ESSA Bancorp, Inc.
Form 10-Q
February 11, 2013
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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 December 31, 2012

OR

¨ **Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the transition period from _________ to _________

Commission File No. 001-33384

ESSA Bancorp, Inc.

(Exact name of registrant as specified in its charter)

Pennsylvania	**20-8023072**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification Number)**
200 Palmer Street, Stroudsburg, Pennsylvania	**18360**
(Address of Principal Executive Offices)	**(Zip Code)**

(570) 421-0531

(Registrant s telephone number)

N/A

(Former name or former address, if changed since last report)

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 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 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 definition of large accelerated filer and accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer	¨	Accelerated filer	x
Non-accelerated filer	¨	Smaller reporting company	¨

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). YES ¨ NO x

As of February 5, 2013 there were 13,084,108 shares of the Registrant s common stock, par value $0.01 per share, outstanding.

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Part I. Financial Information

Item 1. Financial Statements

ESSA BANCORP, INC. AND SUBSIDIARY

CONSOLIDATED BALANCE SHEET

(UNAUDITED)

	December 31, 2012	September 30, 2012
	(dollars in thousands)	
Cash and due from banks	$ 12,443	$ 11,034
Interest-bearing deposits with other institutions	7,474	4,516
Total cash and cash equivalents	19,917	15,550
Certificates of deposit	1,766	1,266
Investment securities available for sale, at fair value	331,525	329,585
Loans receivable, held for sale	2,096	346
Loans receivable (net of allowance for loan losses of $7,555 and $7,302)	940,275	950,009
Regulatory stock, at cost	19,054	21,914
Premises and equipment, net	16,100	16,170
Bank-owned life insurance	28,075	27,848
Foreclosed real estate	2,503	2,998
Intangible assets, net	3,207	3,457
Goodwill	8,541	8,541
Deferred income taxes	11,359	11,336
Other assets	21,224	29,766
TOTAL ASSETS	$ 1,405,642	$ 1,418,786
LIABILITIES		
Deposits	$ 967,892	$ 995,634
Short-term borrowings	84,500	43,281
Other borrowings	159,460	191,460
Advances by borrowers for taxes and insurance	6,943	3,432
Other liabilities	9,500	9,568
TOTAL LIABILITIES	1,228,295	1,243,375
STOCKHOLDERS EQUITY		
Preferred Stock ($.01 par value; 10,000,000 shares authorized, none issued)		
Common stock ($.01 par value; 40,000,000 shares authorized, 18,133,095 issued; 13,191,008 and 13,229,908 outstanding at December 31, 2012 and September 30, 2012)	181	181
Additional paid in capital	181,748	181,220
Unallocated common stock held by the Employee Stock Ownership Plan (ESOP)	(10,872)	(10,985)
Retained earnings	67,455	65,181
Treasury stock, at cost; 4,942,087 and 4,903,187 shares outstanding at December 31, 2012 and September 30, 2012, respectively	(62,353)	(61,944)
Accumulated other comprehensive income	1,188	1,758

TOTAL STOCKHOLDERS EQUITY	177,347	175,411
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	$ 1,405,642	$ 1,418,786

See accompanying notes to the unaudited consolidated financial statements.

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ESSA BANCORP, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENT OF INCOME

(UNAUDITED)

	For the Three Months Ended December 31, 2012	2011
	(dollars in thousands, except per share data)	
INTEREST INCOME		
Loans receivable, including fees	$ 12,237	$ 9,341
Investment securities:		
Taxable	1,630	1,638
Exempt from federal income tax	54	48
Other investment income	29	2
Total interest income	13,950	11,029
INTEREST EXPENSE		
Deposits	1,971	1,911
Short-term borrowings	36	5
Other borrowings	1,224	2,405
Total interest expense	3,231	4,321
NET INTEREST INCOME	10,719	6,708
Provision for loan losses	1,000	500
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	9,719	6,208
NONINTEREST INCOME		
Service fees on deposit accounts	807	727
Services charges and fees on loans	229	184
Trust and investment fees	215	215
Gain on sale of investments, net	30	
Gain on sale of loans, net	334	
Earnings on Bank-owned life insurance	226	198
Insurance commissions	175	191
Other	10	9
Total noninterest income	2,026	1,524
NONINTEREST EXPENSE		
Compensation and employee benefits	4,556	3,936
Occupancy and equipment	949	756
Professional fees	312	490
Data processing	663	482
Advertising	110	86

Federal Deposit Insurance Corporation FDIC premiums	185	162
Loss (Gain) on foreclosed real estate	(226)	67
Amortization of intangible assets	250	81
Other	706	602
Total noninterest expense	7,505	6,662
Income before income taxes	4,240	1,070
Income taxes	1,361	184
NET INCOME	$ 2,879	$ 886
Earnings per share		
Basic	$ 0.24	$ 0.08
Diluted	$ 0.24	$ 0.08
Dividends per share	$ 0.05	$ 0.05

See accompanying notes to the unaudited consolidated financial statements.

