TIMBERLAND BANCORP INC
Form 10-Q
May 09, 2016
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 March 31, 2016

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 MAY 5, 2016 |
|---|---|
| Common stock, $.01 par value | 6,936,068 |

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PART I. FINANCIAL INFORMATION
Item 1. Financial Statements (unaudited)
TIMBERLAND BANCORP, INC. AND SUBSIDIARY
CONSOLIDATED BALANCE SHEETS
March 31, 2016 and September 30, 2015
(Dollars in thousands, except per share amounts)

| | March 31, 2016 (Unaudited) | September 30, 2015 * |
|---|---|---|
| Assets | | |
| Cash and cash equivalents: | | |
| Cash and due from financial institutions | $ 17,121 | $ 14,014 |
| Interest-bearing deposits in banks | 92,908 | 78,275 |
| Total cash and cash equivalents | 110,029 | 92,289 |
| | | |
| Certificates of deposit ("CDs") held for investment (at cost, which approximates fair value) | 52,524 | 48,611 |
| Investment securities held to maturity, at amortized cost (estimated fair value $8,628 and $8,894) | 7,743 | 7,913 |
| Investment securities available for sale | 1,365 | 1,392 |
| Federal Home Loan Bank ("FHLB") stock | 2,804 | 2,699 |
| Loans held for sale | 1,584 | 3,051 |
| | | |
| Loans receivable | 632,894 | 614,201 |
| Less: Allowance for loan losses | (10,043) | (9,924) |
| Net loans receivable | 622,851 | 604,277 |
| | | |
| Premises and equipment, net | 16,355 | 16,854 |
| Other real estate owned ("OREO") and other repossessed assets, net | 5,458 | 7,854 |
| Accrued interest receivable | 2,232 | 2,170 |
| Bank owned life insurance ("BOLI") | 18,443 | 18,170 |
| Goodwill | 5,650 | 5,650 |
| Mortgage servicing rights ("MSRs"), net | 1,488 | 1,478 |
| Other assets | 3,436 | 3,407 |
| Total assets | $ 851,962 | $ 815,815 |
| | | |
| Liabilities and shareholders' equity | | |
| Liabilities | | |
| Deposits: | | |
| Non-interest-bearing demand | $ 148,980 | $ 141,388 |
| Interest-bearing | 563,058 | 537,524 |
| Total deposits | 712,038 | 678,912 |
| | | |
| FHLB advances | 45,000 | 45,000 |
| Other liabilities and accrued expenses | 2,662 | 2,716 |
| Total liabilities | 759,700 | 726,628 |

* Derived from audited consolidated financial statements.

See notes to unaudited consolidated financial statements

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TIMBERLAND BANCORP, INC. AND SUBSIDIARY
CONSOLIDATED BALANCE SHEETS (continued)
March 31, 2016 and September 30, 2015
(Dollars in thousands, except per share amounts)

| | March 31, 2016 (Unaudited) | September 30, 2015 * |
|---|---|---|
| Shareholders’ equity | | |
| Preferred stock, $.01 par value; 1,000,000 shares authorized; none issued | $ — | $ — |
| Common stock, $.01 par value; 50,000,000 shares authorized; | | |
| 6,933,068 shares issued and outstanding - March 31, 2016 6,988,848 shares issued and outstanding - September 30, 2015 | 9,698 | 10,293 |
| Unearned shares issued to Employee Stock Ownership Plan (“ESOP”) | (793) | (926) |
| Retained earnings | 83,643 | 80,133 |
| Accumulated other comprehensive loss | (286) | (313) |
| Total shareholders’ equity | 92,262 | 89,187 |
| Total liabilities and shareholders’ equity | $ 851,962 | $ 815,815 |

* Derived from audited consolidated financial statements.

