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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 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 March 31, 2001

Commission file number 0-13814

Cortland Bancorp
(Exact name of registrant as specified in its charter)

Ohio	34-1451118
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

194 West Main Street, Cortland, Ohio 44410
(Address of principal executive offices) (Zip Code)

(330) 637-8040
(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 ☐

APPLICABLE ONLY TO CORPORATE ISSUERS:

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

Class	Outstanding at May 8, 2001
Common Stock, No Par Value	3,801,475 Shares

PART I – FINANCIAL INFORMATION

PART II – OTHER INFORMATION

CORTLAND BANCORP AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS (UNAUDITED)

(Amounts in thousands, except share data)

	MARCH 31, 2001	DECEMBER 31, 2000
ASSETS		
Cash and due from banks	**$ 10,994**	$ 13,437
Federal funds sold	**9,650**	1,450
Total cash and cash equivalents	**20,644**	14,887
Investment securities available for sale (Note 3)	**126,228**	132,906
Investment securities held to maturity (approximate market value of $66,600 in 2001 and $62,958 in 2000) (Note 3)	**66,115**	63,058
Total loans (Note 4)	**205,217**	204,968
Less allowance for loan losses (Note 4)	**(3,021)**	(2,974)
Net loans	**202,196**	201,994
Premises and equipment	**6,020**	6,002
Other assets	**11,026**	10,619
Total assets	**$ 432,229**	$ 429,466
LIABILITIES		
Noninterest-bearing deposits	**$ 45,839**	$ 50,079
Interest-bearing deposits	**283,492**	279,870
Total deposits	**329,331**	329,949
Federal Home Loan Bank advances and other borrowings	**48,912**	49,468
Other liabilities	**4,944**	2,313
Total liabilities	**383,187**	381,730
Commitments and contingent liabilities (Notes 4 & 5)		
SHAREHOLDERS' EQUITY		
Common stock – $5.00 stated value – authorized 20,000,000 shares; issued 3,887,484 shares in 2001 and 3,887,484 in 2000 (Note 6)	**19,437**	19,437
Additional paid-in capital (Note 6)	**9,271**	9,271
Retained earnings	**20,222**	19,789
Accumulated other comprehensive income	**1,629**	896
Treasury stock, at cost, 85,673 shares in 2001 and 95,573 shares in 2000	**(1,517)**	(1,657)
Total shareholders' equity	**49,042**	47,736
Total liabilities and shareholders' equity	**$ 432,229**	$ 429,466

See accompanying notes to consolidated financial statements
of Cortland Bancorp and Subsidiaries

CORTLAND BANCORP AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)

(Amounts in thousands, except per share data)

	THREE MONTHS ENDED MARCH 31,	
	2001	**2000**
INTEREST INCOME		
Interest and fees on loans	**$ 4,434**	$ 4,265
Interest and dividends on investment securities:		
Taxable interest income	**1,188**	1,259
Nontaxable interest income	**442**	447
Dividends	**72**	71
Interest on mortgage-backed securities	**1,346**	1,392
Other interest income	**76**	11
Total interest income	**7,558**	7,445
INTEREST EXPENSE		
Deposits	**3,022**	2,625
Borrowed funds	**682**	691
Total interest expense	**3,704**	3,316
Net interest income	**3,854**	4,129
Provision for loan losses	**75**	100
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	**3,779**	4,029
OTHER INCOME		
Fees for other customer services	**367**	321
Investment securities gains – net	**126**	5
Gain on sale of loans – net	**10**	12
Other non-interest income	**143**	34
Total other income	**646**	372
OTHER EXPENSES		
Salaries and employee benefits	**1,536**	1,467
Net occupancy expense	**212**	199
Equipment expense	**305**	270
State and local taxes	**155**	148
Office supplies	**127**	132
Marketing expense	**20**	48
Other operating expenses	**391**	415
Total other expenses	**2,746**	2,679
INCOME BEFORE FEDERAL INCOME TAXES	**1,679**	1,722
Federal income taxes	**406**	444
NET INCOME	**$ 1,273**	$ 1,278
BASIC EARNINGS PER COMMON SHARE (NOTE 6)	**$ 0.33**	$ 0.33
DILUTED EARNINGS PER COMMON SHARE (NOTE 6)	**$ 0.33**	$ 0.33
CASH DIVIDENDS DECLARED PER SHARE	**$ 0.22**	$ 0.17

See accompanying notes to consolidated financial statements
of Cortland Bancorp and Subsidiaries

CORTLAND BANCORP AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY (UNAUDITED)

(Amounts in thousands)

