TIMBERLAND BANCORP INC
Form 10-Q
August 11, 2014
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2014

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 number 0-23333

TIMBERLAND BANCORP, INC.
(Exact name of registrant as specified in its charter)

Washington	91-1863696
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)
624 Simpson Avenue, Hoquiam, Washington	98550
(Address of principal executive offices)	(Zip Code)

(360) 533-4747
(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes _X_ No __

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

Large accelerated filer ___ Accelerated Filer Non-accelerated filer __ Smaller reporting company _X_

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

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

CLASS	SHARES OUTSTANDING AT JULY 31, 2014
Common stock, $.01 par value	7,045,936

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PART I. FINANCIAL INFORMATION
Item 1. Financial Statements (unaudited)
TIMBERLAND BANCORP, INC. AND SUBSIDIARY
CONDENSED CONSOLIDATED BALANCE SHEETS
June 30, 2014 and September 30, 2013
(Dollars in thousands, except per share amounts)
(Unaudited)

	June 30, 2014	September 30, 2013
Assets		
Cash and cash equivalents:		
Cash and due from financial institutions	$13,500	$12,879
Interest-bearing deposits in banks	50,467	81,617
Total cash and cash equivalents	63,967	94,496
Certificates of deposit (“CDs”) held for investment (at cost which approximates fair value)	32,336	30,042
Mortgage-backed securities (“MBS”) and other investments - held to maturity, at amortized cost (estimated fair value $6,285 and $3,533)	5,417	2,737
MBS and other investments - available for sale	2,928	4,101
Federal Home Loan Bank of Seattle (“FHLB”) stock	5,299	5,452
Loans receivable	566,757	557,329
Loans held for sale	1,501	1,911
Less: Allowance for loan losses	(10,563)	(11,136)
Net loans receivable	557,695	548,104
Premises and equipment, net	17,867	17,764
Other real estate owned (“OREO”) and other repossessed assets, net	11,172	11,720
Accrued interest receivable	1,922	1,972
Bank owned life insurance (“BOLI”)	17,494	17,102
Goodwill	5,650	5,650
Core deposit intangible (“CDI”)	32	119
Mortgage servicing rights (“MSRs”), net	1,812	2,266
Other assets	4,040	4,123
Total assets	$727,631	$745,648
Liabilities and shareholders’ equity		
Liabilities:		
Deposits:		
Non-interest-bearing demand	$92,995	$87,657
Interest-bearing	505,637	520,605
Total deposits	598,632	608,262
FHLB advances	45,000	45,000
Other liabilities and accrued expenses	2,669	2,698
Total liabilities	646,301	655,960

See notes to unaudited condensed consolidated financial statements

TIMBERLAND BANCORP, INC. AND SUBSIDIARY
CONDENSED CONSOLIDATED BALANCE SHEETS (continued)
June 30, 2014 and September 30, 2013
(Dollars in thousands, except per share amounts)
(Unaudited)

	June 30, 2014	September 30, 2013
Shareholders' equity		
Fixed Rate Cumulative Perpetual Preferred Stock. Series A, $0.01 par value; 1,000,000 shares authorized; redeemable at $1,000 per share; 12,065 shares issued and outstanding - September 30, 2013	$—	$11,936
Common stock, $.01 par value; 50,000,000 shares authorized; 7,045,936 shares issued and outstanding - June 30, 2014 7,045,036 shares issued and outstanding - September 30, 2013	10,710	10,570
Unearned shares issued to Employee Stock Ownership Plan ("ESOP")	(1,256)	(1,454)
Retained earnings	72,240	68,998
Accumulated other comprehensive loss	(364)	(362)
Total shareholders' equity	81,330	89,688
Total liabilities and shareholders' equity	$727,631	$745,648

See notes to unaudited condensed consolidated financial statements

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TIMBERLAND BANCORP, INC. AND SUBSIDIARY
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
For the three and nine months ended June 30, 2014 and 2013
(Dollars in thousands, except per share amounts)
(Unaudited)

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2014	2013	2014	2013
Interest and dividend income				
Loans receivable	$7,238	$7,422	$21,811	$22,231
MBS and other investments	66	69	190	216
Dividends from mutual funds and FHLB stock	6	5	21	22
Interest-bearing deposits in banks	87	79	268	247
Total interest and dividend income	7,397	7,575	22,290	22,716
Interest expense				
Deposits	498	609	1,562	1,987
FHLB advances	466	467	1,399	1,399
Total interest expense	964	1,076	2,961	3,386
Net interest income	6,433	6,499	19,329	19,330
Provision for loan losses	—	1,385	—	2,760
Net interest income after provision for loan losses	6,433	5,114	19,329	16,570
Non-interest income				
Recoveries (Other than temporary impairment "OTTI") on MBS and other investments	(38)	(1)	49	(9)
Adjustment for portion recorded as (transferred from) other comprehensive income (loss) before taxes	29	(2)	29	(30)
Net recoveries (OTTI) on MBS and other investments	(9)	(3)	78	(39)
Loss on sale of MBS and other investments, net	—	—	(32)	—
Service charges on deposits	921	882	2,795	2,657
ATM and debit card interchange transaction fees	611	526	1,769	1,562
BOLI net earnings	134	144	392	431
Gain on sales of loans, net	241	579	714	2,054
Escrow fees	45	55	111	135
Valuation recovery on MSRs	—	—	—	475
Fee income from non-deposit investment sales	14	19	58	92
Other	159	170	439	498
Total non-interest income, net	2,116	2,372	6,324	7,865

See notes to unaudited condensed consolidated financial statements

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TIMBERLAND BANCORP, INC. AND SUBSIDIARY
CONDENSED CONSOLIDATED STATEMENTS OF INCOME (continued)
For the three and nine months ended June 30, 2014 and 2013
(Dollars in thousands, except per share amounts)
(Unaudited)

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2014	2013	2014	2013
Non-interest expense				
Salaries and employee benefits	$3,325	$3,176	$10,138	$9,376
Premises and equipment	754	739	2,094	2,154
Advertising	187	184	537	533
OREO and other repossessed assets, net	240	313	795	1,107
ATM and debit card processing	207	219	791	636
Postage and courier	122	107	329	342
Amortization of CDI	29	33	87	98
State and local taxes	123	170	361	466
Professional fees	196	202	590	636
Federal Deposit Insurance Corporation ("FDIC") insurance	158	157	479	526
Other insurance	34	39	113	133
Loan administration and foreclosure	129	91	377	278
Data processing and telecommunications	399	319	1,058	911
Deposit operations	146	157	569	450
Other	381	331	1,107	1,152
Total non-interest expense	6,430	6,237	19,425	18,798
Income before federal income taxes	2,119	1,249	6,228	5,637
Provision for federal income taxes	685	373	2,024	1,774
Net income	1,434	876	4,204	3,863
Preferred stock dividends	—	(151)	(136)	(559)
Preferred stock discount accretion	—	(47)	(70)	(236)
Discount on redemption of preferred stock	—	—	—	255
Net income to common shareholders	$1,434	$678	$3,998	$3,323
Net income per common share				
Basic	$0.21	$0.10	$0.58	$0.49
Diluted	$0.20	$0.10	$0.57	$0.48
Weighted average common shares outstanding				
Basic	6,857,149	6,818,752	6,855,811	6,816,772
Diluted	7,033,713	6,902,497	7,015,155	6,870,751
Dividends paid per common share	$0.04	$0.03	$0.11	$0.06

See notes to unaudited condensed consolidated financial statements

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TIMBERLAND BANCORP, INC. AND SUBSIDIARY
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
For the three and nine months ended June 30, 2014 and 2013
(Dollars in thousands)
(Unaudited)

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2014	2013	2014	2013
Comprehensive income:				
Net income	$1,434	$876	$4,204	$3,863
Unrealized holding gain (loss) on securities available for sale, net of tax	(8)	82	(59)	55
Change in OTTI on securities held to maturity, net of tax:				
Additional amount recognized (recovered) related to credit loss for which OTTI was previously recognized	11	(1)	11	17
Amount reclassified to credit loss for previously recorded market loss	8	—	8	3
Accretion of OTTI securities held to maturity, net of tax	14	15	38	38
Total comprehensive income	$1,459	$972	$4,202	$3,976

See notes to unaudited condensed consolidated financial statements

TIMBERLAND BANCORP, INC. AND SUBSIDIARY
CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
For the nine months ended June 30, 2014 and the year ended September 30, 2013
(Dollars in thousands, except per share amounts)
(Unaudited)