See notes to unaudited consolidated financial statements

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TIMBERLAND BANCORP, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF INCOME
For the three and six months ended March 31, 2016 and 2015
(Dollars in thousands, except per share amounts)
(Unaudited)

| | Three Months Ended March 31, | | Six Months Ended March 31, | |
|---|---|---|---|---|
| | 2016 | 2015 | 2016 | 2015 |
| Interest and dividend income | | | | |
| Loans receivable and loans held for sale | $8,306 | $7,352 | $16,735 | $14,861 |
| Investment securities | 74 | 55 | 143 | 120 |
| Dividends from mutual funds and FHLB stock | 39 | 6 | 61 | 13 |
| Interest-bearing deposits in banks and CDs | 231 | 114 | 402 | 219 |
| Total interest and dividend income | 8,650 | 7,527 | 17,341 | 15,213 |
| | | | | |
| Interest expense | | | | |
| Deposits | 507 | 495 | 1,012 | 1,004 |
| FHLB advances | 472 | 465 | 948 | 940 |
| Total interest expense | 979 | 960 | 1,960 | 1,944 |
| | | | | |
| Net interest income | 7,671 | 6,567 | 15,381 | 13,269 |
| | | | | |
| Provision for loan losses | — | — | — | — |
| | | | | |
| Net interest income after provision for loan losses | 7,671 | 6,567 | 15,381 | 13,269 |
| | | | | |
| Non-interest income | | | | |
| Other than temporary impairment (“OTTI”) on investment securities | (24) | — | (24) | — |
| Adjustment for portion of OTTI (transferred from) recorded as other comprehensive income (loss) before income taxes | 1 | (1) | 1 | (1) |
| Net OTTI on investment securities | (23) | (1) | (23) | (1) |
| Gain on sale of investment securities available for sale, net | — | — | — | 45 |
| Service charges on deposits | 937 | 852 | 1,909 | 1,737 |
| ATM and debit card interchange transaction fees | 710 | 643 | 1,409 | 1,273 |
| BOLI net earnings | 137 | 131 | 273 | 268 |
| Gain on sales of loans, net | 393 | 348 | 787 | 584 |
| Escrow fees | 49 | 56 | 89 | 98 |
| Servicing income (loss) on loans sold | 55 | (12) | 120 | (40) |
| Other, net | 255 | 197 | 467 | 374 |
| Total non-interest income, net | 2,513 | 2,214 | 5,031 | 4,338 |

See notes to unaudited consolidated financial statements

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TIMBERLAND BANCORP, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF INCOME (continued)
For the three and six months ended March 31, 2016 and 2015
(Dollars in thousands, except per share amounts)
(Unaudited)

| | Three Months Ended March 31, | | Six Months Ended March 31, | |
|---|---|---|---|---|
| | 2016 | 2015 | 2016 | 2015 |
| Non-interest expense | | | | |
| Salaries and employee benefits | $3,466 | $ 3,284 | $6,936 | $ 6,680 |
| Premises and equipment | 771 | 751 | 1,531 | 1,476 |
| Advertising | 193 | 173 | 398 | 361 |
| OREO and other repossessed assets, net | 195 | 349 | 438 | 425 |
| ATM and debit card interchange transaction fees | 331 | 255 | 653 | 593 |
| Postage and courier | 110 | 114 | 211 | 218 |
| State and local taxes | 138 | 119 | 270 | 236 |
| Professional fees | 117 | 223 | 247 | 399 |
| Federal Deposit Insurance Corporation ("FDIC") insurance | 127 | 148 | 234 | 308 |
| Loan administration and foreclosure | 95 | 76 | 124 | 119 |
| Data processing and telecommunications | 474 | 471 | 924 | 850 |
| Deposit operations | 234 | 219 | 406 | 395 |
| Other | 378 | 472 | 735 | 868 |
| Total non-interest expense | 6,629 | 6,654 | 13,107 | 12,928 |
| | | | | |
| Income before federal income taxes | 3,555 | 2,127 | 7,305 | 4,679 |
| | | | | |
| Provision for federal income taxes | 1,175 | 676 | 2,397 | 1,501 |
| | | | | |
| Net income | $2,380 | $ 1,451 | $4,908 | $ 3,178 |
| | | | | |
| Net income per common share | | | | |
| Basic | $0.35 | $ 0.21 | $0.72 | $ 0.46 |
| Diluted | $0.34 | $ 0.21 | $0.69 | $ 0.45 |
| | | | | |
| Weighted average common shares outstanding | | | | |
| Basic | 6,846,527 | 6,898,192 | 6,858,190 | 6,895,038 |
| Diluted | 7,080,005 | 7,071,792 | 7,081,945 | 7,067,621 |
| | | | | |
| Dividends paid per common share | $0.08 | $ 0.06 | $0.20 | $ 0.11 |