	COMMON STOCK	ADDITIONAL PAID-IN CAPITAL	RETAINED EARNINGS	ACCUMULATED OTHER COMPREHENSIVE INCOME	TREASURY STOCK	TOTAL SHARE-HOLDERS' EQUITY
BALANCE AT JANUARY 1, 2001	**$ 19,437**	**$ 9,271**	**$ 19,789**	**$ 896**	**($1,657)**	**$ 47,736**
Comprehensive income:						
Net income			1,273			1,273
Other comprehensive income, net of tax:						
Unrealized gains or (losses) on available-for-sale securities, net of reclassification adjustment				733		733
Total comprehensive income						2,006
Common stock transactions:						
Shares sold						
Treasury shares reissued net of shares repurchased					140	140
Cash dividends declared			(840)			(840)
BALANCE AT MARCH 31, 2001	**$ 19,437**	**$ 9,271**	**$ 20,222**	**$ 1,629**	**($1,517)**	**$ 49,042**
DISCLOSURE OF RECLASSIFICATION FOR AVAILABLE FOR SALE SECURITY GAINS AND LOSSES:						
Net unrealized holding gains or (losses) on available-for -sale securities arising during the period, net of tax				$ 650		
Less: Reclassification adjustment for net gains realized in net income, net of tax				(83)		
Net unrealized gains on available- for-sale securities, net of tax				$ 733		

See accompanying notes to consolidated financial statements of Cortland Bancorp and Subsidiaries

CORTLAND BANCORP AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

(Amounts in thousands)

	FOR THE THREE MONTHS ENDED MARCH 31, 2001	2000
NET CASH FLOWS FROM OPERATING ACTIVITIES	**$ 3,367**	$ 150
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of securities held to maturity	**(8,716)**	(3,350)
Purchases of securities available for sale	**(4,268)**	(4,175)
Proceeds from sales of securities available for sale		3,016
Proceeds from call, maturity and principal payments on securities	**17,750**	5,906
Net decrease (increase) in loans made to customers	**(277)**	(6,186)
Proceeds from disposition of other real estate		42
Proceeds from sale of fixed assets	**9**	29
Purchase of premises and equipment	**(234)**	(201)
Net cash flows from investing activities	**4,264**	(4,919)
CASH FLOWS FROM FINANCING ACTIVITIES		
Net increase (decrease) in deposit accounts	**(618)**	6,279
Net increase (decrease) in borrowings	**(556)**	(6,669)
Dividends paid	**(840)**	(678)
Purchases of treasury stock		(945)
Treasury shares reissued net of shares repurchased	**140**	
Proceeds from sale of common stock		817
Net cash flows from financing activities	**(1,874)**	(1,196)
NET CHANGE IN CASH AND CASH EQUIVALENTS	**5,757**	(5,965)
CASH AND CASH EQUIVALENTS		
Beginning of period	**14,887**	16,568
End of period	**$ 20,644**	$ 10,603
SUPPLEMENTAL DISCLOSURES		
Interest paid	**$ 3,720**	$ 3,329
Income taxes paid	**$ 0**	$ 0

See accompanying notes to consolidated financial statements of Cortland Bancorp and Subsidiaries

CORTLAND BANCORP AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

(Dollars in thousands)

1.) Management Representation:

The accompanying unaudited consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring items) considered necessary for a fair presentation have been included. Operating results for the three months ended March 31, 2001 are not necessarily indicative of the results that may be expected for the year ending December 31, 2001. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company’s annual report on Form 10-K for the year ended December 31, 2000.

2.) Reclassifications:

Certain items contained in the 2000 financial statements have been reclassified to conform with the presentation for 2001. Such reclassifications had no effect on the net results of operations.

3.) Investment Securities:

Securities classified as held to maturity are those that management has the positive intent and ability to hold to maturity. Securities held to maturity are stated at cost, adjusted for amortization of premiums and accretion of discounts, with such amortization or accretion included in interest income.

Securities classified as available for sale are those that could be sold for liquidity, investment management, or similar reasons even though management has no present intentions to do so. Securities available for sale are carried at fair value using the specific identification method. Changes in the unrealized gains and losses on available for sale securities are recorded net of tax effect as a component of comprehensive income.

Trading securities are principally held with the intention of selling in the near term. Trading securities are carried at fair value with changes in fair value reported in the Consolidated Statements of Income.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

(Dollars in thousands)

Realized gains or losses on dispositions are based on net proceeds and the adjusted carrying amount of securities sold, using the specific identification method. The table below sets forth the proceeds, gains and losses realized on securities sold or called for the period ended:

	THREE MONTHS March 31, 2001	THREE MONTHS March 31, 2000
Proceeds on securities sold	$ 0	$ 3,016
Gross realized gains	0	5
Gross realized losses	0	0
Proceeds on securities called	4,745	0
Gross realized gains	126	0
Gross realized losses	0	0

Securities available for sale, carried at fair value, totalled $126,228 at March 31, 2001 and $132,906 at December 31, 2000 representing 65.6% and 67.8%, respectively, of all investment securities. These levels were deemed to provide an adequate level of liquidity in management's opinion.