	Number of Shares		Amount					
	Preferred Stock	Common Stock	Preferred Stock	Common Stock	Unearned Shares Issued to ESOP	Retained Earnings	Accumulated Other Compre-hensive Loss	Total
Balance, September 30, 2012	16,641	7,045,036	$16,229	$10,484	$(1,719)	$65,788	$ (463)	$90,319
Net income	—	—	—	—	—	4,757	—	4,757
Accretion of preferred stock discount	—	—	283	—	—	(283)	—	—
Redemption of preferred stock	(4,576)	—	(4,576)	—	—	255	—	(4,321)
5% preferred stock dividend	—	—	—	—	—	(885)	—	(885)
Common stock dividends ($0.09 per common share)	—	—	—	—	—	(634)	—	(634)
Earned ESOP shares, net of tax	—	—	—	6	265	—	—	271
MRDP (1) compensation expense, net of tax	—	—	—	31	—	—	—	31
Stock option compensation expense	—	—	—	49	—	—	—	49
Unrealized holding gain on securities available for sale, net of tax	—	—	—	—	—	—	23	23
Change in OTTI on securities held to maturity, net of tax	—	—	—	—	—	—	21	21
Accretion of OTTI on securities held to maturity, net of tax	—	—	—	—	—	—	57	57
Balance, September 30, 2013	12,065	7,045,036	11,936	10,570	(1,454)	68,998	(362)	89,688
Net income	—	—	—	—	—	4,204	—	4,204
Accretion of preferred stock discount	—	—	70	—	—	(70)	—	—

Redemption of preferred stock	(12,065)	—	(12,006)	—	—	(59)	—	(12,065)
Exercise of stock options	—	3,600	—	16	—	—	—	16
Forfeiture of MRDP shares	—	(2,700)	—	—	—	—	—	—
5% preferred stock dividends	—	—	—	—	—	(58)	—	(58)
Common stock dividends ($0.11 per common share)	—	—	—	—	—	(775)	—	(775)
Earned ESOP shares, net of tax	—	—	—	46	198	—	—	244
MRDP compensation expense, net of tax	—	—	—	2	—	—	—	2
Stock option compensation expense	—	—	—	76	—	—	—	76
Unrealized holding loss on securities available for sale, net of tax	—	—	—	—	—	—	(59)	(59)
Change in OTTI on securities held to maturity, net of tax	—	—	—	—	—	—	19	19
Accretion of OTTI on securities held to maturity, net of tax	—	—	—	—	—	—	38	38
Balance, June 30, 2014	—	7,045,936	$—	$10,710	$(1,256)	$72,240	$ (364)	$81,330

(1) 1998 Management Recognition and Development Plan ("MRDP").

See notes to unaudited condensed consolidated financial statements

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TIMBERLAND BANCORP, INC. AND SUBSIDIARY
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
For the nine months ended June 30, 2014 and 2013
(Dollars in thousands)
(Unaudited)

	Nine Months Ended June 30, 2014	2013
Cash flows from operating activities		
Net income	$4,204	$3,863
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	—	2,760
Depreciation	886	810
Deferred federal income taxes	—	522
Amortization of CDI	87	98
Earned ESOP shares	198	198
MRDP compensation expense	2	32
Stock option compensation expense	76	37
Gain on sales of OREO and other repossessed assets, net	(185)	(261)
Provision for OREO losses	491	759
Gain on sale of premises and equipment	(5)	(7)
BOLI net earnings	(392)	(431)
Gain on sales of loans, net	(714)	(2,054)
Decrease in deferred loan origination fees	(23)	(272)
Net OTTI (recoveries) on MBS and other investments	(78)	39
Loss on sale of MBS and other investments, net	32	—
Valuation recovery on MSRs	—	(475)
Loans originated for sale	(22,177)	(73,559)
Proceeds from sales of loans	23,301	74,607
Decrease in other assets, net	559	1,327
Decrease in other liabilities and accrued expenses, net	(29)	(377)
Net cash provided by operating activities	6,233	7,616
Cash flows from investing activities		
Net increase in CDs held for investment	(2,294)	(3,259)
Proceeds from sale of MBS and other investments available for sale	856	—
Proceeds from maturities and prepayments of MBS and other investments available for sale	288	666
Purchase of MBS and other investments held to maturity	(3,003)	—
Proceeds from maturities and prepayments of MBS and other investments held to maturity	424	506
Redemption of FHLB stock	153	153
Increase in loans receivable, net	(14,834)	(13,461)
Additions to premises and equipment	(1,021)	(967)
Proceeds from sale of premises and equipment	37	7
Proceeds from sale of OREO and other repossessed assets	5,098	2,661
Net cash used in investing activities	(14,296)	(13,694)

See notes to unaudited condensed consolidated financial statements

TIMBERLAND BANCORP, INC. AND SUBSIDIARY
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (continued)
For the nine months ended June 30, 2014 and 2013
(Dollars in thousands)
(Unaudited)

	Nine Months Ended June 30, 2014	2013
Cash flows from financing activities		
Decrease in deposits, net	$(9,630)	$(1,862)
Decrease in repurchase agreements, net	—	(855)
ESOP tax effect	46	(2)
Proceeds from exercise of stock options	16	—
Redemption of preferred stock	(12,065)	(4,321)
Dividends paid	(833)	(1,005)
Net cash used in financing activities	(22,466)	(8,045)
Net decrease in cash and cash equivalents	(30,529)	(14,123)
Cash and cash equivalents		
Beginning of period	94,496	96,668
End of period	$63,967	$82,545
Supplemental disclosure of cash flow information		
Income taxes paid	$2,108	$1,793
Interest paid	2,987	3,454
Supplemental disclosure of non-cash investing activities		
Loans transferred to OREO and other repossessed assets	$5,665	$5,919
Loans originated to facilitate the sale of OREO	809	748

See notes to unaudited condensed consolidated financial statements

Timberland Bancorp, Inc. and Subsidiary
Notes to Unaudited Condensed Consolidated Financial Statements

(1) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES
(a) Basis of Presentation: The accompanying unaudited condensed consolidated financial statements for Timberland Bancorp, Inc. ("Company") were prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") for interim financial information and with instructions for Form 10-Q and, therefore, do not include all disclosures necessary for a complete presentation of financial condition, results of operations, and cash flows in conformity with GAAP. However, all adjustments which are, in the opinion of management, necessary for a fair presentation of the interim condensed consolidated financial statements have been included. All such adjustments are of a normal recurring nature. The unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements included in the Company's Annual Report on Form 10-K for the year ended September 30, 2013 ("2013 Form 10-K"). The unaudited condensed consolidated results of operations for the nine months ended June 30, 2014 are not necessarily indicative of the results that may be expected for the entire fiscal year ending September 30, 2014.

(b) Principles of Consolidation: The unaudited condensed consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary, Timberland Bank ("Bank"), and the Bank's wholly-owned subsidiary, Timberland Service Corp. All significant intercompany transactions and balances have been eliminated in consolidation.

(c) Operating Segment: The Company has one reportable operating segment which is defined as community banking in western Washington under the operating name, "Timberland Bank."

(d) The preparation of condensed consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the condensed consolidated financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

(e) Certain prior period amounts have been reclassified to conform to the June 30, 2014 presentation with no change to net income or total shareholders' equity previously reported.

(2) PREFERRED STOCK SOLD IN TROUBLED ASSET RELIEF PROGRAM ("TARP") CAPITAL PURCHASE PROGRAM ("CPP")
On December 23, 2008, the Company received $16.64 million from the U.S. Treasury Department ("Treasury") as a part of the Treasury's CPP, which was established as part of the TARP. The Company sold 16,641 shares of Fixed Rate Cumulative Perpetual Preferred Stock, Series A ("Series A Preferred Stock"), with a liquidation value of $1,000 per share and a related warrant to purchase 370,899 shares of the Company's common stock at an exercise price of $6.73 per share (subject to anti-dilution adjustments) at any time through December 23, 2018. The Series A Preferred Stock paid a 5.0% dividend for the first five years, after which the rate was scheduled to increase to 9.0% if the preferred shares were not redeemed by the Company.

On November 13, 2012, the Company's outstanding 16,641 shares of Series A Preferred Stock were sold by the Treasury as part of its efforts to manage and recover its investments under the TARP. While the sale of the shares of Series A Preferred Stock to new owners did not result in any proceeds to the Company and did not change the Company's capital position or accounting for these securities, it did eliminate restrictions put in place by the Treasury on TARP recipients.

On June 12, 2013, the Treasury sold, to private investors, the warrant to purchase up to 370,899 shares of the Company's common stock. The sale of the warrant to new owners did not result in any proceeds to the Company and did not change the Company's capital position or accounting for the warrant.