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ESSA BANCORP, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (LOSS)

(UNAUDITED)

	Three Months Ended December 31, 2012	Three Months Ended December 31, 2011
Net income	$ 2,879	$ 886
Other comprehensive loss:		
Investment securities available for sale:		
Unrealized holding loss	(932)	(1,871)
Tax effect	318	636
Reclassification of gains recognized in net income	(30)	
Tax effect	10	
Net of tax amount	(634)	(1,235)
Pension plan adjustment:		
Related to actuarial losses and prior service cost	97	119
Tax effect	(33)	(41)
Net of tax amount	64	78
Total other comprehensive loss	(570)	(1,157)
Comprehensive income (loss)	$ 2,309	$ (271)

See accompanying notes to the unaudited consolidated financial statements.

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ESSA BANCORP, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS EQUITY

(UNAUDITED)

	Common Stock Number of Shares	Common Stock Amount	Additional Paid In Capital	Unallocated Common Stock Held by the ESOP	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income (Loss)	Total Stockholders Equity
				(Dollars in thousands)				
Balance, September 30, 2012	13,229,908	$ 181	$ 181,220	$ (10,985)	$ 65,181	$ (61,944)	$ 1,758	$ 175,411
Net income					2,879			2,879
Other comprehensive loss:								
Unrealized loss on securities available for sale, net of income tax benefit of $327							(634)	(634)
Change in unrecognized pension cost, net of income taxes of $33							64	64
Cash dividends declared ($.05 per share)					(605)			(605)
Stock based compensation			527					527
Allocation of ESOP stock			1	113				114
Treasury shares purchased	(38,900)					(409)		(409)
Balance, December 31, 2012	13,191,008	$ 181	$ 181,748	$ (10,872)	$ 67,455	$ (62,353)	$ 1,188	$ 177,347

See accompanying notes to the unaudited consolidated financial statements.

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ESSA BANCORP, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENT OF CASH FLOWS

(UNAUDITED)

	For the Three Months Ended December 31, 2012	2011
	(dollars in thousands)	
OPERATING ACTIVITIES		
Net income	$ 2,879	$ 886
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	1,000	500
Provision for depreciation and amortization.	286	240
Amortization and accretion of discounts and premiums, net	369	423
Net gain on sale of investment securities	(30)	
Gain on sale of loans, net	(334)	
Origination of mortgage loans sold	(12,963)	
Proceeds from sale of mortgage loans originated for sale	11,547	
Compensation expense on ESOP	114	121
Stock based compensation	527	534
Decrease in accrued interest receivable	360	326
(Decrease) Increase in accrued interest payable	(13)	226
Earnings on bank-owned life insurance	(226)	(198)
Deferred federal income taxes	307	510
Decrease in prepaid FDIC premiums	175	146
(Gain) loss on foreclosed real estate, net	(226)	67
Amortization of identifiable intangible assets	250	81
Other, net	2,038	51
Net cash provided by operating activities	6,060	3,913
INVESTING ACTIVITIES		
Purchase of certificates of deposit	(500)	
Investment securities available for sale:		
Proceeds from sale of investment securities	1,106	
Proceeds from principal repayments and maturities	37,955	21,253
Purchases	(42,306)	(32,895)
Increase (decrease) in loans receivable, net	8,214	(4,272)
Redemption of FHLB stock	2,860	844
Investment in limited partnership	(110)	(945)
Proceeds from sale of foreclosed real estate	1,246	472
Purchase of premises, equipment, and software	(245)	(221)
Net cash provided by (used for) investing activities	8,220	(15,764)
FINANCING ACTIVITIES		
(Decrease) increase in deposits, net	(21,745)	2,420
Net increase in short-term borrowings	41,219	6,000
Proceeds from other borrowings	7,000	
Repayment of other borrowings	(39,000)	(11,000)
Increase in advances by borrowers for taxes and insurance	3,511	2,347
Purchase of treasury stock shares.	(293)	

Dividends on common stock	(605)	(546)
Net cash used for financing activities	(9,913)	(779)
Increase (decrease) in cash and cash equivalents	4,367	(12,630)
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	15,550	41,694
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ 19,917	$ 29,064
SUPPLEMENTAL CASH FLOW DISCLOSURES		
Cash Paid:		
Interest	$ 3,244	$ 4,096
Income taxes	5	
Noncash items:		
Transfers from loans to foreclosed real estate	$ 525	$ 286
Treasury stock payable	116	

See accompanying notes to the unaudited consolidated financial statements.