Investment securities with a carrying value of approximately $50,027 at March 31, 2001 and $52,670 at December 31, 2000 were pledged to secure deposits and for other purposes.

CORTLAND BANCORP AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

(Dollars in thousands)

The amortized cost and estimated market value of debt securities at March 31, 2001, by contractual maturity, are shown below. Expected maturities may differ from contractual maturities because borrowers have the right to call or prepay certain obligations with or without call or prepayment penalties.

Investment securities available for sale	AMORTIZED COST	ESTIMATED FAIR VALUE
Due in one year or less	$ 6,098	$ 6,119
Due after one year through five years	7,447	7,632
Due after five years through ten years	16,204	16,826
Due after ten years	17,182	17,931
	46,931	48,508
Mortgage-backed Securities	71,974	73,023
	$ 118,905	$ 121,531

Investment securities held to maturity	AMORTIZED COST	ESTIMATED FAIR VALUE
Due in one year or less	$ 1,096	$ 1,097
Due after one year through five years	334	337
Due after five years through ten years	23,441	23,681
Due after ten years	29,114	29,303
	53,985	54,418
Mortgage-backed Securities	12,130	12,182
	$ 66,115	$ 66,600

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

(Dollars in thousands)

The amortized cost and estimated fair value of investment securities available for sale and investment securities held to maturity as of March 31, 2001, are as follows:

Investment securities available for sale	AMORTIZED COST	GROSS UNREALIZED GAINS	GROSS UNREALIZED LOSSES	ESTIMATED FAIR VALUE
U.S. Treasury Securities	$ 8,388	$ 724	$ 0	$ 9,112
U.S. Government agencies and corporations	21,180	743	6	21,917
Obligations of states and political subdivisions	17,363	207	91	17,479
Mortgage-backed and related securities	71,974	1,101	52	73,023
Total	118,905	2,775	149	121,531
Marketable equity Securities	2,111	93	261	1,943
Other securities	2,754	0	0	2,754
Total available for sale	$123,770	$2,868	$ 410	$126,228

Investment securities held to maturity	AMORTIZED COST	GROSS UNREALIZED GAINS	GROSS UNREALIZED LOSSES	ESTIMATED FAIR VALUE
U.S. Government agencies and corporations	$32,171	$ 438	$ 9	$32,600
Obligations of states and political subdivisions	21,814	212	208	21,818
Mortgage-backed and related securities	12,130	78	26	12,182
Total held to maturity	$66,115	$ 728	$ 243	$66,600

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

(Dollars in thousands)

The following provides a summary of the amortized cost and estimated fair value of investment securities available for sale and investment securities held to maturity as of December 31, 2000:

Investment securities available for sale	AMORTIZED COST	GROSS UNREALIZED GAINS	GROSS UNREALIZED LOSSES	ESTIMATED FAIR VALUE
U.S. Treasury Securities	$ 8,413	$ 689	$ 1	$ 9,101
U.S. Government agencies and corporations	28,656	611	67	29,200
Obligations of states and political subdivisions	16,638	138	80	16,696
Mortgage-backed and related securities	73,029	521	274	73,276
Total	126,736	1,959	422	128,273
Marketable equity securities	2,111	91	279	1,923
Other securities	2,710	0	0	2,710
Total available for sale	$131,557	$2,050	$ 701	$132,906

Investment securities held to maturity	AMORTIZED COST	GROSS UNREALIZED GAINS	GROSS UNREALIZED LOSSES	ESTIMATED FAIR VALUE
U.S. Government agencies and corporations	$34,429	$ 150	$ 198	$34,381
Obligations of states and political subdivisions	19,848	184	219	19,813
Mortgage-backed and related securities	8,781	104	121	8,764
Total held to maturity	$63,058	$ 438	$ 538	$62,958

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

(Dollars in thousands)

4.) Concentration of Credit Risk and Off Balance Sheet Risk:

The Company is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit, standby letters of credit, and financial guarantees. Such instruments involve, to varying degrees, elements of credit risk in excess of the amount recognized on the balance sheet. The contract or notional amounts of those instruments reflect the extent of involvement the Company has in particular classes of financial instruments.

In the event of nonperformance by the other party, the Company’s exposure to credit loss on these financial instruments is represented by the contract or notional amount of the instrument. The Company uses the same credit policies in making commitments and conditional obligations as it does for instruments recorded on the balance sheet. The amount and nature of collateral obtained, if any, is based on management’s credit evaluation.