During the year ended September 30, 2013 the Company purchased and retired 4,576 shares of its Series A Preferred Stock for $4.32 million; a $255,000 discount from the liquidation value. The discount from the liquidation value on the repurchased shares was recorded as an increase to retained earnings. On December 20, 2013, the Company redeemed the remaining 12,065 shares of its Series A Preferred Stock at the liquidation value of $12.07 million.

(3) MBS AND OTHER INVESTMENTS

MBS and other investments have been classified according to management's intent and are as follows as of June 30, 2014 and September 30, 2013 (dollars in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
June 30, 2014				
Held to Maturity				
MBS:				
U.S. government agencies	$1,053	$29	$(2)	$1,080
Private label residential	1,348	853	(5)	2,196
U.S. agency securities	3,016	1	(8)	3,009
Total	$5,417	$883	$(15)	$6,285
Available for Sale				
MBS:				
U.S. government agencies	$1,866	$102	$(1)	$1,967
Mutual funds	1,000	—	(39)	961
Total	$2,866	$102	$(40)	$2,928
September 30, 2013				
Held to Maturity				
MBS:				
U.S. government agencies	$1,202	$31	$(2)	$1,231
Private label residential	1,521	781	(15)	2,287
U.S. agency securities	14	1	—	15
Total	$2,737	$813	$(17)	$3,533
Available for Sale				
MBS:				
U.S. government agencies	$2,144	$87	$(2)	$2,229
Private label residential	804	120	(10)	914
Mutual funds	1,000	—	(42)	958
Total	$3,948	$207	$(54)	$4,101

The following table summarizes the estimated fair value and gross unrealized losses for all securities and the length of time these unrealized losses existed as of June 30, 2014 (dollars in thousands):

	Less Than 12 Months			12 Months or Longer			Total	
	Estimated Fair Value	Gross Unrealized Losses	Qty	Estimated Fair Value	Gross Unrealized Losses	Qty	Estimated Fair Value	Gross Unrealized Losses
Held to Maturity								
MBS:								
U.S. government agencies	$14	$—	1	$81	$(2)	10	$95	$(2)
Private label residential	9	—	1	156	(5)	12	165	(5)
U.S. agency securities	2,995	(8)	1	—	—	—	2,995	(8)
Total	$3,018	$(8)	3	$237	$(7)	22	$3,255	$(15)
Available for Sale								
MBS:								
U.S. government agencies	$21	$—	1	$40	$(1)	2	$61	$(1)
Mutual Funds	—	—	—	961	(39)	1	961	(39)
Total	$21	$—	1	$1,001	$(40)	3	$1,022	$(40)

The following table summarizes the estimated fair value and gross unrealized losses for all securities and the length of time the unrealized losses existed as of September 30, 2013 (dollars in thousands):

	Less Than 12 Months			12 Months or Longer			Total	
	Estimated Fair Value	Gross Unrealized Losses	Qty	Estimated Fair Value	Gross Unrealized Losses	Qty	Estimated Fair Value	Gross Unrealized Losses
Held to Maturity								
MBS:								
U.S. government agencies	$3	$—	6	$88	$(2)	4	$91	$(2)
Private label residential	80	(4)	4	239	(11)	14	319	(15)
Total	$83	$(4)	10	$327	$(13)	18	$410	$(17)
Available for Sale								
MBS:								
U.S. government agencies	$96	$(2)	3	$—	$—	1	$96	$(2)
Private label residential	—	—	—	108	(10)	2	108	(10)
Mutual Funds	958	(42)	1	—	—	—	958	(42)
Total	$1,054	$(44)	4	$108	$(10)	3	$1,162	$(54)

During the three months ended June 30, 2014 and 2013, the Company recorded net recoveries (OTTI) through earnings on residential MBS of ($9,000) and ($3,000), respectively. During the nine months ended June 30, 2014 and 2013, the Company recorded net recoveries (OTTI) through earnings of $78,000 and ($39,000) respectively. The Company provides for the bifurcation of OTTI into (i) amounts related to credit losses which are recognized through earnings, and (ii) amounts related to all other factors which are recognized as a component of other comprehensive income.

To determine the component of the gross OTTI related to credit losses, the Company compared the amortized cost basis of each OTTI security to the present value of its revised expected cash flows, discounted using its pre-impairment yield. The revised expected cash flow estimates for individual securities are based primarily on an analysis of default rates and prepayment speeds included in third-party analytic reports. Significant judgment by management is required in this analysis that includes, but is not limited to, assumptions regarding the collectability of principal and interest, net of related expenses, on the underlying loans.

The following table presents a summary of the significant inputs utilized to measure management's estimate of the credit loss component on OTTI securities as of June 30, 2014 and September 30, 2013:

	Range Minimum		Maximum		Weighted Average	
June 30, 2014						
Constant prepayment rate	6.00	%	15.00	%	10.01	%
Collateral default rate	0.03	%	17.46	%	6.46	%
Loss severity rate	0.51	%	69.48	%	40.95	%
September 30, 2013						
Constant prepayment rate	6.00	%	15.00	%	12.33	%
Collateral default rate	0.73	%	22.53	%	7.84	%
Loss severity rate	20.48	%	75.02	%	52.69	%

The following tables present the recoveries (OTTI) for the three and nine months ended June 30, 2014 and 2013 (dollars in thousands):

	Three Months Ended June 30, 2014			Three Months Ended June 30, 2013		
	Held To Maturity		Available For Sale	Held To Maturity		Available For Sale
Total recoveries (OTTI)	$(38	)	$—	$—		$(1)
Adjustment for portion recorded as (transferred from) other comprehensive income (loss) before taxes (1)	29		—	(2	)	—
Net recoveries (OTTI) recognized in earnings (2)	$(9	)	$—	$(2	)	$(1)

	Nine Months Ended June 30, 2014		Nine Months Ended June 30, 2013		
	Held To Maturity	Available For Sale	Held To Maturity		Available For Sale
Total recoveries (OTTI)	$49	$—	$(7	)	$(2)
Adjustment for portion recorded as (transferred from) other comprehensive income (loss) before taxes (1)	29	—	(30	)	—
Net recoveries (OTTI) recognized in earnings (2)	$78	$—	$(37	)	$(2)

(1) Represents OTTI related to all other factors.

(2) Represents net recoveries (OTTI) related to credit losses.

The following table presents a roll-forward of the credit loss component of held to maturity and available for sale debt securities that have been written down for OTTI with the credit loss component recognized in earnings and the remaining impairment loss related to all other factors recognized in other comprehensive income for the nine months ended June 30, 2014 and 2013 (dollars in thousands):

	Nine Months Ended June 30,	
	2014	2013
Beginning balance of credit loss	$ 2,084	$ 2,703
Additions:		
Credit losses for which OTTI was not previously recognized	2	5
Additional increases to the amount related to credit loss for which OTTI was previously recognized	13	39
Subtractions:		
Realized losses previously recorded as credit losses	(535)	(571)
Recovery of prior credit loss	90	—
Ending balance of credit loss	$ 1,654	$ 2,176

There was no realized loss on sale of securities for the three months ended June 30, 2014 and there was a $32,000 realized loss on sale of securities for the nine months ended June 30, 2014. There was no realized loss on sale of securities for the three and nine months ended June 30, 2013. During the three months ended June 30, 2014, the Company recorded a net $40,000 realized loss (as a result of the securities being deemed worthless) on 12 held to maturity residential MBS, of which the entire amount had been recognized previously as a credit loss. During the nine months ended June 30, 2014, the Company recorded a net $445,000 realized loss (as a result of securities being deemed worthless) on 15 held to maturity residential MBS and six available for sale MBS, of which the entire amount had been recognized previously as a credit loss. During the three months ended June 30, 2013, the Company recorded a $188,000 realized loss (as a result of the securities being deemed worthless) on 12 held to maturity residential MBS and six available for sale residential MBS, of which the entire amount had been recognized previously as a credit loss. During the nine months ended June 30, 2013, the Company recorded a $571,000 realized loss (as a result of securities being deemed worthless) on 17 held to maturity residential MBS and six available for sale MBS, of which the entire amount had been recognized previously as a credit loss.

The amortized cost of residential mortgage-backed and agency securities pledged as collateral for public fund deposits, federal treasury tax and loan deposits, FHLB collateral, retail repurchase agreements and other non-profit organization deposits totaled $6.39 million and $4.54 million at June 30, 2014 and September 30, 2013, respectively.

The contractual maturities of debt securities at June 30, 2014 were as follows (dollars in thousands). Expected maturities may differ from scheduled maturities as a result of the prepayment of principal or call provisions.