See notes to unaudited consolidated financial statements

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TIMBERLAND BANCORP, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
For the three and six months ended March 31, 2016 and 2015
(Dollars in thousands)
(Unaudited)

| | Three Months Ended March 31, | | Six Months Ended March 31, | |
|---|---|---|---|---|
| | 2016 | 2015 | 2016 | 2015 |
| Comprehensive income | | | | |
| Net income | $2,380 | $1,451 | $4,908 | $3,178 |
| Unrealized holding gain (loss) on investment securities available for sale, net of income taxes of $6, $4, ($1) and $2, respectively | 11 | 8 | (1) | 5 |
| Reclassification adjustment for gain on sale of investment securities available for sale included in net income, net of income taxes of $0, $0, $0 and ($15), respectively. | — | — | — | (30) |
| Change in OTTI on investment securities held to maturity, net of income taxes: | | | | |
| Additional amount recovered related to credit loss for which OTTI was previously recognized, net of income taxes of $6, $1, $7 and $1, respectively | 12 | 1 | 12 | 1 |
| Amount reclassified to credit loss for previously recorded market loss, net of income taxes of ($1), $1, ($1) and $1, respectively | (1) | 1 | (1) | 1 |
| Accretion of OTTI on investment securities held to maturity, net of income taxes of $4, $4, $9, and $8, respectively | 7 | 7 | 17 | 15 |
| Total other comprehensive income (loss), net of income taxes | $29 | $17 | $27 | $(8) |
| Total comprehensive income | $2,409 | $1,468 | $4,935 | $3,170 |

See notes to unaudited consolidated financial statements

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TIMBERLAND BANCORP, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
For the six months ended March 31, 2016 and 2015
(Dollars in thousands, except per share amounts)
(Unaudited)

| | Number of Shares Common Stock | Amount Common Stock | Unearned Shares Issued to ESOP | Retained Earnings | Accumulated Other Compre-hensive Loss | Total |
|---|---|---|---|---|---|---|
| Balance, September 30, 2014 | 7,047,336 | $10,773 | $(1,190) | $73,534 | $ (339) | $82,778 |
| Net income | — | — | — | 3,178 | — | 3,178 |
| Other comprehensive loss | — | — | — | — | (8) | (8) |
| Exercise of stock options | 5,300 | 25 | — | — | — | 25 |
| Common stock dividends ($0.11 per common share) | — | — | — | (775) | — | (775) |
| Earned ESOP shares, net of income taxes | — | 36 | 132 | — | — | 168 |
| Stock option compensation expense | — | 58 | — | — | — | 58 |
| Balance, March 31, 2015 | 7,052,636 | 10,892 | (1,058) | 75,937 | (347) | 85,424 |
| | | | | | | |
| Balance, September 30, 2015 | 6,988,848 | 10,293 | (926) | 80,133 | (313) | 89,187 |
| Repurchase of common stock | (66,000) | (820) | — | — | — | (820) |
| Net income | — | — | — | 4,908 | — | 4,908 |
| Other comprehensive income | — | — | — | — | 27 | 27 |
| Exercise of stock options | 10,220 | 86 | — | — | — | 86 |
| Common stock dividends ($0.20 per common share) | — | — | — | (1,398) | — | (1,398) |
| Earned ESOP shares, net of income taxes | — | 55 | 133 | — | — | 188 |
| Stock option compensation expense | — | 84 | — | — | — | 84 |
| Balance, March 31, 2016 | 6,933,068 | $9,698 | $(793) | $83,643 | $ (286) | $92,262 |

See notes to unaudited consolidated financial statements

TIMBERLAND BANCORP, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS
For the six months ended March 31, 2016 and 2015
(In thousands)
(Unaudited)