	CONTRACT OR NOTIONAL AMOUNT	
	March 31, 2001	**December 31, 2000**
Financial instruments whose contract amount represents credit risk:		
Commitments to extend credit:		
Fixed rate	$ 2,652	$ 1,280
Variable	32,592	30,221
Standby letters of credit	237	237

Standby letters of credit are conditional commitments issued by the Company to guarantee the performance of a customer to a third party. 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. Generally these financial arrangements have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of these commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

(Dollars in thousands)

The Company, through its subsidiary bank, grants residential, consumer and commercial loans, and also offers a variety of saving plans to customers located primarily in Northeast Ohio and Western Pennsylvania. The following represents the composition of the loan portfolio:

	March 31, 2001	December 31, 2000
1-4 family residential mortgages	40.8%	41.2%
Commercial mortgages	35.1%	34.9%
Consumer loans	8.9%	8.7%
Commercial loans	11.5%	11.6%
Home equity loans	3.7%	3.6%

There are no mortgage loans held for sale included in 1-4 family residential mortgages as of March 31, 2001, or at December 31, 2000.

The following table sets forth the aggregate balance of underperforming loans for each of the following categories at March 31, 2001 and December 31, 2000:

	March 31, 2001	December 31, 2000
Loans accounted for on a nonaccrual basis	$ 1,870	$ 1,648
Loans contractually past due 90 days or more as to interest or principal payments (not included in nonaccrual loans above)	10	9
Loans considered troubled debt restructurings (not included in nonaccrual loans or loans contractually past due above)	140	143

CORTLAND BANCORP AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

(Dollars in thousands)

The following shows the amounts of contractual interest income and interest income actually reflected in income on loans accounted for on a nonaccrual basis and loans considered troubled debt restructuring as of March 31, 2001.

	March 31, 2001	March 31, 2000
Gross interest income that would have been recorded if the loans had been current in accordance with their original terms	$ 68	$ 92
Interest income actually included in income on the loan	32	56

A loan is placed on a nonaccrual basis whenever sufficient information is received to question the collectibility of the loan or any time legal proceedings are initiated involving a loan. When a loan is placed on nonaccrual status, any interest that has been accrued and not collected on the loan is charged against earnings. Cash payments received while a loan is classified as nonaccrual are recorded as a reduction to principal or reported as interest income according to management’s judgement as to collectibility of principal.

Impaired loans are generally included in nonaccrual loans. Management does not individually evaluate certain smaller balance loans for impairment as such loans are evaluated on an aggregate basis. These loans include 1-4 family , consumer and home equity loans. Impaired loans were evaluated using the fair value of collateral as the measurement method. At March 31, 2001, the recorded investment in impaired loans was $282.

As of March 31, 2001, there were $1,514 in loans not included in the above categories and not considered impaired, but which can be considered potential problem loans.

Any loans classified for regulatory purposes as loss, doubtful, substandard, or special mention that have not been disclosed above do not (i) represent or result from trends or uncertainties which management reasonably expects will materially impact future operating results, liquidity, or capital resources, or (ii) represent material credits about which management is aware of any information which causes management to have serious doubts as to the ability of such borrowers to comply with the loan repayment terms.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

(Dollars in thousands)

The following is an analysis of the allowance for loan losses for the three month periods ended March 31, 2001 and March 31, 2000:

	2001	2000
Balance at beginning of period	$2,974	$2,956
Loan charge-offs:		
1-4 family residential mortgages		
Commercial mortgages		104
Consumer loans	50	53
Commercial loans		
Home equity loans	3	5
	53	162
Recoveries on previous loan losses:		
1-4 family residential mortgages		
Commercial mortgages		1
Consumer loans	24	18
Commercial loans	1	3
Home equity loans		1
	25	23
Net charge-offs	(28)	(139)
Provision charged to operations	75	100
Balance at end of period	$3,021	$2,917
Ratio of annualized net charge-offs to average net loans outstanding	0.05%	0.28%

For each of the periods presented above, the provision for loan losses charged to operations is based on management's judgment after taking into consideration all known factors connected with the collectibility of the existing portfolio. Management evaluates the portfolio in light of economic conditions, changes in the nature and volume of the portfolio, industry standards and other relevant factors. Specific factors considered by management in determining the amounts charged to operations include previous loan loss experience, the status of past due interest and principal payments, the quality of financial information supplied by customers and the general economic conditions present in the lending area of the Company's bank subsidiary.

5.) Legal Proceedings:

The Company's subsidiary bank was a defendant in a class action lawsuit Frank Slentz, et al. v. Cortland Savings and Banking Company, involving purchased interests in two campgrounds.