ESSA BANCORP, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements

(unaudited)

1. Nature of Operations and Basis of Presentation

The consolidated financial statements include the accounts of ESSA Bancorp, Inc. (the Company), and its wholly owned subsidiary, ESSA Bank & Trust (the Bank), and the Bank s wholly owned subsidiaries, ESSACOR, Inc.; Pocono Investments Company; ESSA Advisory Services, LLC; Integrated Financial Corporation; Integrated Delaware, Inc. and Integrated Abstract Incorporated, a wholly owned subsidiary of Integrated Financial Corporation. The primary purpose of the Company is to act as a holding company for the Bank. The Company is subject to regulation and supervision as a savings and loan holding company by the Federal Reserve Board. The Bank is a Pennsylvania-chartered savings association located in Stroudsburg, Pennsylvania. The Bank s primary business consists of the taking of deposits and granting of loans to customers generally in Monroe, Northampton and Lehigh counties, Pennsylvania. The Bank is subject to regulation and supervision by the Pennsylvania Banking Department and the Federal Deposit Insurance Corporation. The investment in subsidiary on the parent company s financial statements is carried at the parent company s equity in the underlying net assets.

ESSACOR, Inc. is a Pennsylvania corporation that has been used to purchase properties at tax sales that represent collateral for delinquent loans of the Bank. Pocono Investment Company is a Delaware corporation formed as an investment company subsidiary to hold and manage certain investments, including certain intellectual property. ESSA Advisory Services, LLC is a Pennsylvania limited liability company owned 100 percent by ESSA Bank & Trust. ESSA Advisory Services, LLC is a full-service insurance benefits consulting company offering group services such as health insurance, life insurance, short-term and long-term disability, dental, vision, and 401(k) retirement planning as well as individual health products. Integrated Financial Corporation is a Pennsylvania Corporation that provided investment advisory services to the general public as a former subsidiary of First Star Bank. The Company acquired First Star Bank in a transaction that closed on July 31, 2012. Integrated Financial Corporation is currently inactive. Integrated Delaware, Inc. is a Delaware Investment Corporation and was previously owned by First Star Bank. Integrated Abstract Incorporated is a Pennsylvania Corporation that provides title insurance services. All significant intercompany accounts and transactions have been eliminated in consolidation.

The unaudited consolidated financial statements reflect all adjustments, which in the opinion of management, are necessary for a fair presentation of the results of the interim periods and are of a normal and recurring nature. Operating results for the three month periods ended December 31, 2012 are not necessarily indicative of the results that may be expected for the year ending September 30, 2013.

2. Earnings per Share

The following table sets forth the composition of the weighted-average common shares (denominator) used in the basic and diluted earnings per share computation for the three month period ended December 31, 2012 and 2011.

	Three months ended	
	December 31, 2012	December 31, 2011
Weighted-average common shares outstanding	18,133,095	16,980,900
Average treasury stock shares	(4,906,440)	(4,871,278)
Average unearned ESOP shares	(1,080,703)	(1,125,979)
Average unearned non-vested shares	(57,827)	(176,045)
Weighted average common shares and common stock equivalents used to calculate basic earnings per share	12,088,125	10,807,598
Additional common stock equivalents (non-vested stock) used to calculate diluted earnings per share		

Additional common stock equivalents (stock options) used to calculate diluted earnings per share		
Weighted average common shares and common stock equivalents used to calculate diluted earnings per share	12,088,125	10,807,598

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At December 31, 2012 and 2011 there were options to purchase 1,458,379 shares of common stock outstanding at a price of $12.35 per share that were not included in the computation of diluted EPS because to do so would have been anti-dilutive. At December 31, 2012 and 2011 there were 47,913 and 165,958 shares, respectively, of nonvested stock outstanding at a price of $12.35 per share that were not included in the computation of diluted EPS because to do so would have been anti-dilutive.

3. Use of Estimates in the Preparation of Financial Statements

The accounting principles followed by the Company and its subsidiaries and the methods of applying these principles conform to U.S. generally accepted accounting principles (GAAP) and to general practice within the banking industry. In preparing the consolidated financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the Consolidated Balance Sheet date and related revenues and expenses for the period. Actual results could differ significantly from those estimates.

4. Recent Accounting Pronouncements:

In May 2011, the FASB issued ASU 2011-04, Fair Value Measurement (Topic 820): *Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs.* The amendments in this Update result in common fair value measurement and disclosure requirements in U.S. GAAP and IFRSs. Consequently, the amendments change the wording used to describe many of the requirements in U.S. GAAP for measuring fair value and for disclosing information about fair value measurements. The amendments in this Update are to be applied prospectively. For public entities, the amendments are effective during interim and annual periods beginning after December 15, 2011. For nonpublic entities, the amendments are effective for annual periods beginning after December 15, 2011. Early application by public entities is not permitted. The Company has provided the necessary disclosure in Note 11 of the Company s financial statements for the three months ended December 31, 2012.