| | Six Months Ended March 31, | |
|---|---|---|
| | 2016 | 2015 |
| Cash flows from operating activities | | |
| Net income | $4,908 | $3,178 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation | 673 | 669 |
| Amortization of core deposit intangible ("CDI") | — | 3 |
| Earned ESOP shares | 133 | 132 |
| Stock option compensation expense | 75 | 56 |
| Stock option tax effect less excess tax benefit | 5 | 1 |
| Gain on sales of OREO and other repossessed assets, net | (13) | (127) |
| Provision for OREO losses | 301 | 405 |
| Loss on sales/dispositions of premises and equipment, net | 3 | — |
| BOLI net earnings | (273) | (268) |
| Gain on sales of loans, net | (787) | (584) |
| Increase (decrease) in deferred loan origination fees | (145) | 147 |
| Net OTTI on investment securities | 23 | 1 |
| Gain on sale of investment securities available for sale, net | — | (45) |
| Amortization of MSRs | 295 | 40 |
| Loans originated for sale | (24,305) | (21,696) |
| Proceeds from sales of loans | 26,559 | 20,927 |
| Net change in accrued interest receivable and other assets, and other liabilities and accrued expenses | (514) | 524 |
| Net cash provided by operating activities | 6,938 | 3,363 |
| | | |
| Cash flows from investing activities | | |
| Net increase in CDs held for investment | (3,913) | (6,023) |
| Proceeds from sale of investment securities available for sale | — | 1,220 |
| Proceeds from maturities and prepayments of investment securities available for sale | 27 | 159 |
| Proceeds from maturities and prepayments of investment securities held to maturity | 238 | 243 |
| Purchase of FHLB stock | (105) | — |
| Redemption of FHLB stock | — | 111 |
| Increase in loans receivable, net | (18,505) | (17,955) |
| Additions to premises and equipment | (177) | (412) |
| Capitalized improvements to OREO | (142) | — |
| Proceeds from sales of OREO and other repossessed assets | 2,326 | 1,589 |
| Net cash used in investing activities | (20,251) | (21,068) |

See notes to unaudited consolidated financial statements

TIMBERLAND BANCORP, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS (continued)
For the six months ended March 31, 2016 and 2015
(In thousands)
(Unaudited)

| | Six Months Ended March 31, | |
|---|---|---|
| | 2016 | 2015 |
| Cash flows from financing activities | | |
| Net increase in deposits | $33,126 | $28,157 |
| ESOP tax effect | 55 | 36 |
| Proceeds from exercise of stock options | 86 | 24 |
| Stock option excess tax benefit | 4 | 1 |
| Issuance of common stock | — | 1 |
| Repurchase of common stock | (820) | — |
| Payment of dividends | (1,398) | (775) |
| Net cash provided by financing activities | 31,053 | 27,444 |
| | | |
| Net increase in cash and cash equivalents | 17,740 | 9,739 |
| Cash and cash equivalents | | |
| Beginning of period | 92,289 | 72,354 |
| End of period | $110,029 | $82,093 |
| | | |
| Supplemental disclosure of cash flow information | | |
| Income taxes paid | $2,280 | $1,560 |
| Interest paid | 1,938 | 1,937 |
| | | |
| Supplemental disclosure of non-cash investing activities | | |
| Loans transferred to OREO and other repossessed assets | $76 | $641 |
| Other comprehensive loss related to investment securities | 27 | (8) |

See notes to unaudited consolidated financial statements

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

(1) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES
(a) Basis of Presentation: The accompanying unaudited 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 consolidated 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 consolidated financial statements have been included. All such adjustments are of a normal recurring nature. The unaudited 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, 2015 ("2015 Form 10-K"). The unaudited consolidated results of operations for the six months ended March 31, 2016 are not necessarily indicative of the results that may be expected for the entire fiscal year ending September 30, 2016.

(b) Principles of Consolidation: The unaudited 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 Corporation. 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 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 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 March 31, 2016 presentation with no change to net income or total shareholders' equity as previously reported.

(2) INVESTMENT SECURITIES

Held to maturity and available for sale investment securities have been classified according to management's intent and were as follows as of March 31, 2016 and September 30, 2015 (dollars in thousands):

| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Estimated Fair Value |
|---|---|---|---|---|
| March 31, 2016 | | | | |
| Held to maturity | | | | |
| Mortgage-backed securities ("MBS"): | | | | |
| U.S. government agencies | $ 745 | $ 21 | $ (1 ) | $ 765 |
| Private label residential | 993 | 799 | (6 ) | 1,786 |
| U.S. Treasury and U.S government agency securities | 6,005 | 72 | — | 6,077 |
| Total | $ 7,743 | $ 892 | $ (7 ) | $ 8,628 |
| | | | | |
| Available for sale | | | | |
| MBS: | | | | |
| U.S. government agencies | $ 361 | $ 30 | $ — | $ 391 |
| Mutual funds | 1,000 | — | (26 ) | 974 |
| Total | $ 1,361 | $ 30 | $ (26 ) | $ 1,365 |
| | | | | |
| September 30, 2015 | | | | |
| Held to maturity | | | | |
| MBS: | | | | |
| U.S. government agencies | $ 828 | $ 23 | $ (1 ) | $ 850 |
| Private label residential | 1,081 | 894 | (12 ) | 1,963 |
| U.S. Treasury and U.S. government agency securities | 6,004 | 77 | — | 6,081 |
| Total | $ 7,913 | $ 994 | $ (13 ) | $ 8,894 |
| | | | | |
| Available for sale | | | | |
| MBS: | | | | |
| U.S. government agencies | $ 387 | $ 34 | $ — | $ 421 |
| Mutual funds | 1,000 | — | (29 ) | 971 |
| Total | $ 1,387 | $ 34 | $ (29 ) | $ 1,392 |