(Dollars in thousands except per share data)

On October 20, 1997 the judge presiding over this case filed a judgment entry dismissing all claims against the Bank without prejudice. The judgment was appealed by the plaintiffs. On March 2, 1999, the United States Court of Appeals for the Sixth Circuit affirmed the decision of the district court to grant summary judgment in favor of the defendant Bank. The plaintiffs have the right to appeal to the United States Supreme Court. Plaintiffs have also filed a similar suit in the Common Pleas Court of Trumbull County. Accordingly, the ultimate outcome of this litigation presently cannot be determined, and therefore no provision for any liability relative to such litigation has been made in the accompanying consolidated financial statements.

In a case filed in 1990 regarding campground loans in Pennsylvania, the subsidiary bank's board of directors agreed to a negotiated settlement proposed by plaintiffs' attorney during the second quarter of 2000 as it did not materially exceed the anticipated cost of continuing to defend against the complainant. The Bank recorded an additional expense provision of $240,000 during 2000, bringing the litigation accrual to the agreed upon settlement amount of $375,000, which was fully disbursed in the first quarter of 2001.

The Bank is also involved in other legal actions arising in the ordinary course of business. In the opinion of management, the outcome of these matters is not expected to have any material effect on the Company.

6.) Earnings Per Share and Capital Transactions:

The following table sets forth the computation of basic earnings per common share and diluted earnings per common share.

	THREE MONTHS ENDED MARCH 31,	
	2001	**2000**
Net Income	$ 1,273	$ 1,278
Weighted average common shares outstanding *	3,815,511	3,867,378
Basic earnings per share *	$ 0.33	$ 0.33
Diluted earnings per share *	$ 0.33	$ 0.33

* Average shares outstanding and resultant per share amounts have been restated to give retroactive effect to the 3% stock dividend of January 1, 2001.

(Dollars in thousands except per share data)

7.) Stock Repurchase Program

On January 26, 2000, the Company's Board of Directors approved a Stock Repurchase Program (the “Program”) under which the Company could repurchase up to 185,000 shares (or approximately 4.9% of the 3,764,759 shares outstanding as of January 26, 2000) of the Company's outstanding common stock. The Program expired on February 3, 2001. On January 23, 2001 the Company's Board of Directors approved a new Program which allows the Company to repurchase up to 187,000 shares (or approximately 4.9% of the 3,815,125 shares outstanding as of January 31, 2001) of the Company's outstanding common stock. This program will expire not later than February 6, 2002, and results will depend on market conditions. Accordingly, there is no guarantee as to the exact number of shares to be repurchased. The repurchased shares will become treasury shares available for general corporate purposes, including possible use in connection with the Company's dividend reinvestment program, employee benefit plans, acquisitions or other distributions.

Any repurchase would be effected through open market purchases or in privately negotiated transactions in accordance with applicable regulations of the Securities and Exchange Commission. Under the 2000 program based on the value of the Company's stock on January 26, 2000, the commitment to repurchase the stock over the next year was approximately $2,636,000. The Company repurchased 7,403 shares between January 1 and February 3, 2001, bringing the total repurchased shares to 138,218 under this plan. The Company also reissued 30,742 shares to existing shareholders under itÎs dividend reinvestment program in 2001.

Under the 2001 program, based on the value of the Company's stock on January 31, 2001, the commitment to repurchase the stock over the next year was $3,179,000. At March 31, 2001, the remaining commitment to repurchase the stock was approximately $3,081,000. As of March 31, 2001 the Company had repurchased 13,439 shares under the new program..

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

(Dollars in thousands)

The following is management's discussion and analysis of the financial condition and results of operations of Cortland Bancorp (the "Company"). The discussion should be read in conjunction with the Consolidated Financial Statements and related notes included elsewhere in this report.

Note Regarding Forward-looking Statements

In addition to historical information contained herein, the following discussion may contain forward-looking statements that involve risks and uncertainties. Economic circumstances, the Company's operations and actual results could differ significantly from those discussed in any forward-looking statements. Some of the factors that could cause or contribute to such differences are changes in the economy and interest rates either nationally or in the Company's market area; increased competitive pressures or changes in either the nature or composition of competitors; changes in the legal and regulatory environment; changes in factors influencing liquidity such as expectations regarding the rate of inflation or deflation, currency exchange rates, and other factors influencing market volatility; unforeseen risks associated with other global economic and financial factors.

Liquidity

The central role of the Company's liquidity management is to (1) ensure sufficient liquid funds to meet the normal transaction requirements of its customers, (2) take advantage of market opportunities requiring flexibility and speed, and (3) provide a cushion against unforeseen liquidity needs.

Principal sources of liquidity for the Company include assets considered relatively liquid, such as interest-bearing deposits in other banks, federal funds sold, cash and due from banks, as well as cash flows from maturities and repayments of loans, investment securities and mortgage-backed securities.