In June 2011, the FASB issued ASU 2011-05, Comprehensive Income (Topic 220): *Presentation of Comprehensive Income.* The amendments in this Update improve the comparability, clarity, consistency, and transparency of financial reporting and increase the prominence of items reported in other comprehensive income. To increase the prominence of items reported in other comprehensive income and to facilitate convergence of U.S. GAAP and IFRS, the option to present components of other comprehensive income as part of the statement of changes in stockholders equity was eliminated. The amendments require that all non-owner changes in stockholders equity be presented either in a single continuous statement of comprehensive income or in two separate but consecutive statements. In the two-statement approach, the first statement should present total net income and its components followed consecutively by a second statement that should present total other comprehensive income, the components of other comprehensive income, and the total of comprehensive income. All entities that report items of comprehensive income, in any period presented, will be affected by the changes in this Update. For public entities, the amendments are effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. For nonpublic entities, the amendments are effective for fiscal years ending after December 15, 2012, and interim and annual periods thereafter. The amendments in this Update should be applied retrospectively, and early adoption is permitted. The Company has provided the necessary disclosure in the Statement of Comprehensive Income.

In December 2011, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2011-10, *Property, Plant, and Equipment (Topic 360): Derecognition of in Substance Real Estate a Scope Clarification.* The amendments in this Update affect entities that cease to have a controlling financial interest in a subsidiary that is in substance real estate as a result of default on the subsidiary s nonrecourse debt. Under the amendments in this Update, when a parent (reporting entity) ceases to have a controlling financial interest in a subsidiary that is in substance real estate as a result of default on the subsidiary s nonrecourse debt, the reporting entity should apply the guidance in Subtopic 360-20 to determine whether it should derecognize the in substance real estate. Generally, a reporting entity would not satisfy the requirements to derecognize the in substance real estate before the legal transfer of the real estate to the lender and the extinguishment of the related nonrecourse indebtedness. That is, even if the reporting entity ceases to have a controlling financial interest under Subtopic 810-10, the reporting entity would continue to include the real estate, debt, and the results of the subsidiary s operations in its consolidated financial statements until legal title to the real estate is transferred to legally satisfy the debt. The amendments in this Update should be applied on a prospective basis to deconsolidation events occurring after the effective date. Prior periods should not be adjusted even if the reporting entity has continuing involvement with previously derecognized in substance real estate entities. For public entities, the amendments in this Update are effective for fiscal years, and interim periods within those years, beginning on or after June 15, 2012. For nonpublic entities, the amendments are effective for fiscal years ending after December 15, 2013, and interim and annual periods thereafter. Early adoption is permitted. This ASU is not expected to have a significant impact on the Company s financial statements.

In December 2011, the FASB issued ASU 2011-11, *Balance Sheet (Topic 210): Disclosures about Offsetting Assets and Liabilities*. The amendments in this Update affect all entities that have financial instruments and derivative instruments that are either (1) offset in accordance with either Section 210-20-45 or Section 815-10-45 or (2) subject to an enforceable master netting arrangement or similar agreement. The requirements amend the disclosure requirements on offsetting in Section 210-20-50. This information will enable users of an entity s financial statements to evaluate the effect or potential effect of netting arrangements on an entity s financial position, including the effect or potential effect of rights of setoff associated with certain financial instruments and derivative instruments in the scope of this Update. An entity is required to apply the amendments for annual reporting periods beginning on or after January 1, 2013, and interim periods within those annual periods. An entity should provide the disclosures required by those amendments retrospectively for all comparative periods presented. This ASU is not expected to have a significant impact on the Company s financial statements.

In July, 2012, the FASB issued ASU 2012-02, *Intangibles Goodwill and Other (Topic 350) Testing Indefinite-Lived Intangible Assets for Impairment*. ASU 2012-02 give entities the option to first assess qualitative factors to determine whether the existence of events or circumstances leads to a determination that it is more likely than not that an indefinite-lived intangible asset is impaired. If, after assessing the totality of events or circumstances, an entity determines it is more likely than not that an indefinite-lived intangible asset is impaired, then the entity must perform the quantitative impairment test. If, under the quantitative impairment test, the carrying amount of the intangible asset exceeds its fair value, an entity should recognize an impairment loss in the amount of that excess. Permitting an entity to assess qualitative factors when testing indefinite-lived intangible assets for impairment results in guidance that is similar to the goodwill impairment testing guidance in ASU 2011-08. ASU 2012-02 is effective for annual and interim impairment tests performed for fiscal years beginning after September 15, 2012 (early adoption permitted). This ASU is not expected to have a significant impact on the Company s financial statements.