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 March 31, 2016 (dollars in thousands):

| | Less Than 12 Months | | | 12 Months or Longer | | | Total | |
|---|---|---|---|---|---|---|---|---|
| | Estimated Fair Value | Gross Unrealized Losses | Quantity | Estimated Fair Value | Gross Unrealized Losses | Quantity | Estimated Fair Value | Gross Unrealized Losses |
| Held to maturity | | | | | | | | |
| MBS: | | | | | | | | |
| U.S. government agencies | $91 | $ — | 2 | $59 | $ (1) | 4 | $150 | $ (1) |
| Private label residential | 40 | (1) | 3 | 163 | (5) | 12 | 203 | (6) |
| Total | $131 | $ (1) | 5 | $222 | $ (6) | 16 | $353 | $ (7) |
| Available for sale | | | | | | | | |
| Mutual funds | $— | $ — | — | $974 | $ (26) | 1 | $974 | $ (26) |
| Total | $— | $ — | — | $974 | $ (26) | 1 | $974 | $ (26) |

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 September 30, 2015 (dollars in thousands):

| | Less Than 12 Months | | | 12 Months or Longer | | | Total | |
|---|---|---|---|---|---|---|---|---|
| | Estimated Fair Value | Gross Unrealized Losses | Quantity | Estimated Fair Value | Gross Unrealized Losses | Quantity | Estimated Fair Value | Gross Unrealized Losses |
| Held to maturity | | | | | | | | |
| MBS: | | | | | | | | |
| U.S. government agencies | $49 | $ — | 4 | $63 | $ (1) | 5 | $112 | $ (1) |
| Private label residential | 1 | — | 1 | 157 | (12) | 11 | 158 | (12) |
| Total | $50 | $ — | 5 | $220 | $ (13) | 16 | $270 | $ (13) |
| Available for sale | | | | | | | | |
| MBS: | | | | | | | | |
| U.S. government agencies | $1 | $ — | 1 | $48 | $ — | 2 | $49 | $ — |
| Mutual funds | — | — | — | 971 | (29) | 1 | 971 | (29) |
| Total | $1 | $ — | 1 | $1,019 | $ (29) | 3 | $1,020 | $ (29) |

The Company has evaluated these securities and has determined that the decline in their value is temporary. The unrealized losses are primarily due to changes in market interest rates and spreads in the market for mortgage-related products. The fair value of these securities is expected to recover as the securities approach their maturity dates and/or as the pricing spreads narrow on mortgage-related securities. The Company has the ability and the intent to hold the investments until the market value recovers. Furthermore, as of March 31, 2016, management does not have the intent to sell any of the securities classified as available for sale where the estimated fair value is below the recorded value and believes that it is more likely than not that the Company will not have to sell such securities before a recovery of cost or recorded value if previously written down.

In accordance with GAAP, the Company bifurcates OTTI into (1) amounts related to credit losses which are recognized through earnings and (2) amounts related to all other factors which are recognized as a component of other comprehensive income (loss). To determine the component of the gross OTTI related to credit losses, the Company compared the amortized cost basis of the 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, prepayment speeds and

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 March 31, 2016 and September 30, 2015:

| | Range Minimum | Range Maximum | Weighted Average |
|---|---|---|---|
| March 31, 2016 | | | |
| Constant prepayment rate | 6.00% | 15.00 % | 9.16 % |
| Collateral default rate | 0.24% | 17.64 % | 5.70 % |
| Loss severity rate | 7.00% | 77.00 % | 41.97 % |
| | | | |
| September 30, 2015 | | | |
| Constant prepayment rate | 6.00% | 15.00 % | 11.49 % |
| Collateral default rate | 0.16% | 14.65 % | 6.08 % |
| Loss severity rate | 3.92% | 65.00 % | 39.83 % |