	Held to Maturity		Available for Sale	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
Due within one year	$—	$—	$—	$—
Due after one year to five years	3,022	3,015	22	21
Due after five to ten years	10	10	34	35
Due after ten years	2,385	3,260	1,810	1,911
Total	$ 5,417	$ 6,285	$ 1,866	$ 1,967

(4) GOODWILL

The Company performed its fiscal year 2014 goodwill impairment test during the quarter ended June 30, 2014 with the assistance of a third-party firm specializing in goodwill impairment valuations for financial institutions. The third-party analysis was conducted as of May 31, 2014 and concluded that the recorded value of goodwill as of May 31, 2014 was not impaired.

The goodwill impairment test involves a two-step process. Step one of the goodwill impairment test estimates the fair value of the reporting unit. If the estimated fair value of the Company's sole reporting unit, the Bank, under step one exceeds the recorded value of the reporting unit, goodwill is not considered impaired and no further analysis is necessary. If the estimated fair value of the Company's sole reporting unit is less than the recorded value, then a step two test, which calculates the fair value of assets and liabilities to calculate an implied value of goodwill, is performed.

Step one of the goodwill impairment test estimated the fair value of the reporting unit utilizing a discounted cash flow income approach analysis, a public company market approach analysis, a merger and acquisition market approach analysis and a trading price market approach analysis in order to derive an enterprise value for the Company.

The discounted cash flow income approach analysis uses a reporting unit's projection of estimated operating results and cash flows and discounts them using a rate that reflects current market conditions. The projection uses management's estimates of economic and market conditions over the projected period including growth rates in loans and deposits, estimates of future expected changes in net interest margins and cash expenditures. Key assumptions used by the Company in its discounted cash flow model (income approach) included an annual loan growth rate that ranged from 3.00% to 5.10%, an annual deposit growth rate that ranged from 2.80% to 4.00% and a return on assets that ranged from 0.70% to 1.00%. In addition to the above projections of estimated operating results, key assumptions used to determine the fair value estimate under the approach were the discount rate of 13.6% and the residual capitalization rate of 10.6%. The discount rate used was the cost of equity capital. The cost of equity capital was based on the capital asset pricing model ("CAPM"), modified to account for a small stock premium. The small stock premium represents the additional return required by investors for small stocks based on the Stocks, Bonds, Bill and Inflation 2013 Yearbook. Beyond the approximate five-year forecast period, residual free cash flows were estimated to increase at a constant rate into perpetuity. These cash flows were converted to a residual value using an appropriate residual capitalization rate. The residual capitalization rate was equal to the discount rate minus the expected long-term growth rate of cash flows. Based on historical results, the economic climate, the outlook for the industry and management's expectations, a long-term growth rate of 3.0% was estimated.

The public company market approach analysis estimates the fair value by applying cash flow multiples to the reporting unit's operating performance. The multiples were derived from comparable publicly traded companies with operating and investment characteristics similar to those of the Company. Key assumptions used by the Company included the selection of comparable public companies and performance ratios. In applying the public company analysis, the Company selected eight publicly traded institutions based on similar lines of business, markets, growth prospects, risks and firm size. The performance ratios included price to earnings (last twelve months), price to earnings (current year to date), price to book value, price to tangible book value and price to deposits.

The merger and acquisition market approach analysis estimates the fair value by using merger and acquisition transactions involving companies that are similar in nature to the Company. Key assumptions used by the Company included the selection of comparable merger and acquisition transactions and the valuation ratios to be used. The analysis used banks located in Washington or Oregon that were acquired after January 1, 2012. The valuation ratios from these transactions for price to earnings and price to tangible book value were then used to derive an estimated fair value of the Company.

The trading price market approach analysis used the closing market price at May 30, 2014 of the Company's common stock, traded on the NASDAQ Global Market to determine the market value of total equity capital.

A key assumption used by the Company in the public company market approach analysis and the trading price market approach analysis was the application of a control premium. The Company's common stock is thinly traded and therefore management believes reflects a discount for illiquidity. In addition, the trading price of the Company's common stock reflects a minority interest value. To determine the fair market value of a majority interest in the Company's stock, premiums were calculated and applied to the indicated values. Therefore, a control premium was applied to the results of the public company market approach analysis and the trading price market approach analysis because the initial value conclusion was based on minority interest transactions. Merger and acquisition studies were analyzed to conclude that the difference between the acquisition price and a company's stock price prior to acquisition indicates, in part, the price effect of a controlling interest. Based on the evaluation of mergers and acquisition studies, a control premium of 25% was used.

The results of the Company's step one test indicated that the the reporting unit's fair value was more than its recorded value and therefore step two of the analysis was not necessary.

A significant amount of judgment is involved in determining if an indicator of goodwill impairment has occurred. Such indicators may include, among others: a significant decline in the expected future cash flows; a sustained, significant decline in the Company's stock price and market capitalization; a significant adverse change in legal factors or in the business climate; adverse assessment or action by a regulator; and unanticipated competition. Key assumptions used in the annual goodwill impairment test are highly judgmental and include: selection of comparable companies, amount of control premium, projected cash flows and discount rate applied to projected cash flows. Any change in these indicators or key assumptions could have a significant negative impact on the Company's financial condition, impact the goodwill impairment analysis or cause the Company to perform a goodwill impairment analysis more frequently than once per year.

As of June 30, 2014, management believes that there have been no events or changes in the circumstances that would indicate a potential impairment of goodwill. No assurances can be given, however, that the Company will not record an impairment loss on goodwill in the future.

(5) LOANS RECEIVABLE AND ALLOWANCE FOR LOAN LOSSES

Loans receivable and loans held for sale consisted of the following at June 30, 2014 and September 30, 2013 (dollars in thousands):

	June 30, 2014 Amount	Percent		September 30, 2013 Amount	Percent	
Mortgage loans:						
One- to four-family (1)	$100,085	16.9	%	$104,298	18.0	%
Multi-family	47,077	8.0		51,108	8.8	
Commercial	299,707	50.7		291,297	50.3	
Construction and land development	53,695	9.1		45,136	7.8	
Land	28,442	4.8		31,144	5.4	
Total mortgage loans	529,006	89.5		522,983	90.3	
Consumer loans:						
Home equity and second mortgage	31,832	5.4		33,014	5.7	
Other	5,229	0.8		5,981	1.0	
Total consumer loans	37,061	6.2		38,995	6.7	
Commercial business loans	25,341	4.3		17,499	3.0	
Total loans receivable	591,408	100.0	%	579,477	100.0	%
Less:						
Undisbursed portion of construction loans in process	(21,463)			(18,527)		
Deferred loan origination fees	(1,687)			(1,710)		
Allowance for loan losses	(10,563)			(11,136)		
Total loans receivable, net	$557,695			$548,104		

(1) Includes loans held for sale.

Construction and Land Development Loan Portfolio Composition

The following table sets forth the composition of the Company’s construction and land development loan portfolio at June 30, 2014 and September 30, 2013 (dollars in thousands):

	June 30, 2014 Amount	Percent		September 30, 2013 Amount	Percent	
Custom and owner/builder	$48,212	89.8	%	$40,811	90.4	%
Speculative one- to four-family	2,307	4.3		1,428	3.2	
Commercial real estate	2,736	5.1		2,239	5.0	
Multi-family (including condominiums)	440	0.8		143	0.3	
Land development	—	—		515	1.1	
Total construction and land development loans	$53,695	100.0	%	$45,136	100.0	%

Allowance for Loan Losses

The following tables set forth information for the three and nine months ended June 30, 2014 and 2013 regarding activity in the allowance for loan losses (dollars in thousands):

	Three Months Ended June 30, 2014				
	Beginning Allowance	Provision /(Credit)	Charge-offs	Recoveries	Ending Allowance
Mortgage loans:					
One-to four-family	$1,751	$213	$356	$42	$1,650
Multi-family	433	(31)	—	—	402
Commercial	5,168	(4)	—	—	5,164
Construction – custom and owner/builder	348	(15)	—	—	333
Construction – speculative one- to four-family	46	10	—	—	56
Construction – commercial	25	13	—	—	38
Construction – multi-family	—	(110)	—	125	15
Land	1,568	(83)	5	4	1,484
Consumer loans:					
Home equity and second mortgage	868	(7)	—	—	861
Other	194	(4)	2	2	190
Commercial business loans	348	18	—	4	370
Total	$10,749	$—	$363	$177	$10,563

	Nine Months Ended June 30, 2014				
	Beginning Allowance	Provision /(Credit)	Charge-offs	Recoveries	Ending Allowance
Mortgage loans:					
One-to four-family	$1,449	$987	$979	$193	$1,650
Multi-family	749	(347)	—	—	402
Commercial	5,275	348	463	4	5,164
Construction – custom and owner/builder	262	71	—	—	333
Construction – speculative one- to four-family	96	(40)	—	—	56
Construction – commercial	56	(18)	—	—	38
Construction – multi-family	—	(236)	—	251	15
Construction – land development	—	(287)	—	287	—
Land	1,940	(607)	260	411	1,484
Consumer loans:					
Home equity and second mortgage	782	100	28	7	861
Other	200	(8)	4	2	190
Commercial business loans	327	37	14	20	370
Total	$11,136	$—	$1,748	$1,175	$10,563