In October, 2012, the FASB issued ASU 2012-06, *Business Combinations (Topic 805) Subsequent Accounting for an Indemnification Asset Recognized at the Acquisition Date as a Result of a Government-Assisted Acquisition of a Financial Institution*. ASU 2012-06 requires that when a reporting entity recognizes an indemnification asset (in accordance with Subtopic 805-20) as a result of a government assisted acquisition of a financial institution and subsequently a change in the cash flows expected to be collected on the indemnification asset occurs (as a result of a change in cash flows expected to be collected on the assets subject to indemnification), the reporting entity should subsequently account for the change in the measurement of the indemnification asset on the same basis as the change in the assets subject to indemnification. Any amortization of changes in value should be limited to the contractual term of the indemnification agreement (that is, the lesser of the term of the indemnification agreement and the remaining life of the indemnified assets). ASU 2012-06 is effective for fiscal years, and interim periods within those years, beginning on or after December 15, 2012. Early adoption is permitted. The amendments should be applied prospectively to any new indemnification assets acquired after the date of adoption and to indemnification assets existing as of the date of adoption arising from a government-assisted acquisition of a financial institution. This ASU is not expected to have a significant impact on the Company s financial statements.

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5. Investment Securities

The amortized cost and fair value of investment securities available for sale are summarized as follows (in thousands):

	December 31, 2012			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for Sale				
Fannie Mae	$ 123,581	$ 3,940	$ (23)	$ 127,498
Freddie Mac	49,088	1,618	(24)	50,682
Governmental National Mortgage Association	46,555	740	(49)	47,246
Other mortgage-backed securities	4,944	170		5,114
Total mortgage-backed securities	224,168	6,468	(96)	230,540
Obligations of states and political subdivisions	24,336	955	(22)	25,269
U.S. government agency securities	55,559	365	(1)	55,923
Corporate obligations	10,476	193	(22)	10,647
Trust-preferred securities	4,875	575		5,450
Other debt securities	1,476	36		1,512
Total debt securities	320,890	8,592	(141)	329,341
Equity securities - financial services	2,191	12	(19)	2,184
Total	$ 323,081	$ 8,604	$ (160)	$ 331,525

	September 30, 2012			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for Sale				
Fannie Mae	$ 111,145	$ 4,652	$ (3)	$ 115,794
Freddie Mac	48,913	1,952	(11)	50,854
Governmental National Mortgage Association	43,164	803	(16)	43,951
Other mortgage-backed securities	5,043	162		5,205
Total mortgage-backed securities	208,265	7,569	(30)	215,804
Obligations of states and political subdivisions	18,611	906		19,517
U.S. government agency securities	74,106	379	(1)	74,484
Corporate obligations	8,602	146	(91)	8,657
Trust-preferred securities	5,852	382	(1)	6,233
Other debt securities	1,476	36		1,512
Total debt securities	316,912	9,418	(123)	326,207
Equity securities - financial services	3,267	111		3,378
Total	$ 320,179	$ 9,529	$ (123)	$ 329,585

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The amortized cost and fair value of debt securities at December 31, 2012, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties (in thousands):

	Available For Sale	
	Amortized Cost	Fair Value
Due in one year or less	$ 2,233	$ 2,253
Due after one year through five years	49,987	50,534
Due after five years through ten years	51,495	52,918
Due after ten years	217,175	223,636
Total	$ 320,890	$ 329,341

For the three months ended December 31, 2012, the Company realized gross gains of $31,000 and gross losses of $1,000 on proceeds from the sale of investment securities of $1.1 million. The Company had no sales of investment securities for the three months ended December 31, 2011.

6. Unrealized Losses on Securities

The following table shows the Company s gross unrealized losses and fair value, aggregated by investment category and length of time that the individual securities have been in a continuous unrealized loss position (in thousands):

	December 31, 2012						
		Less than Twelve Months		Twelve Months or Greater		Total	
	Number of Securities	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
Fannie Mae	3	$ 3,991	$ (22)	$ 1,345	$ (1)	$ 5,336	$ (23)
Freddie Mac	3	5,998	(24)			5,998	(24)
Governmental National Mortgage Association	5	9,087	(49)			9,087	(49)
Obligations of states and political subdivisions	4	5,330	(22)			5,330	(22)
U.S. government agency securities	3	2,905	(1)			2,905	(1)
Corporate obligations	4	2,366	(15)	993	(7)	3,359	(22)
Equity securities-financial services	1	2,041	(19)			2,041	(19)
Total	23	$ 31,718	$ (152)	$ 2,338	$ (8)	$ 34,056	$ (160)

	September 30, 2012						
		Less than Twelve Months		Twelve Months or Greater		Total	
	Number of Securities	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
Fannie Mae	3	$ 4,083	$ (3)	$	$	$ 4,083	$ (3)
Freddie Mac	1	2,002	(11)			2,002	(11)
Governmental National Mortgage Association	5	6,090	(16)			6,090	(16)
U.S. government agency securities	1	999	(1)			999	(1)

Corporate obligations	5	1,059	(25)	1,434	(66)	2,493	(91)
Trust-preferred securities	1	998	(1)			998	(1)
Total	16	$ 15,231	$ (57)	$ 1,434	$ (66)	$ 16,665	$ (123)

The Company s investment securities portfolio contains unrealized losses on securities, including mortgage-related instruments issued or backed by the full faith and credit of the United States government, or generally viewed as having the implied guarantee of the U.S. government, debt obligations of a U.S. state or political subdivision and corporate debt obligations.