The following table presents the OTTI for the three and six months ended March 31, 2016 and 2015 (dollars in thousands):

| | Three Months Ended March 31, 2016 | | Three Months Ended March 31, 2015 | |
|---|---|---|---|---|
| | Held To Maturity | Available For Sale | Held To Maturity | Available For Sale |
| Total OTTI | $(24) | $ — | $ — | $ — |
| Adjustment for portion of OTTI recorded as (transfered from) other comprehensive income (loss) before income taxes (1) | 1 | — | (1) | — |
| Net OTTI recognized in earnings (2) | $(23) | $ — | $(1) | $ — |

| | Six Months Ended March 31, 2016 | | Six Months Ended March 31, 2015 | |
|---|---|---|---|---|
| | Held To Maturity | Available For Sale | Held To Maturity | Available For Sale |
| Total OTTI | $(24) | $ — | $ — | $ — |
| Adjustment for portion recorded as (transferred from) other comprehensive income (loss) before income taxes (1) | 1 | — | (1) | — |
| Net OTTI recognized in earnings (2) | $(23) | $ — | $(1) | $ — |

(1) Represents OTTI related to all other factors.
(2) Represents 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 for the six months ended March 31, 2016 and 2015 (dollars in thousands):

| | Six Months Ended March 31, | |
|---|---|---|
| | 2016 | 2015 |
| Beginning balance of credit loss | $1,576 | $1,654 |
| Additions: | | |
| Credit losses for which OTTI was not previously recognized | — | 1 |
| Additional increases to the amount related to credit loss for which OTTI was previously recognized | 20 | — |
| Subtractions: | | |
| Realized losses previously recorded as credit losses | (59) | (38) |
| Ending balance of credit loss | $1,537 | $1,617 |

There was no realized gain on the sale of investment securities for the three and six months ended March 31, 2016. There was no realized gain on the sale of investment securities for the three months ended March 31, 2015 and there was a $45,000 realized gain on the sale of investment securities for the six months ended March 31, 2015. During the three months ended March 31, 2016, the Company recorded a $35,000 net realized loss (as a result of the securities being deemed worthless) on 12 held to maturity residential MBS, of which $32,000 had been recognized previously as a credit loss. During the six months ended March 31, 2016 the Company recorded a $63,000 net realized loss (as a result of securities being deemed worthless) on 15 held to maturity residential MBS, of which $59,000 had been previously recognized as a credit loss. During the three months ended March 31, 2015, the Company recorded a $21,000 net 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 six months ended March 31, 2015, the Company recorded a $38,000 net realized loss (as a result of securities being deemed worthless) on 14 held to maturity residential MBS, of which the entire amount had been recognized previously as a credit loss.

The recorded amount of residential MBS, treasury and agency securities pledged as collateral for public fund deposits, federal treasury tax and loan deposits, FHLB collateral and other non-profit organization deposits totaled $7.14 million and $7.25 million at March 31, 2016 and September 30, 2015, respectively.

The contractual maturities of debt securities at March 31, 2016 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 | $— | $ — | $5 | $ 6 |
| Due after one year to five years | 6,005 | 6,077 | — | — |
| Due after five to ten years | 22 | 23 | — | — |
| Due after ten years | 1,716 | 2,528 | 356 | 385 |
| Total | $7,743 | $ 8,628 | $361 | $ 391 |

(3) GOODWILL

Goodwill is initially recorded when the purchase price paid for an acquisition exceeds the estimated fair value of the net identified tangible and intangible assets acquired. Goodwill is presumed to have an indefinite useful life and is analyzed annually for impairment. The Company performs an annual review during the third quarter of each fiscal year, or more frequently if indicators of potential impairment exist, to determine if the recorded goodwill is impaired.

The goodwill impairment test involves a two-step process. Step one 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.

The Company performed its fiscal year 2015 goodwill impairment test during the quarter ended June 30, 2015 with the assistance of an independent third-party firm specializing in goodwill impairment valuations for financial institutions. The third-party analysis was conducted as of May 31, 2015 and the step one test concluded that the reporting unit's fair value was more than its recorded value and, therefore, step two of the analysis was not necessary. Accordingly, the recorded value of goodwill as of May 31, 2015 was not impaired.