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

(Dollars in thousands)

Along with its liquid assets, the Company has other sources of liquidity available to it which help to ensure that adequate funds are available as needed. These other sources include, but are not limited to, the ability to obtain deposits through the adjustment of interest rates, the purchasing of federal funds, borrowings from the Federal Home Loan Bank of Cincinnati and access to the Federal Reserve Discount Window.

Cash and cash equivalents increased compared to year end 2000. Operating activities provided cash of $3,367 and $150 during the three months ended March 31, 2001 and 2000, respectively. Refer to the Consolidated Statements of Cash Flows for a summary of the sources and uses of cash for March 31, 2001 and 2000.

Capital Resources

The capital management function is a continuous process which consists of providing capital for both the current financial position and the anticipated future growth of the Company. Central to this process is internal equity generation, particularly through earnings retention. Internal capital generation is measured as the annualized rate of return on equity, exclusive of any appreciation or depreciation relating to available for sale securities, multiplied by the percentage of earnings retained. Internal capital generation slowed to 3.6% for the three months ended March 31, 2001, as compared to 5.1% for the like period during 2000. The decrease reflects the Company's increase in the dividend payout ratio. Overall capital growth (a figure which reflects earnings, dividends paid, common stock issued, treasury shares purchased, treasury shares reissued, and the net change in the estimated fair value of available for sale securities) was at an annual rate of 10.9%.

Risk-based standards for measuring capital adequacy require banks and bank holding companies to maintain capital based on "risk-adjusted" assets. Categories of assets with potentially higher credit risk require more capital than assets with lower risk. In addition, banks and bank holding companies are required to maintain capital to support, on a risk-adjusted basis, certain off-balance sheet activities such as standby letters of credit and interest rate swaps.

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

(Dollars in thousands)

These standards also classify capital into two tiers, referred to as Tier 1 and Tier 2. The Company's Tier 1 capital consists of common shareholders' equity (excluding any gain or loss on available for sale debt securities) less intangible assets and the net unrealized loss on equity securities with readily determinable fair values. Tier 2 capital is the allowance for loan and lease losses reduced for certain regulatory limitations. Risk based capital standards require a minimum ratio of 8% of qualifying total capital to risk-adjusted total assets with at least 4% constituting Tier 1 capital. Capital qualifying as Tier 2 capital is limited to 100% of Tier 1 capital. All banks and bank holding companies are also required to maintain a minimum leverage capital ratio (Tier 1 capital to total average assets) in the range of 3% to 4%, subject to regulatory guidelines.

The Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA) required banking regulatory agencies to revise risk-based capital standards to ensure that they adequately account for the following additional risks: interest rate, concentration of credit, and nontraditional activities. Accordingly, regulators will subjectively consider an institution's exposure to declines in the economic value of its capital due to changes in interest rates in evaluating capital adequacy. The table below illustrates the Company's risk weighted capital ratios at March 31, 2001 and December 31, 2000.

	March 31, 2001	December 31, 2000
Tier 1 Capital	$ 46,956	$ 46,361
Tier 2 Capital	2,776	2,756
TOTAL QUALIFYING CAPITAL	$ 49,732	$ 49,117
Risk Adjusted Total Assets (*)	$ 221,848	$ 220,263
Tier 1 Risk-Based Capital Ratio	21.17%	21.05%
Total Risk-Based Capital Ratio	22.42%	22.30%
Tier 1 Risk-Based Capital to Average Assets (Leverage Capital Ratio)	11.08%	10.94%

(*) Includes off-balance sheet exposures.

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

(Dollars in thousands)

Assets, less intangibles and the net unrealized market value adjustment of investment securities available for sale, averaged $423,856 for the three months ended March 31, 2001 and $423,933 for the year ended December 31, 2000.

First Three Months of 2001 as Compared to First Three Months of 2000

During the first three months of 2001, net interest income after provision for loan losses decreased by $250 compared to the first three months of 2000. Total interest income increased by $113, or 1.5%, from the level recorded in 2000. This was accompanied by an increase in interest expense of $388 or 11.7%, and a $25 decrease in the provision for loan loss.

The average rate paid on interest sensitive liabilities increased by 42 basis points year-over-year. The average balance of interest sensitive liabilities increased by $7,811 or 2.4%. Compared to the first quarter of last year, average borrowings, primarily with the Federal Home Loan Bank, decreased by $276 while the average rate paid on borrowings increased by 5 basis points, from 5.49% to 5.54%. Average interest bearing demand deposits decreased by $1,214, while savings and money market accounts declined by $5,073 and $1,189 respectively. The average rate paid on these products increased by 10 basis points in the aggregate. The average balance on time deposit products increased by $15,563, as the average rate paid increased by 58 basis points, from 5.43% to 6.01%.