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The Company reviews its position quarterly and has asserted that at December 31, 2012, the declines outlined in the above table represent temporary declines and the Company would not be required to sell the security before its anticipated recovery in market value.

The Company has concluded that any impairment of its investment securities portfolio is not other than temporary but is the result of interest rate changes that are not expected to result in the non-collection of principal and interest during the period.

7. Loans Receivable, Net and Allowance for Loan Losses

Loans receivable consist of the following (in thousands):

	December 31, 2012	September 30, 2012
Held for investment:		
Real Estate Loans:		
Residential	$ 689,622	$ 696,350
Construction	3,916	3,805
Commercial	160,059	160,192
Commercial	11,380	12,818
Obligations of states and political subdivisions	34,138	33,736
Home equity loans and lines of credit	46,389	47,925
Other	2,326	2,485
	947,830	957,311
Less allowance for loan losses	7,555	7,302
Net loans	$ 940,275	$ 950,009
Held for sale:		
Real Estate Loans:		
Residential	2,096	346

	Real Estate Loans							
	Residential	Construction (dollars in thousands)	Commercial	Commercial Loans	Obligations of States and Political Subdivisions	Home Equity and Lines of Credit	Other Loans	Total
December 31, 2012								
Total Loans	$ 689,622	$ 3,916	$ 160,059	$ 11,380	$ 34,138	$ 46,389	$ 2,326	$ 947,830
Individually evaluated for impairment	12,897		18,144	263		258		31,562
Loans acquired with deteriorated credit quality	341		6,160	533		44	17	7,095
Collectively evaluated for impairment	676,384	3,916	135,755	10,584	34,138	46,087	2,309	909,173

	Commercial Loans	Obligations of States and	Home Equity and Lines of	Other Loans	Total

	Real Estate Loans				Political	Credit		
	Residential	Construction (dollars in thousands)	Commercial		Subdivisions			
September 30, 2012								
Total Loans	$ 696,350	$ 3,805	$ 160,192	$ 12,818	$ 33,736	$ 47,925	$ 2,485	$ 957,311
Individually evaluated for impairment	7,942		17,415	423		191		25,971
Loans acquired with deteriorated credit quality	271		6,159	1,007		44	19	7,500
Collectively evaluated for impairment	688,137	3,805	136,618	11,388	33,736	47,690	2,466	923,840

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We maintain a loan review system that allows for a periodic review of our loan portfolio and the early identification of potential impaired loans. Such system takes into consideration, among other things, delinquency status, size of loans, type and market value of collateral and financial condition of the borrowers. Specific loan loss allowances are established for identified losses based on a review of such information. A loan evaluated for impairment is considered to be impaired when, based on current information and events, it is probable that we will be unable to collect all amounts due according to the contractual terms of the loan agreement. All loans identified as impaired are evaluated independently. We do not aggregate such loans for evaluation purposes. Impairment is measured on a loan-by-loan basis for commercial and construction loans by the present value of expected future cash flows discounted at the loan s effective interest rate, the loan s obtainable market price, or the fair value of the collateral if the loan is collateral-dependent.

Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. Accordingly, the Company does not separately identify individual consumer and residential mortgage loans for impairment disclosures, unless such loans are part of a larger relationship that is impaired, or are classified as a troubled debt restructuring.

A loan is considered to be a troubled debt restructuring (TDR) loan when the Company grants a concession to the borrower because of the borrower s financial condition that it would not otherwise consider. Such concessions include the reduction of interest rates, forgiveness of principal or interest, or other modifications of interest rates that are less than the current market rate for new obligations with similar risk. TDR loans that are in compliance with their modified terms and that yield a market rate may be removed from the TDR status after a period of performance.

The following table includes the recorded investment and unpaid principal balances for impaired loans with the associated allowance amount, if applicable. Also presented are the average recorded investments in the impaired loans and the related amount of interest recognized during the time within the period that the impaired loans were impaired.

	Recorded Investment	Unpaid Principal Balance	Associated Allowance	Average Recorded Investment	Interest Income Recognized
December 31, 2012					
With no specific allowance recorded:					
Real Estate Loans					
Residential	$ 10,101	$ 10,097	$	$ 6,405	$ 34
Construction					
Commercial	23,073	23,117		22,524	171
Commercial	752	750		1,115	2
Obligations of states and political subdivisions					
Home equity loans and lines of credit	293	293		229	
Other	17	17		18	
Total	34,236	34,274		30,291	207
With an allowance recorded:					
Real Estate Loans					
Residential	3,137	3,135	698	3,052	27
Construction					
Commercial	1,231	1,234	266	1,244	4
Commercial	44	42	11	43	
Obligations of states and political subdivisions					
Home equity loans and lines of credit	9	9	2	9	
Other					
Total	4,421	4,420	977	4,348	31
Total:					
Real Estate Loans					
Residential	13,238	13,232	698	9,457	61
Construction					
Commercial	24,304	24,351	266	23,768	175
Commercial	796	792	11	1,158	2
Obligations of states and political subdivisions					
Home equity loans and lines of credit	302	302	2	238	
Other	17	17		18	
Total Impaired Loans	$ 38,657	$ 38,694	$ 977	$ 34,639	$ 238