	Three Months Ended June 30, 2013				
	Beginning Allowance	Provision /(Credit)	Charge-offs	Recoveries	Ending Allowance
Mortgage loans:					
One-to four-family	$ 1,846	$ 1	$ 3	$ 19	$ 1,863
Multi-family	815	(1)	—	—	814
Commercial	4,497	179	11	3	4,668
Construction – custom and owner/builder	284	(29)	26	—	229
Construction – speculative one- to four-family	141	(58)	—	—	83
Construction – commercial	85	5	—	—	90
Construction – land development	12	(2)	10	—	—
Land	2,197	1,311	1,543	1	1,966
Consumer loans:					
Home equity and second mortgage	781	(2)	—	5	784
Other	239	2	8	—	233
Commercial business loans	416	(21)	—	1	396
Total	$ 11,313	$ 1,385	$ 1,601	$ 29	$ 11,126

	Nine Months Ended June 30, 2013				
	Beginning Allowance	Provision /(Credit)	Charge-offs	Recoveries	Ending Allowance
Mortgage loans:					
One-to four-family	$ 1,558	$ 792	$ 527	$ 40	$ 1,863
Multi-family	1,156	(227)	116	1	814
Commercial	4,247	1,035	667	53	4,668
Construction – custom and owner/builder	386	(131)	26	—	229
Construction – speculative one- to four-family	128	(45)	—	—	83
Construction – commercial	429	(339)	—	—	90
Construction – land development	—	(130)	16	146	—
Land	2,392	1,821	2,250	3	1,966
Consumer loans:					
Home equity and second mortgage	759	204	184	5	784
Other	254	(7)	14	—	233
Commercial business loans	516	(213)	—	93	396
Total	$ 11,825	$ 2,760	$ 3,800	$ 341	$ 11,126

The following tables presents information on the loans evaluated individually for impairment and collectively evaluated for impairment in the allowance for loan losses at June 30, 2014 and September 30, 2013 (dollars in thousands):

	Allowance for Loan Losses			Recorded Investment in Loans		
	Individually Evaluated for Impairment	Collectively Evaluated for Impairment	Total	Individually Evaluated for Impairment	Collectively Evaluated for Impairment	Total
June 30, 2014						
Mortgage loans:						
One- to four-family	$798	$852	$1,650	$7,520	$92,565	$100,085
Multi-family	50	352	402	3,326	43,751	47,077
Commercial	1,423	3,741	5,164	17,440	282,267	299,707
Construction – custom and owner/builder	—	333	333	—	28,982	28,982
Construction – speculative one- to four-family	—	56	56	—	1,445	1,445
Construction – commercial	—	38	38	—	1,520	1,520
Construction – multi-family	—	15	15	—	285	285
Land	383	1,101	1,484	5,446	22,996	28,442
Consumer loans:						
Home equity and second mortgage	193	668	861	670	31,162	31,832
Other	—	190	190	8	5,221	5,229
Commercial business loans	—	370	370	—	25,341	25,341
Total	$2,847	$7,716	$10,563	$34,410	$535,535	$569,945
September 30, 2013						
Mortgage loans:						
One- to four-family	$600	$849	$1,449	$8,984	$95,314	$104,298
Multi-family	334	415	749	5,184	45,924	51,108
Commercial	1,763	3,512	5,275	19,510	271,787	291,297
Construction – custom and owner/builder	—	262	262	—	22,788	22,788
Construction – speculative one- to four-family	88	8	96	687	236	923
Construction – commercial	—	56	56	—	2,239	2,239
Construction – multi-family	—	—	—	143	1	144
Construction – land development	—	—	—	515	—	515
Land	234	1,706	1,940	2,391	28,753	31,144
Consumer loans:						
Home equity and second mortgage	57	725	782	679	32,335	33,014
Other	—	200	200	6	5,975	5,981
Commercial business loans	—	327	327	—	17,499	17,499
Total	$3,076	$8,060	$11,136	$38,099	$522,851	$560,950

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Credit Quality Indicators
The Company uses credit risk grades which reflect the Company's assessment of a loan's risk or loss potential. The Company categorizes loans into risk grade categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, public information and current economic trends, among other factors such as the estimated fair value of the collateral. The Company uses the following definitions for credit risk ratings as part of the ongoing monitoring of the credit quality of its loan portfolio:

Pass: Pass loans are defined as those loans that meet acceptable quality underwriting standards.

Watch: Watch loans are defined as those loans that still exhibit acceptable quality, but have some concerns that justify greater attention. If these concerns are not corrected, a potential for further adverse categorization exists. These concerns could relate to a specific condition peculiar to the borrower, its industry segment or the general economic environment.

Special Mention: Special mention loans are defined as those loans deemed by management to have some potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in the deterioration of the payment prospects of the loan. Assets in this category do not expose the Company to sufficient risk to warrant a substandard classification.

Substandard: Substandard loans are defined as those loans that are inadequately protected by the current net worth and paying capacity of the obligor, or of the collateral pledged. Loans classified as substandard have a well-defined weakness or weaknesses that jeopardize the repayment of the debt. If the weakness or weaknesses are not corrected, there is the distinct possibility that some loss will be sustained.

Loss: Loans in this classification are considered uncollectible and of such little value that continuance as bankable assets is not warranted. This classification does not mean that the loan has absolutely no recovery or salvage value, but rather it is not practical or desirable to defer writing off this loan even though partial recovery may be realized in the future.

The following table lists the loan credit risk grades utilized by the Company that serve as credit quality indicators at June 30, 2014 and September 30, 2013 (dollars in thousands):

	Loan Grades				
June 30, 2014	Pass	Watch	Special Mention	Substandard	Total
Mortgage loans:					
One- to four-family	$91,467	$1,835	$880	$5,903	$100,085
Multi-family	38,171	1,704	6,435	767	47,077
Commercial	271,593	3,179	18,622	6,313	299,707
Construction – custom and owner/builder	28,982	—	—	—	28,982
Construction – speculative one- to four-family	1,445	—	—	—	1,445
Construction – commercial	1,520	—	—	—	1,520
Construction – multi-family	285	—	—	—	285
Land	19,628	115	2,492	6,207	28,442
Consumer loans:					
Home equity and second mortgage	29,938	729	326	839	31,832
Other	5,182	39	—	8	5,229
Commercial business loans	25,140	106	95	—	25,341
Total	$513,351	$7,707	$28,850	$20,037	$569,945
September 30, 2013					
Mortgage loans:					
One- to four-family	$91,291	$4,032	$769	$8,206	$104,298
Multi-family	41,863	132	8,337	776	51,108
Commercial	262,502	3,309	12,522	12,964	291,297
Construction – custom and owner/builder	22,788	—	—	—	22,788
Construction – speculative one- to four-family	236	687	—	—	923
Construction – commercial	2,239	—	—	—	2,239
Construction – multi-family	—	—	—	144	144
Construction – land development	—	—	—	515	515
Land	20,627	5,101	1,129	4,287	31,144
Consumer loans:					
Home equity and second mortgage	31,096	782	55	1,081	33,014
Other	5,937	39	—	5	5,981
Commercial business loans	17,029	366	104	—	17,499
Total	$495,608	$14,448	$22,916	$27,978	$560,950

The following tables present an age analysis of past due status of loans by category at June 30, 2014 and September 30, 2013 (dollars in thousands):