Interest and dividend income on securities registered a decrease of $121, or 3.8%, during the first three months of 2001 when compared to 2000, while on a fully tax equivalent basis income on securities decreased by $126 or 3.8%. The average invested balances decreased by 6.3%, decreasing by $12,754 over the levels of a year ago. The decrease in the average balance of investment securities was accompanied by an 18 basis point increase in the tax equivalent yield of the portfolio.

Interest and fees on loans increased by $169 for the first three months of 2001 compared to 2000. A $7,306 increase in the average balance of the loan portfolio, or 3.7 %, was accompanied by a 3 basis point increase in the portfolio's tax equivalent yield.

Other interest income increased by $65 from the same period a year ago. The average balance of Federal Funds sold and other money market funds increased by $ 4,787. The yield on federal funds decreased by 28 basis points reflecting the change in Federal Reserve policy initiated early in 2001. The yield on Federal Funds sold is anticipated to decrease further during the second quarter of 2001 as the Federal Reserve is expected to lower the targeted Federal Funds rate by another 50 to 100 basis points.

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

(Dollars in thousands)

The tax equivalent yield on earning assets increased by 12 basis points from the same quarter a year ago. The tax equivalent yield of the investment portfolio measured 6.81%, an 18 basis point increase from the same quarter a year ago, while the loan portfolio yielded 8.71%, up 3 basis points from last year's rate. Meanwhile, the rate paid on interest-bearing liabilities increased 42 basis points compared to a year ago. The net effect of these changes was that the tax equivalent net interest margin declined to 4.02%, a decrease of 31 basis points from that achieved during last year's first quarter.

Other income from all sources increased by $274 from the same period a year ago. Gains on 1-4 residential mortgage loans in the secondary mortgage market decreased by only $2 from the same period a year ago. Gains on securities called and gains on the sale of available for sale investment securities increased by $121 from year ago levels. Fees for other customer services increased by $46, while other sources of non recurring non-interest income increased by $109 from the same period a year ago. This was due primarily to a $91 increase in the cash surrender value of life insurance.

Loans net of the allowance for losses increased by $202 during the period. Gross loans as a percentage of earning assets stood at 50.4% as of March 31, 2001 as compared to 50.3% on March 31, 2000. The loan to deposit ratio at the end of the first three months of 2001 was 62.3% compared to 61.8% at the end of the same period a year ago. The investment portfolio represented 58.4% of each deposit dollar, down from 61.2% a year ago.

Loan charge-offs during the first three months were $53 in 2001 and $162 in 2000, while the recovery of previously charged-off loans amounted to $25 in 2001 compared to $23 in 2000. A provision for loan loss of $75 was charged to operations in 2001, compared to $100 charged in 2000. At March 31, 2001, the loan loss allowance of $3,021 represented 1.48% of outstanding loans. Non accrual loans at March 31, 2001 represented 0.9% of the loan portfolio compared to 0.8% at December 31, 2000 and 1.1% a year ago.

Total other expenses in the first three months were $2,746 in 2001 compared to $2,679 in 2000, an increase of $67 or 2.5%. Full time equivalent employment during the first three months averaged 164 employees in 2001, a 5.2% decline from the 173 employed in the same quarter of 2000. Salaries and benefits increased by $69 or 4.7% compared to the similar period a year ago, primarily due to the increased cost of benefits.

(Dollars in thousands)

For the first three months of 2001, state and local taxes increased by $7 or 4.7%. Occupancy and equipment expense increased by $48, or 10.2%. All other expense categories decreased by 9.6% or $57 as a group.

Income before income tax expense amounted to $1,679 for the first three months of 2001 compared to $1,722 for the similar period of 2000. The effective tax rate for the first three months was 24.2% in 2001 compared to 25.8% in 2000, resulting in income tax expense of $406 and $444 respectively. Net income for the first three months registered $1,273 in 2001 compared to $1,278 in 2000, representing per share amounts of $0.33 both in 2001 and 2000.

Regulatory Matters

On March 13, 2000, the Board of Governors of the Federal Reserve System approved the Company’s application to become a financial holding company. As a financial holding company, the Company may engage in activities that are financial in nature or incidental to a financial activity, as authorized by the Gramm-Leach-Bliley Act of 1999 (The Financial Services Reform Act). Under the Financial Services Reform Act, the Company may continue to claim the benefits of financial holding company status as long as each depository institution that it controls remains well capitalized and well managed. The Company is required to provide notice to the Board of Governors of the Federal Reserve System when it becomes aware that any depository institution controlled by the Company ceases to be well capitalized or well managed. Furthermore, current regulation specifies that prior to initiating or engaging in any new activities that are authorized for financial holding companies, the Company’s insured depository institutions must be rated “satisfactory” or better under the Community Reinvestment Act (CRA). As of March 31, 2001, the Company's bank subsidiary was rated “satisfactory” for CRA purposes, and remained well capitalized and well managed, in management's opinion.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