	Recorded Investment	Unpaid Principal Balance	Associated Allowance	Average Recorded Investment	Interest Income Recognized
September 30, 2012					
With no specific allowance recorded:					
Real Estate Loans					
Residential	$ 5,182	$ 5,177	$	$ 4,687	$ 82
Construction					
Commercial	22,290	22,341		13,584	457
Commercial	1,386	1,385		581	28
Obligations of states and political subdivisions					
Home equity loans and lines of credit	226	226		238	
Other	19	19		25	
Total	29,103	29,148		19,115	567
With an allowance recorded:					
Real Estate Loans					
Residential	3,031	3,030	661	1,892	68
Construction					
Commercial	1,284	1,286	270	1,326	13
Commercial	44	44	12	47	
Obligations of states and political subdivisions					
Home equity loans and lines of credit	9	9	9	13	1
Other					
Total	4,368	4,369	952	3,278	82
Total:					
Real Estate Loans					
Residential	8,213	8,207	661	6,579	150
Construction					
Commercial	23,574	23,627	270	14,910	470
Commercial	1,430	1,429	12	628	28
Obligations of states and political subdivisions					
Home equity loans and lines of credit	235	235	9	251	1
Other	19	19		25	
Total Impaired Loans	$ 33,471	$ 33,517	$ 952	$ 22,393	$ 649

Management uses a ten point internal risk rating system to monitor the credit quality of the overall loan portfolio. The first six categories are considered not criticized, and are aggregated as Pass rated. The criticized rating categories utilized by management generally follow bank regulatory definitions. The Special Mention category includes assets that are currently protected but are potentially weak, resulting in an undue and unwarranted credit risk, but not to the point of justifying a Substandard classification. Loans in the Substandard category have well-defined weaknesses that jeopardize the liquidation of the debt, and have a distinct possibility that some loss will be sustained if the weaknesses are not corrected. All loans greater than 90 days past due are considered Substandard. The portion of any loan that represents a specific allocation of the allowance for loan losses is placed in the Doubtful category. Any portion of a loan that has been charged off is placed in the Loss category.

To help ensure that risk ratings are accurate and reflect the present and future capacity of borrowers to repay a loan as agreed, the Bank has a structured loan rating process with several layers of internal and external oversight. Generally, consumer and residential mortgage loans are included in the Pass categories unless a specific action, such as bankruptcy, repossession, or death occurs to raise awareness of a possible credit event. The Bank s Commercial Loan Officers are responsible for the timely and accurate risk rating of the loans in their portfolios at origination and on an ongoing basis. The Bank s Commercial Loan Officers perform an annual review of all commercial relationships $250,000 or greater. Confirmation of the appropriate risk grade is included in the review on an ongoing basis. The Bank engages an external consultant to conduct loan reviews on at least a semi-annual basis. Generally, the external consultant reviews commercial relationships greater than $500,000 and/or all criticized relationships. Detailed reviews, including plans for resolution, are performed on loans classified as Substandard on a quarterly basis. Loans in the Special Mention and Substandard categories that are collectively evaluated for impairment are given separate consideration in the determination of the allowance.

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The following tables present the classes of the loan portfolio summarized by the aggregate Pass and the criticized categories of Special Mention, Substandard and Doubtful within the internal risk rating system as of December 31, 2012 and September 30, 2012 (in thousands):

December 31, 2012	Pass	Special Mention	Substandard	Doubtful	Total
Commercial real estate loans	$ 132,220	$ 3,900	$ 23,939	$	$ 160,059
Commercial	10,764	358	258		11,380
Obligations of states and political subdivisions	34,138				34,138
Total	$ 177,122	$ 4,258	$ 24,197	$	$ 205,577

September 30, 2012	Pass	Special Mention	Substandard	Doubtful	Total
Commercial real estate loans	$ 132,841	$ 5,502	$ 21,849	$	$ 160,192
Commercial	12,035	360	423		12,818
Obligations of states and political subdivisions	33,736				33,736
Total	$ 178,612	$ 5,862	$ 22,272	$	$ 206,746

All other loans are underwritten and structured using standardized criteria and characteristics, primarily payment performance, and are normally risk rated and monitored collectively on a monthly basis. These are typically loans to individuals in the consumer categories and are delineated as either performing or non-performing. The following tables present the risk ratings in the consumer categories of performing and non-performing loans at December 31, 2012 and September 30, 2012 (in thousands):

