Company on January 1, 2006 and there was no material impact on its consolidated financial statements.

In June 2006, the FASB issued FASB Interpretation No. 48 "Accounting for Uncertainty in Income Taxes", an Interpretation of SFAS No. 109 "Accounting for Income Taxes". FASB Interpretation No. 48 clarifies the accounting for uncertainty in income taxes in financial statements and prescribes a recognition threshold and measurement attribute for financial statement recognition and measurement of a tax position taken or expected to be taken. The Interpretation also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. The FASB Interpretation is effective for fiscal years beginning after December 15, 2006. The Company is currently evaluating the requirements of FASB Interpretation No. 48 to determine the impact on its financial condition and results of operations.

In September 2006, the FASB issued Statement No. 157, "Fair Value Measurements" ("SFAS No. 157"). SFAS No. 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements. It applies under other accounting pronouncements that require or permit fair value measurements; therefore, it does not require any new fair value measurements. This statement is effective for financial statements issued for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. The company is currently assessing the impact of SFAS No. 157 on its financial statements.

In September 2006, the FASB issued Statement 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 No. 158"). SFAS No. 158 requires companies to recognize the overfunded or underfunded status of a defined benefit postretirement plan as an asset or liability in its statement of financial position and to recognize changes in that funded status in the year in which the changes occur through comprehensive income. The funded status is measured as the difference between the fair value of the plan assets and the benefit obligation as of the date of its fiscal year-end. Additional footnote disclosures will also be required. This statement is effective for fiscal years ending after December 15, 2006. The Company is currently assessing the impact of SFAS No. 158 on its financial statements.

In September 2006, the SEC issued Staff Accounting Bulletin No. 108,

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

"Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements" ("SAB No. 108"). SAB No. 108 provides interpretive guidance on the consideration of the effects of prior year misstatements in quantifying current year misstatements for the purpose of a materiality assessment. This statement is effective for fiscal years ending after November 15, 2006. The company is currently assessing the impact of SAB No. 108 on its financial statements.

-24-

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

As described in the Company's Annual Report on Form 10-K for the year ended December 31, 2005, the Company manages its interest rate risk through measurement techniques that include gap analysis and a simulation model. As part of the risk management process, asset/liability management policies are established and monitored by management. The policy objective is to limit the change in annualized net interest income to 15% from an immediate and sustained parallel change in interest rates of 200 basis points. Based on the Company's most recent evaluation, management does not believe the Company's risk position at September 30, 2006 has changed materially from that at December 31, 2005.

ITEM 4. CONTROLS AND PROCEDURES

The Company maintains disclosure controls and procedures designed to ensure that the information it is required to disclose in the reports it files with the Securities and Exchange Commission ("SEC") is recorded, processed, summarized and reported to management, including the Chief Executive Officer and Principal Financial Officer, within the time periods specified in the rules of the SEC. The Company's Chief Executive Officer and Principal Financial Officer have evaluated the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended) as of September 30, 2006 and based on their evaluation, believe that, as of September 30, 2006, these controls and procedures were effective at the reasonable assurance level to ensure that the Company is able to collect, process and disclose the information it is required to disclose in the reports it files with the SEC within the required time periods.

There were no changes in the Third Quarter of 2006 in the Company's internal control over financial reporting identified by the Chief Executive Officer and Principal Financial Officer in connection with their evaluation that materially affected or are reasonably likely to materially affect the Company's internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934, as amended).

-25-

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

The Company and its subsidiaries are not involved in any pending proceedings other than ordinary routine litigation incidental to its businesses. Management believes none of these proceedings, if determined adversely, would have a material effect on the business or financial conditions of the Company or its subsidiaries.

ITEM 1A. RISK FACTORS

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

There have been no material changes from the risk factors as previously disclosed in the Company's Annual Report on Form 10-K for the year ended December 31, 2005.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

The Company maintains a treasury stock buyback program pursuant to which the Board of Directors authorized the repurchase of up to 150,000 shares of the Company's common stock effective as of April 18, 2006. The Company did not repurchase any shares during the three months ended September 30, 2006. Repurchases are made in the open market or through negotiated transactions from time to time depending on market conditions. The information contained in Note 5 to the financial statements filed with this report is incorporated herein by reference.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None

ITEM 5. OTHER INFORMATION

None

ITEM 6. EXHIBITS

Exhibit 3.1 Articles of Merger of Cass Commercial Corporation.

Exhibit 31.1 Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

Exhibit 31.2 Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

Exhibit 32.1 Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

Exhibit 32.2 Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

-26-

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.

CASS INFORMATION SYSTEMS, INC.

DATE: November 6, 2006

By /s/ Lawrence A. Collett

Lawrence A. Collett
Chairman and Chief Executive Officer
(Principal Executive Officer)

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

DATE: November 6, 2006

By /s/ P. Stephen Appelbaum

P. Stephen Appelbaum
Chief Financial Officer
(Principal Financial and
Accounting Officer)

-27-