(Dollars in thousands)

Management considers interest rate risk to be the Company’s principal source of market risk. Since December 31, 2000, short term interest rates, as measured by U. S. Treasury securities with maturities of one year or less, have decreased by 89 to 149 basis points, reflecting monetary easing on the part of the Federal Reserve. The Federal Reserve dropped short-term rates by 50 basis points twice during January and once again during the March meeting of the Federal Open Market Committee. Intermediate interest rates, as measured by U. S. Treasury securities with maturities of two to five years, decreased by approximately 53 to 101 basis points. Meanwhile, long term interest rates, as measured by U.S. Treasury securities with maturities of ten years or more responded less dramatically, declining by 15 to 35 basis points, as these rates are more influenced by the U.S. Government's plans to repurchase Treasury debt, federal spending plans and taxation policies and expectations of growth and inflation in the future.

The net effect of these changes had minimal impact on the Company’s risk position. When these changes are incorporated into the Company’s risk analysis, simulated results for an unchanged rate environment indicate a $218 decrease in net interest income for the twelve month horizon subsequent to March 31, 2001 compared to the simulated results for a similar twelve month horizon subsequent to December 31, 2000. The Company's sensitivity to a declining rate environment increased slightly. The Company's sensitivity to an increasing rate environment improved marginally.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

(CONTINUED)

(Dollars in thousands)

The following table indicates the Company's current estimate of interest rate sensitivity based on the composition of the balance sheet at March 31, 2001 and December 31, 2000. For purposes of this analysis, short term interest rates as measured by the federal funds rate and the prime lending rate are assumed to increase (decrease) gradually over the subsequent twelve month period, reaching a level 300 basis points higher (lower) than the rates in effect at March 31, 2001 and December 31, 2000. Under both the rising rate scenario and the falling rate scenario, the yield curve is assumed to exhibit a parallel shift. The analysis assumes no growth in assets and liabilities and no change in asset or liability mix over the subsequent twelve month period.

Over the past twelve months, the Federal Reserve has decreased its target rate for overnight federal funds by 100 basis points. During the quarter ended March 31, 2001, the difference between the yield on the ten year Treasury and the three month Treasury increased to a positive 34 basis points from the negative 70 basis points at December 31, 2000, with interest rates peaking in the long-end of the Treasury curve.

Simulated Net Interest Income (NII) Scenarios for the Twelve Months Ending

	Net Interest Income		**$ Change in NII**		**% Change in NII**	
Changes in	**March 31,**	**Dec. 31,**	**March 31,**	**Dec. 31,**	**March 31,**	**Dec. 31,**
Interest Rates	**2002**	**2001**	**2002**	**2001**	**2002**	**2001**
Graduated increase of +300 basis points	16,542	16,580	(756)	(936)	(4.4)%	(5.3)%
Short term rates unchanged	17,298	17,516				
Graduated decrease of -300 basis points	16,925	17,293	(373)	(223)	(2.2)%	(1.3)%

The level of interest rate risk indicated remains within limits that management considers acceptable. However, given that interest rate movements can be sudden and unanticipated, and are increasingly influenced by global events and circumstances beyond the purview of the Federal Reserve, no assurance can be made that interest rate movements will not impact key assumptions and relationships in a manner not presently anticipated.

CORTLAND BANCORP AND SUBSIDIARIES

PART II —OTHER INFORMATION

Item 1. Legal Proceedings

See Note (5) of the financial statements.

Item 2. Changes in Securities

Not applicable

Item 3. Defaults upon Senior Securities

Not applicable

Item 4. Submission of Matters to a Vote of Security Holders

None

Item 5. Other Information

Not applicable

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits

2. Not applicable

4. Not applicable

10. Not applicable

11. See Note (6) of the Financial Statements

15. Not applicable

18. Not applicable

19. Not applicable

22. Not applicable

23. Not applicable

24. Not applicable

27. Financial Data Schedule

99. Not applicable

PART II – OTHER INFORMATION

(b) Reports on Form 8-K

Form 8-K was filed with the United States Securities and Exchange Commission, dated February 2, 2001. The 8-K applied to Item 5 – Other Events, per the 8-K instructions, and announced that the Board of Directors had approved a stock repurchase program authorizing the acquisition of up to 4.9% of Cortland Bancorp's outstanding common stock. No financial statements were filed with this report.

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.

Cortland Bancorp
(Registrant)

DATED: May 8, 2001

Lawrence A. Fantauzzi
Secretary/Treasurer
(Chief Financial Officer)

DATED: May 8, 2001

Rodger W. Platt
Chairman and President
(Duly Authorized Officer)