	30–59 Days Past Due	60-89 Days Past Due	Non-Accrual	Past Due 90 Days or More and Still Accruing	Total Past Due	Current	Total Loans
June 30, 2014							
Mortgage loans:							
One- to four-family	$—	$163	$4,873	$—	$5,036	$95,049	$100,085
Multi-family	—	—	—	—	—	47,077	47,077
Commercial	—	812	1,631	—	2,443	297,264	299,707
Construction – custom and owner/builder	—	—	—	—	—	28,982	28,982
Construction – speculative one- to four- family	—	—	—	—	—	1,445	1,445
Construction – commercial	—	—	—	—	—	1,520	1,520
Construction – multi-family	—	—	—	—	—	285	285
Land	48	—	5,204	—	5,252	23,190	28,442
Consumer loans:							
Home equity and second mortgage	—	—	371	150	521	31,311	31,832
Other	—	—	8	—	8	5,221	5,229
Commercial business loans	—	—	—	—	—	25,341	25,341
Total	$48	$975	$12,087	$150	$13,260	$556,685	$569,945
September 30, 2013							
Mortgage loans:							
One- to four-family	$14	$1,218	$6,985	$—	$8,217	$96,081	$104,298
Multi-family	—	—	—	—	—	51,108	51,108
Commercial	—	2,537	3,435	—	5,972	285,325	291,297
Construction – custom and owner/ builder	—	—	—	—	—	22,788	22,788
Construction – speculative one- to four- family	—	—	—	—	—	923	923
Construction – commercial	—	—	—	—	—	2,239	2,239
Construction – multi-family	—	—	144	—	144	—	144
Construction – land development	—	—	515	—	515	—	515
Land	—	—	2,146	284	2,430	28,714	31,144
Consumer loans:							
Home equity and second mortgage	101	20	380	152	653	32,361	33,014
Other	1	39	5	—	45	5,936	5,981
Commercial business loans	83	15	—	—	98	17,401	17,499
Total	$199	$3,829	$13,610	$436	$18,074	$542,876	$560,950

Impaired Loans

A loan is considered impaired when it is probable that the Company will be unable to collect all contractual principal and interest payments due in accordance with the original or modified terms of the loan agreement. Impaired loans are measured based on the estimated fair value of the collateral less estimated cost to sell if the loan is considered collateral dependent. Impaired loans that are not considered to be collateral dependent are measured based on the present value of expected future cash flows.

The categories of non-accrual loans and impaired loans overlap, although they are not coextensive. The Company considers all circumstances regarding the loan and borrower on an individual basis when determining whether an impaired loan should be placed on non-accrual status, such as the financial strength of the borrower, the estimated collateral value, reasons for the delay, payment record, the amount past due and the number of days past due.

The following is a summary of information related to impaired loans as of June 30, 2014 and for the three and nine months then ended (in thousands):

	Recorded Investment	Unpaid Principal Balance (Loan Balance Plus Charge Off)	Related Allowance	QTD Average Recorded Investment (1)	YTD Average Recorded Investment (2)	QTD Interest Income Recognized (1)	YTD Interest Income Recognized (2)	QTD Cash Basis Interest Income Recognized (1)	YTD Cash Basis Interest Income Recognized (2)
With no related allowance recorded:									
Mortgage loans:									
One- to four-family	$ 2,635	$ 3,300	$ —	$ 2,749	$ 3,767	$ —	$ —	$ —	$ —
Multi-family	—	857	—	—	158	—	—	—	—
Commercial	9,047	12,342	—	9,077	7,704	151	267	122	210
Construction – custom and owner/builder	—	—	—	—	15	—	—	—	—
Construction – speculative one- to four-family	—	—	—	—	—	—	—	—	—
Construction – multi-family	—	338	—	—	115	—	—	—	—
Construction – land development	—	—	—	—	244	—	—	—	—
Land	1,039	1,819	—	1,003	1,080	3	9	2	7
Consumer loans:									
Home equity and second mortgage	185	389	—	211	251	—	—	—	—
Other	8	8	—	10	7	—	—	—	—
Commercial business loans	—	14	—	53	22	—	—	—	—
Subtotal	12,914	19,067	—	13,103	13,363	154	276	124	217
With an allowance recorded:									
Mortgage loans:									
One- to four-family	4,885	4,903	798	4,925	4,336	39	109	31	81
Multi-family	3,326	3,326	50	3,675	4,580	45	175	34	132
Commercial	8,393	8,393	1,423	8,425	10,370	117	440	90	347
Construction – custom and owner/builder	—	—	—	—	—	—	—	—	—
Construction – speculative one- to four-family	—	—	—	—	413	—	11	—	7
Construction – multi-family	—	—	—	—	—	—	—	—	—
Construction - land development	—	—	—	—	—	—	—	—	—
Land	4,407	4,407	383	4,477	3,225	6	12	6	12

Consumer loans:									
Home equity and second mortgage	485	485	193	488	375	4	12	3	9
Other	—	—	—		—	—	—	—	—
Commercial business loans	—	—	—		—	—	—	—	—
Subtotal	21,496	21,514	2,847	21,990	23,299	211	759	164	588

Total									
Mortgage loans:									
One- to four-family	$7,520	$8,203	$798	$7,674	$8,103	$39	$109	$31	$81
Multi-family	3,326	4,183	50	3,675	4,738	45	175	34	132
Commercial	17,440	20,735	1,423	17,502	18,074	268	707	212	557
Construction – custom and owner/builder	—	—	—	—	15	—	—	—	—
Construction – speculative one- to four-family	—	—	—	—	413	—	11	—	7
Construction – multi-family	—	338	—	—	115	—	—	—	—
Construction – land development	—	—	—	—	244	—	—	—	—
Land	5,446	6,226	383	5,480	4,305	9	21	8	19
Consumer loans:									
Home equity and second mortgage	670	874	193	699	626	4	12	3	9
Other	8	8	—	10	7	—	—	—	—
Commercial business loans	—	14	—	53	22	—	—	—	—
Total	$34,410	$40,581	$2,847	$35,093	$36,662	$365	$1,035	$288	$805

(1) For the three months ended June 30, 2014
(2) For the nine months ended June 30, 2014

The following is a summary of information related to impaired loans as of and for the year ended September 30, 2013 (in thousands):

	Recorded Investment	Unpaid Principal Balance (Loan Balance Plus Charge Off)	Related Allowance	YTD Average Recorded Investment (1)	YTD Interest Income Recognized (1)	YTD Cash Basis Interest Income Recognized (1)
With no related allowance recorded:						
Mortgage loans:						
One- to four-family	$5,342	$5,775	$—	$2,661	$18	$13
Multi-family	—	982	—	473	3	3
Commercial	4,879	8,005	—	8,781	322	267
Construction – custom and owner/builder	—	—	—	97	—	—
Construction – speculative one- to four-family	—	—	—	65	—	—
Construction – multi-family	143	608	—	293	—	—
Construction – land development	515	3,279	—	534	—	—
Land	1,188	2,133	—	3,519	9	8
Consumer loans:						
Home equity and second mortgage	380	556	—	266	—	—
Other	6	6	—	8	—	—
Commercial business loans	—	33	—	—	—	—
Subtotal	12,453	21,377	—	16,697	352	291
With an allowance recorded:						
Mortgage loans:						
One- to four-family	3,642	3,726	600	4,397	91	68
Multi-family	5,184	5,184	334	5,960	301	230
Commercial	14,631	15,297	1,763	9,052	526	420
Construction – custom and owner/builder	—	—	—	60	—	—
Construction – speculative one- to four-family	687	687	88	695	29	16
Construction – multi-family	—	—	—	—	—	—
Construction - land development	—	—	—	—	—	—
Land	1,203	1,226	234	1,962	27	27
Consumer loans:						
Home equity and second mortgage	299	299	57	352	16	12
Other	—	—	—	—	—	—
Subtotal	25,646	26,419	3,076	22,478	990	773
Total						
Mortgage loans:						
One- to four-family	8,984	9,501	600	7,058	109	81
Multi-family	5,184	6,166	334	6,433	304	233
Commercial	19,510	23,302	1,763	17,833	848	687
Construction – custom and owner/builder	—	—	—	157	—	—

Construction – speculative one- to four-family	687	687	88	760	29	16
Construction – multi-family	143	608	—	293	—	—
Construction – land development	515	3,279	—	534	—	—
Land	2,391	3,359	234	5,481	36	35
Consumer loans:						
Home equity and second mortgage	679	855	57	618	16	12
Other	6	6	—	8	—	—
Commercial business loans	—	33	—	—	—	—
Total	$38,099	$47,796	$3,076	$39,175	$1,342	$1,064

(1) For the year ended September 30, 2013

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The following table sets forth information with respect to the Company's non-performing assets at June 30, 2014 and September 30, 2013 (dollars in thousands):

	June 30, 2014		September 30, 2013	
Loans accounted for on a non-accrual basis:				
Mortgage loans:				
One- to four-family	$4,873		$6,985	
Commercial	1,631		3,435	
Construction – multi-family	—		144	
Construction – land development	—		515	
Land	5,204		2,146	
Consumer loans:				
Home equity and second mortgage	371		380	
Other	8		5	
Commercial business loans	—		—	
Total loans accounted for on a non-accrual basis	12,087		13,610	
Accruing loans which are contractually past due 90 days or more	150		436	
Total of non-accrual and 90 days past due loans	12,237		14,046	
Non-accrual investment securities	1,162		2,187	
OREO and other repossessed assets, net	11,172		11,720	
Total non-performing assets (1)	$24,571		$27,953	
Troubled debt restructured loans on accrual status (2)	$16,524		$18,573	
Non-accrual and 90 days or more past due loans as a percentage of loans receivable	2.15	%	2.51	%
Non-accrual and 90 days or more past due loans as a percentage of total assets	1.68	%	1.88	%
Non-performing assets as a percentage of total assets	3.38	%	3.75	%
Loans receivable (3)	$568,258		$559,240	
Total assets	$727,631		$745,648	

(1) Does not include troubled debt restructured loans on accrual status.
(2) Does not include troubled debt restructured loans totaling $2.9 million and $4.0 million reported as non-accrual loans at June 30, 2014 and September 30, 2013, respectively.
(3) Includes loans held for sale and before the allowance for loan losses.