	Performing	Non-performing	Total
December 31, 2012			
Real estate loans:			
Residential	$ 677,765	$ 11,857	$ 689,622
Construction	3,916		3,916
Home Equity loans and lines of credit	46,069	320	46,389
Other	2,309	17	2,326
Total	$ 730,059	$ 12,194	$ 742,253

	Performing	Non-performing	Total
September 30, 2012			
Real estate loans:			
Residential	$ 685,814	$ 10,536	$ 696,350
Construction	3,805		3,805
Home Equity loans and lines of credit	47,552	373	47,925
Other	2,466	19	2,485
Total	$ 739,637	$ 10,928	$ 750,565

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Management further monitors the performance and credit quality of the loan portfolio by analyzing the age of the portfolio as determined by the length of time a recorded payment is past due. The following tables present the classes of the loan portfolio summarized by the aging categories of performing loans and nonaccrual loans as of December 31, 2012 and September 30, 2012 (in thousands):

	Current	31-60 Days Past Due	61-90 Days Past Due	Greater than 90 Days Past Due and still accruing	Non-Accrual	Total Past Due and Non-Accrual	Total Loans
December 31, 2012							
Real estate loans							
Residential	$ 672,854	$ 3,531	$ 1,380	$	$ 11,857	$ 16,768	$ 689,622
Construction	3,916						3,916
Commercial	146,902	1,142	58		11,957	13,157	160,059
Commercial	10,043				1,337	1,337	11,380
Obligations of states and political subdivisions	34,138						34,138
Home equity loans and lines of credit	45,795	245	29		320	594	46,389
Other	2,274	35			17	52	2,326
Total	$ 915,922	$ 4,953	$ 1,467	$	$ 25,488	$ 31,908	$ 947,830

	Current	31-60 Days Past Due	61-90 Days Past Due	Greater than 90 Days Past Due and still accruing	Non-Accrual	Total Past Due and Non-Accrual	Total Loans
September 30, 2012							
Real estate loans							
Residential	$ 680,876	$ 3,664	$ 1,274	$	$ 10,536	$ 15,474	$ 696,350
Construction	3,805						3,805
Commercial	142,277	3,658	3,348		10,909	17,915	160,192
Commercial	10,948				1,870	1,870	12,818
Obligations of states and political subdivisions	33,736						33,736
Home equity loans and lines of credit	46,967	447	138		373	958	47,925
Other	2,452	14			19	33	2,485
Total	$ 921,061	$ 7,783	$ 4,760	$	$ 23,707	$ 36,250	$ 957,311

Our allowance for loan losses is maintained at a level necessary to absorb loan losses that are both probable and reasonably estimable. Management, in determining the allowance for loan losses, considers the losses inherent in its loan portfolio and changes in the nature and volume of loan activities, along with the general economic and real estate market conditions. Our allowance for loan losses consists of two elements: (1) an allocated allowance, which comprises allowances established on specific loans and class allowances based on historical loss experience and current trends, and (2) an allocated allowance based on general economic conditions and other risk factors in our markets and portfolios. We maintain a loan review system, which allows for a periodic review of our loan portfolio and the early identification of potential impaired loans. Such system takes into consideration, among other things, delinquency status, size of loans, type and market value of collateral and financial condition of the borrowers. General loan loss allowances are based upon a combination of factors including, but not limited to, actual loan loss experience, composition of the loan portfolio, current economic conditions, management s judgment and losses which are probable and reasonably estimable. The allowance is increased through provisions charged against current earnings and recoveries of previously charged-off loans. Loans that are determined to be uncollectible are charged against the allowance. While management uses available information to recognize probable and reasonably estimable loan losses, future loss provisions may be necessary, based on changing economic conditions. Payments received on impaired loans generally are either applied against principal or reported as interest income, according to management s judgment as to the collectability of principal. The allowance for loan losses as of December 31, 2012 is maintained at a level that represents management s best estimate of losses inherent in the loan portfolio, and such losses were both probable and reasonably estimable.

In addition, the FDIC and the Pennsylvania Department of Banking, as an integral part of their examination process, have periodically reviewed our allowance for loan losses. The banking regulators may require that we recognize additions to the allowance based on its analysis and review of information available to it at the time of its examination.

Management reviews the loan portfolio on a quarterly basis using a defined, consistently applied process in order to make appropriate and timely adjustments to the ALL. When information confirms all or part of specific loans to be uncollectible, these amounts are promptly charged off against the ALL.

The following table summarizes the primary segments of the ALL, segregated into the amount required for loans individually evaluated for impairment and the amount required for loans collectively evaluated for impairment as of December 31, 2012 (in thousands):

	Real Estate Loans	Commercial Loans	Obligations of States and Political Subdivisions	Home Equity Loans and Lines of Credit	Other Loans	Unallocated