Step one of the goodwill impairment test estimates 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 3.60%, an annual deposit growth rate that ranged from 2.20% to 3.20% and a return on assets that ranged from 0.80% to 1.00%. In addition to the above projections of estimated operating results, key assumptions used to determine the fair value estimate under the income approach were the discount rate of 12.2% and the residual capitalization rate of 9.2%. 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 2015 Valuation Handbook - Guide to Cost of Capital. 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 are 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 nine 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, 2013. 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 29, 2015 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 discounted cash flow income approach analysis, 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.

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 March 31, 2016, management believed that there had been no events or changes in the circumstances since May 31, 2015 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.

(4) LOANS RECEIVABLE AND ALLOWANCE FOR LOAN LOSSES

Loans receivable and loans held for sale by portfolio segment consisted of the following at March 31, 2016 and September 30, 2015 (dollars in thousands):

| | March 31, 2016 | | September 30, 2015 | |
|---|---|---|---|---|
| | Amount | Percent | Amount | Percent |
| Mortgage loans: | | | | |
| One- to four-family | $117,465 | 17.3 % | $116,664 | 17.4 % |
| Multi-family | 42,666 | 6.3 | 52,322 | 7.8 |
| Commercial | 290,817 | 42.8 | 291,216 | 43.5 |
| Construction - custom and owner/builder | 69,817 | 10.3 | 62,954 | 9.4 |
| Construction - speculative one- to four-family | 6,384 | 0.9 | 6,668 | 1.0 |
| Construction - commercial | 22,487 | 3.3 | 20,728 | 3.1 |
| Construction - multi-family | 20,570 | 3.0 | 20,570 | 3.1 |
| Land | 24,322 | 3.6 | 26,140 | 3.9 |
| Total mortgage loans | 594,528 | 87.5 | 597,262 | 89.2 |
| | | | | |
| Consumer loans: | | | | |
| Home equity and second mortgage | 37,144 | 5.5 | 34,157 | 5.1 |
| Other | 4,380 | 0.6 | 4,669 | 0.7 |
| Total consumer loans | 41,524 | 6.1 | 38,826 | 5.8 |
| | | | | |
| Commercial business loans | 43,355 | 6.4 | 33,763 | 5.0 |
| | | | | |
| Total loans receivable | 679,407 | 100.0% | 669,851 | 100.0% |
| Less: | | | | |
| Undisbursed portion of construction loans in process | 44,465 | | 53,457 | |
| Deferred loan origination fees | 2,048 | | 2,193 | |
| Allowance for loan losses | 10,043 | | 9,924 | |
| | 56,556 | | 65,574 | |
| Loans receivable, net | 622,851 | | 604,277 | |
| Loans held for sale (one- to four-family) | 1,584 | | 3,051 | |
| Total loans receivable and loans held for sale, net | $624,435 | | $607,328 | |

Allowance for Loan Losses
The following tables set forth information for the three and six months ended March 31, 2016 and 2015 regarding activity in the allowance for loan losses by portfolio segment (dollars in thousands):

| | Three Months Ended March 31, 2016 | | | | |
|---|---|---|---|---|---|
| | Beginning Allowance | Provision for / (Recapture of) | Charge-offs | Recoveries | Ending Allowance |
| Mortgage loans: | | | | | |
| One-to four-family | $1,420 | $ (147) | $ (2) | $ 52 | $ 1,323 |
| Multi-family | 373 | (58) | — | — | 315 |
| Commercial | 3,898 | 239 | (54) | — | 4,083 |
| Construction – custom and owner/builder | 555 | (13) | — | — | 542 |
| Construction – speculative one- to four-family | 122 | (28) | — | 2 | 96 |
| Construction – commercial | 486 | 131 | — | — | 617 |
| Construction – multi-family | 336 | (77) | — | 150 | 409 |
| Land | 923 | 24 | — | 7 | 954 |
| Consumer loans: | | | | | |
| Home equity and second mortgage | 1,102 | (81) | — | — | 1,021 |
| Other | 161 | 3 | (2) | — | 162 |
| Commercial business loans | 513 | 7 | — | 1 | 521 |
| Total | $9,889 | $ — | $ (58) | $ 212 | $ 10,043 |