Troubled debt restructured loans are loans for which the Company, for economic or legal reasons related to the borrower's financial condition, has granted a significant concession to the borrower that it would otherwise not consider. The loan terms which have been modified or restructured due to a borrower's financial difficulty include but are not limited to: a reduction in the stated interest rate; an extension of the maturity at an interest rate below current market; a reduction in the face amount of the debt; a reduction in the accrued interest; or re-aging, extensions, deferrals and renewals. Troubled debt restructured loans are considered impaired loans and are individually evaluated for impairment. Troubled debt restructured loans can be classified as either accrual or non-accrual. Troubled debt restructured loans are classified as non-performing loans unless they have been performing in accordance with their modified terms for a period of at least six months. The Company had $19.44 million in troubled debt restructured loans included in impaired loans at June 30, 2014 and had no commitments to lend additional funds on these loans. The Company had $22.60 million in troubled debt restructured loans included in impaired loans at September 30, 2013 and had $1,000 in commitments to lend additional funds on these loans. The allowance for loan losses allocated to troubled debt restructured loans at June 30, 2014 and September 30, 2013 was $1.72 million and $2.37 million, respectively.

The following table sets forth information with respect to the Company’s troubled debt restructured loans by interest accrual status as of June 30, 2014 and September 30, 2013 (dollars in thousands):

	June 30, 2014		
	Accruing	Non-Accrual	Total
Mortgage loans:			
One- to four-family	$2,647	$193	$2,840
Multi-family	3,327	—	3,327
Commercial	10,009	1,495	11,504
Land	242	1,075	1,317
Consumer loans:			
Home equity and second mortgage	299	152	451
Total	$16,524	$2,915	$19,439

	September 30, 2013		
	Accruing	Non-Accrual	Total
Mortgage loans:			
One- to four-family	$1,999	$198	$2,197
Multi-family	5,184	—	5,184
Commercial	10,160	1,574	11,734
Construction – speculative one- to four-family	687	—	687
Construction – land development	—	515	515
Land	244	1,564	1,808
Consumer loans:			
Home equity and second mortgage	299	180	479
Total	$18,573	$4,031	$22,604

The following table sets forth information with respect to the Company's troubled debt restructured loans by portfolio segment that occurred during the nine months ended June 30, 2014 and the year ended September 30, 2013 (dollars in thousands):

June 30, 2014	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	End of Period Balance
Land (1)	1	$ 157	$157	$156
Total	1	$ 157	$157	$156

September 30, 2013	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	End of Period Balance
One-to four-family (2)	2	$ 353	$353	$350
Commercial (1)	2	2,327	2,327	2,318
Total	4	$ 2,680	$2,680	$2,668

(1) Modifications were a result of a reduction in the stated interest rate.
(2) Modifications were a result of a combination of changes (i.e., a reduction in the stated interest rate and an extension of the maturity at an interest rate below current market).

(6) NET INCOME PER COMMON SHARE
Basic net income per common share is computed by dividing net income to common shareholders by the weighted average number of common shares outstanding during the period, without considering any dilutive items. Diluted net income per common share is computed by dividing net income to common shareholders by the weighted average number of common shares and common stock equivalents for items that are dilutive, net of shares assumed to be repurchased using the treasury stock method at the average share price for the Company's common stock during the period. The dividend and related accretion for the amount of the Company's Series A Preferred Stock outstanding for the respective period was deducted from net income and the discount on the redemption of Series A Preferred Stock was added to net income in computing net income to common shareholders. Common stock equivalents arise from the assumed conversion of outstanding stock options and the outstanding warrant to purchase common stock. Shares owned by the Bank's ESOP that have not been allocated are not considered to be outstanding for the purpose of computing basic and diluted net income per common share. At June 30, 2014 and 2013, there were 187,807 and 225,070 shares, respectively, that had not been allocated under the Bank's ESOP.

Information regarding the calculation of basic and diluted net income per common share for the three and nine months ended June 30, 2014 and 2013 is as follows (dollars in thousands, except per share amounts):

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2014	2013	2014	2013
	(In thousands, except for per share data)			
Basic net income per common share computation				
Numerator – net income	$1,434	$876	$4,204	$3,863
Preferred stock dividends	—	(151)	(136)	(559)
Preferred stock discount accretion	—	(47)	(70)	(236)
Discount on redemption of preferred stock	—	—	—	255
Net income to common shareholders	$1,434	$678	$3,998	$3,323
Denominator – weighted average common shares outstanding	6,857,149	6,818,752	6,855,811	6,816,772
Basic net income per common share	$0.21	$0.10	$0.58	$0.49
Diluted net income per common share computation				
Numerator – net income	$1,434	$876	$4,204	$3,863
Preferred stock dividends	—	(151)	(136)	(559)
Preferred stock discount accretion	—	(47)	(70)	(236)
Discount on redemption of preferred stock	—	—	—	255
Net income to common shareholders	$1,434	$678	$3,998	$3,323
Denominator – weighted average common shares outstanding	6,857,149	6,818,752	6,855,811	6,816,772
Effect of dilutive stock options (1)	38,582	18,458	36,070	13,035
Effect of dilutive stock warrant	137,982	65,287	123,274	40,944
Weighted average common shares and common stock equivalents	7,033,713	6,902,497	7,015,155	6,870,751
Diluted net income per common share	$0.20	$0.10	$0.57	$0.48

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(1) For the three and nine months ended June 30, 2014, average options to purchase 126,000 and 131,489 shares of common stock, respectively, were outstanding but not included in the computation of diluted net income per common share because their effect would have been anti-dilutive. For the three and nine months ended June 30, 2013, options to purchase 56,546 and

131,152 shares of common stock, respectively, were outstanding but not included in the computation of diluted net income per common share because their effect would have been anti-dilutive.

(7) STOCK PLANS AND STOCK BASED COMPENSATION
Stock Option Plans
Under the Company’s stock option plans (the 1999 Stock Option Plan and the 2003 Stock Option Plan), the Company was able to grant options for up to a combined total of 1,622,500 shares of common stock to employees, officers and directors. Shares issued may be purchased in the open market or may be issued from authorized and unissued shares. The exercise price of each option equals the fair market value of the Company’s common stock on the date of grant. Generally, options vest in 20% annual installments on each of the five anniversaries from the date of the grant. At June 30, 2014, there were no options for shares available for future grant under the 2003 Stock Option Plan or the 1999 Stock Option Plan.

Activity under the plans for the nine months ended June 30, 2014 and 2013 is as follows:

	Nine Months Ended June 30, 2014		Nine Months Ended June 30, 2013	
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
Options outstanding, beginning of period	162,946	$6.96	195,626	$7.97
Exercised	(3,600)	4.65	—	—
Granted	135,000	9.29	29,000	6.00
Forfeited	(66,046)	9.97	(56,680)	9.52
Options outstanding, end of period	228,300	$7.50	167,946	$7.10
Options exercisable, end of period	38,300	$4.90	68,446	$9.55

The aggregate intrinsic value of options outstanding at June 30, 2014 was $693,000.

At June 30, 2014, there were 190,000 unvested options with an aggregate grant date fair value of $464,000, all of which the Company assumes will vest. The aggregate intrinsic value of unvested options at June 30, 2014 was $477,000. There were 14,600 options with an aggregate grant date fair value of $26,000 that vested during the nine months ended June 30, 2014.

At June 30, 2013, there were 99,500 unvested options with an aggregate grant date fair value of $208,000. There were 8,800 options with an aggregate grant date fair value of $13,000 that vested during the nine months ended June 30, 2013.

The Company uses the Black-Scholes option pricing model to estimate the fair value of stock-based awards with the weighted average assumptions noted in the following table. The risk-free interest rate is based on the U.S. Treasury rate of a similar term as the stock option at the particular grant date. The expected life is based on historical data, vesting terms and estimated exercise dates. The expected dividend yield is based on the most recent quarterly dividend on an annualized basis in effect at the time the options were granted, adjusted, if appropriate for management's expectations regarding future dividends. The expected volatility is based on historical volatility of the Company’s stock price. There were 135,000 options granted during the nine months ended June 30, 2014 with an aggregate grant date fair value of $349,000. There were 29,000 options granted during the nine months ended June 30, 2013 with an aggregate grant date fair value of $69,000.