| | Six Months Ended March 31, 2016 | | | | |
|---|---|---|---|---|---|
| | Beginning Allowance | Provision for / (Recapture of) | Charge-offs | Recoveries | Ending Allowance |
| Mortgage loans: | | | | | |
| One-to four-family | $1,480 | $ (184) | $ (28) | $ 55 | $ 1,323 |
| Multi-family | 392 | (77) | — | — | 315 |
| Commercial | 4,065 | 99 | (81) | — | 4,083 |
| Construction – custom and owner/builder | 451 | 91 | — | — | 542 |
| Construction – speculative one- to four-family | 123 | (29) | — | 2 | 96 |
| Construction – commercial | 426 | 191 | — | — | 617 |
| Construction – multi-family | 283 | (55) | — | 181 | 409 |
| Land | 1,021 | (72) | (8) | 13 | 954 |
| Consumer loans: | | | | | |
| Home equity and second mortgage | 1,073 | (39) | (13) | — | 1,021 |
| Other | 187 | (21) | (5) | 1 | 162 |
| Commercial business loans | 423 | 96 | — | 2 | 521 |
| Total | $9,924 | $ — | $ (135) | $ 254 | $ 10,043 |

| | Three Months Ended March 31, 2015 | | | | |
|---|---|---|---|---|---|
| | Beginning Allowance | Provision for (Recapture of) | Charge-offs | Recoveries | Ending Allowance |
| Mortgage loans: | | | | | |
| One-to four-family | $ 1,504 | $ 24 | $ (39 ) | $ 107 | $ 1,596 |
| Multi-family | 368 | (66) | — | — | 302 |
| Commercial | 3,646 | (45) | — | — | 3,601 |
| Construction – custom and owner/builder | 460 | 15 | — | — | 475 |
| Construction – speculative one- to four-family | 50 | 14 | — | — | 64 |
| Construction – commercial | 28 | 9 | — | — | 37 |
| Construction – multi-family | 75 | 54 | — | — | 129 |
| Land | 2,817 | (67 ) | — | 3 | 2,753 |
| Consumer loans: | | | | | |
| Home equity and second mortgage | 801 | 5 | (9 ) | — | 797 |
| Other | 159 | 34 | (4 ) | 1 | 190 |
| Commercial business loans | 414 | 23 | — | 1 | 438 |
| Total | $ 10,322 | $ — | $ (52 ) | $ 112 | $ 10,382 |

| | Six Months Ended March 31, 2015 | | | | |
|---|---|---|---|---|---|
| | Beginning Allowance | Provision for (Recapture of) | Charge-offs | Recoveries | Ending Allowance |
| Mortgage loans: | | | | | |
| One-to four-family | $ 1,650 | $ (23 ) | $ (157 ) | $ 126 | $ 1,596 |
| Multi-family | 387 | (85) | — | — | 302 |
| Commercial | 4,836 | (1,235) | — | — | 3,601 |
| Construction – custom and owner/builder | 450 | 25 | — | — | 475 |
| Construction – speculative one- to four-family | 52 | 12 | — | — | 64 |
| Construction – commercial | 78 | (41) | — | — | 37 |
| Construction – multi-family | 25 | 104 | — | — | 129 |
| Land | 1,434 | 1,312 | (4 ) | 11 | 2,753 |
| Consumer loans: | | | | | |
| Home equity and second mortgage | 879 | (62) | (20 ) | — | 797 |
| Other | 176 | 17 | (5 ) | 2 | 190 |
| Commercial business loans | 460 | (24) | — | 2 | 438 |
| Total | $ 10,427 | $ — | $ (186 ) | $ 141 | $ 10,382 |

The following tables present information on the loans evaluated individually and collectively for impairment in the allowance for loan losses by portfolio segment at March 31, 2016 and September 30, 2015 (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 |
| March 31, 2016 | | | | | | |
| Mortgage loans: | | | | | | |
| One- to four-family | $120 | $ 1,203 | $1,323 | $2,930 | $ 114,535 | $117,465 |
| Multi-family | — | 315 | 315 | — | 42,666 | 42,666 |
| Commercial | 412 | 3,671 | 4,083 | 11,977 | 278,840 | 290,817 |
| Construction – custom and owner/builder | — | 542 | 542 | — | 41,312 | 41,312 |
| Construction – speculative one- to four-family | — | 96 | 96 | — | 2,956 | 2,956 |
| Construction – commercial | — | 617 | 617 | — | 16,902 | 16,902 |
| Construction – multi-family | — | 409 | 409 | — | 13,623 | 13,623 |
| Land | 57 | 897 | 954 | 1,185 | 23,137 | 24,322 |
| Consumer loans: | | | | | | |