The weighted average assumptions used for options granted during the nine months ended June 30, 2014 and 2013 were:

	2014		2013	
Expected volatility	39	%	45	%
Expected term (in years)	5		5	
Expected dividend yield	2.51	%	—	%
Risk free interest rate	1.41	%	0.76	%
Grant date fair value per share	$2.59		$2.37	

Stock Grant Plan

The Company adopted the MRDP in 1998 for the benefit of employees, officers and directors of the Company. The objective of the MRDP is to retain and attract personnel of experience and ability in key positions by providing them with a proprietary interest in the Company.

The MRDP allowed for the issuance to participants of up to 529,000 shares of the Company's common stock. Awards under the MRDP were made in the form of shares of common stock that are subject to restrictions on the transfer of ownership and are subject to a five-year vesting period. Compensation expense is the amount of the fair value of the common stock at the date of the grant to the plan participants and is recognized over a five-year vesting period, with 20% vesting on each of the five anniversaries from the date of the grant.

No MRDP shares were granted during the nine months ended June 30, 2014 or 2013. At June 30, 2014, no shares were available for future awards under the MRDP.

At June 30, 2014, there were no unvested MRDP shares. There were 3,254 MRDP shares that vested during the nine months ended June 30, 2014 with an aggregate grant date fair value of $23,000.

At June 30, 2013, there were 3,248 unvested MRDP shares with an aggregated grant date fair value of $23,000. There were 6,213 MRDP shares that vested during the nine months ended June 30, 2013 with an aggregated grant date fair value of $62,000. At June 30, 2013, no shares were available for future awards under the MRDP.

Expense for Stock Compensation Plans

Compensation expense for all stock-based plans were as follows:

	Nine Months Ended June 30,			
	2014		2013	
	(Dollars in thousands)			
	Stock Options	Stock Grants	Stock Options	Stock Grants
Compensation expense	$76	$2	$37	$32
Related tax benefit recognized	$—	$—	$13	$11

As of June 30, 2014, the compensation expense yet to be recognized for stock-based awards that have been awarded but not vested for the years ending September 30 is as follows (dollars in thousands):

	Stock Options	Stock Grants	Total Awards
Remainder of 2014	$28	$—	$28
2015	106	—	106
2016	106	—	106
2017	98	—	98
2018	67	—	67
2019	9	—	9

Total	$414	$—	$414

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(8) FAIR VALUE MEASUREMENTS
GAAP requires disclosure of estimated fair values for financial instruments. Such estimates are subjective in nature, and significant judgment is required regarding the risk characteristics of various financial instruments at a discrete point in time. Therefore, such estimates could vary significantly if assumptions regarding uncertain factors were to change. In addition, as the Company normally intends to hold the majority of its financial instruments until maturity, it does not expect to realize many of the estimated amounts disclosed. The disclosures also do not include estimated fair value amounts for certain items which are not defined as financial instruments but which may have significant value. The Company does not believe that it would be practicable to estimate a representational fair value for these types of items as of June 30, 2014 and September 30, 2013. Because GAAP excludes certain items from fair value disclosure requirements, any aggregation of the fair value amounts presented would not represent the underlying value of the Company.

Accounting guidance regarding fair value measurements defines fair value and establishes a framework for measuring fair value in accordance with GAAP. Fair value is the exchange price that would be received for an asset or paid to transfer a liability in an orderly transaction between market participants on the measurement date. The following definitions describe the levels of inputs that may be used to measure fair value:

Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date.

Level 2: Significant observable inputs other than quoted prices included within Level 1, such as quoted prices in markets that are not active, and inputs other than quoted prices that are observable or can be corroborated by observable market data.

Level 3: Significant unobservable inputs that reflect a company’s own assumptions about the assumptions market participants would use in pricing an asset or liability based on the best information available in the circumstances.

The Company used the following methods and significant assumptions to estimate fair value on a recurring basis:

MBS and Other Investments Available for Sale
The estimated fair value of MBS and other investments are based upon the assumptions market participants would use in pricing the security. Such assumptions include quoted market prices (Level 1), market prices of similar securities or observable inputs (Level 2).

Mutual Funds
The estimated fair value of mutual funds are based upon quoted market price assumptions (Level 1).

The following table summarizes the balances of assets and liabilities measured at estimated fair value on a recurring basis at
June 30, 2014 (dollars in thousands):

	Estimated Fair Value			
	Level 1	Level 2	Level 3	Total
Available for Sale Securities				
MBS:				
U.S. government agencies	$—	$1,967	$—	$1,967
Mutual funds	961	—	—	961
Total	$961	$1,967	$—	$2,928

There were no transfers among Level 1, Level 2 and Level 3 during the three and nine months ended June 30, 2014.

The following table summarizes the balances of assets and liabilities measured at estimated fair value on a recurring basis at September 30, 2013 (dollars in thousands):

	Estimated Fair Value			
	Level 1	Level 2	Level 3	Total
Available for Sale Securities				
MBS:				
U.S. government agencies	$—	$2,229	$—	$2,229
Private label residential	—	914	—	914
Mutual funds	958	—	—	958
Total	$958	$3,143	$—	$4,101

There were no transfers between Level 1, Level 2 and Level 3 during the year ended September 30, 2013.

The Company may be required, from time to time, to measure certain financial assets and financial liabilities at fair value on a nonrecurring basis in accordance with GAAP. These include assets that are measured at the lower of cost or market value that were recognized at fair value below cost at the end of the period.

The Company uses the following methods and significant assumptions to estimate fair value on a non-recurring basis:

Impaired Loans: A loan is considered to be impaired when, based on current information and events, it is probable that the Company will be unable to collect all amounts due according to the contractual terms of the loan agreement. The specific reserve for collateral dependent impaired loans was based on the estimated fair value of the collateral less estimated costs to sell, if applicable. The estimated fair value of collateral was determined based primarily on appraisals. In some cases, adjustments were made to the appraised values due to various factors including age of the appraisal, age of comparables included in the appraisal, and known changes in the market and in the collateral. Such adjustments may be significant and typically result in a Level 3 classification of the inputs for determining fair value. Impaired loans are evaluated on a quarterly basis for additional impairment and adjusted accordingly.

MBS and Other Investments Held to Maturity: The estimated fair value of MBS and other investments are based upon the assumptions market participants would use in pricing the security. Such assumptions include quoted market prices (Level 1), market prices of similar securities or observable inputs (Level 2) and unobservable inputs such as dealer quotes, discounted cash flows or similar techniques (Level 3).

OREO and Other Repossessed Assets, net: The Company's OREO and other repossessed assets are initially recorded at estimated fair value less estimated costs to sell. This amount becomes the property's new basis. Estimated fair value was generally determined by management based on a number of factors, including third-party appraisals of estimated fair value in an orderly sale. Estimated costs to sell were based on standard market factors. The valuation of OREO and other repossessed assets is subject to significant external and internal judgment (Level 3).

MSRs: The fair value of the MSRs was determined using a third-party model, which incorporates the expected life of the loans, estimated cost to service the loans, servicing fees received and other factors. The estimated fair value is calculated by stratifying the MSRs based on the predominant risk characteristics that include the underlying loan's interest rate, cash flows of the loan, origination date and term (Level 3).

The following table summarizes the balances of assets measured at estimated fair value on a non-recurring basis at June 30, 2014, and the total losses resulting from these estimated fair value adjustments for the nine months ended June 30, 2014 (dollars in thousands):

	Estimated Fair Value			
	Level 1	Level 2	Level 3	Total Losses
Impaired loans:				
Mortgage Loans:				
One-to four-family	$—	$—	$4,087	$979
Multi-family	—	—	3,276	—
Commercial	—	—	6,970	463
Land	—	—	4,024	260
Consumer loans:				
Home equity and second mortgage	—	—	292	28
Total impaired loans (1)	—	—	18,649	1,730
MBS – held to maturity (2):				
Private label residential	—	91	—	15
OREO and other repossessed items (3)	—	—	11,172	478
Total	$—	$91	$29,821	$2,223

(1) The loss represents charge-offs on collateral dependent loans for estimated fair value adjustments based on the estimated fair value of the collateral. Fair value is the recorded investment less the related allowance.

(2) The loss represents OTTI credit-related charges on held to maturity MBS.

(3) The loss represents the results of management's periodic reviews of the recorded value to determine whether the property continues to be recorded at the lower of its recorded book value or estimated fair value, net of estimated costs to sell.