RIVERVIEW BANCORP INC
Form 10-Q
January 31, 2012
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, 2011

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: 0-22957

RIVERVIEW BANCORP, INC.

(Exact name of registrant as specified in its charter)

| | |
|---|---|
| Washington | 91-1838969 |
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer I.D. Number) |
| 900 Washington St., Ste. 900,Vancouver, Washington | 98660 |
| (Address of principal executive offices) | (Zip Code) |

Registrant's telephone number, including area code: (360) 693-6650

Indicate by check mark whether the registrant (1) 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 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: Common Stock, $.01 par value per share, 22,471,890 shares outstanding as of January 27, 2012.

Form 10-Q

RIVERVIEW BANCORP, INC. AND SUBSIDIARY
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Forward Looking Statements

As used in this Form 10-Q, the terms “we,” “our” and “Company” refer to Riverview Bancorp, Inc. and its consolidated subsidiaries, unless the context indicates otherwise. When we refer to “Bank” in this Form 10-Q, we are referring to Riverview Community Bank, a wholly-owned subsidiary of Riverview Bancorp, Inc.

“Safe Harbor” statement under the Private Securities Litigation Reform Act of 1995: When used in this Form 10-Q the words “believes,” “expects,” “anticipates,” “estimates,” “forecasts,” “intends,” “plans,” “targets,” “potentially,” “probab “outlook,” or similar expressions or future or conditional verbs such as “may,” “will,” “should,” “would,” and “could.” or si expression are intended to identify “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements include statements with respect to our beliefs, plans, objectives, goals, expectations, assumptions and statements about future performance. These forward-looking statements are subject to known and unknown risks, uncertainties and other factors that could cause actual results to differ materially from the results anticipated, including, but not limited to: the credit risks of lending activities, including changes in the level and trend of loan delinquencies and write-offs and changes in the Company’s allowance for loan losses and provision for loan losses that may be impacted by deterioration in the housing and commercial real estate markets; changes in general economic conditions, either nationally or in the Company’s market areas; changes in the levels of general interest rates, and the relative differences between short and long term interest rates, deposit interest rates, the Company’s net interest margin and funding sources; fluctuations in the demand for loans, the number of unsold homes, land and other properties and fluctuations in real estate values in the Company’s market areas; secondary market conditions for loans and the Company’s ability to sell loans in the secondary market; results of examinations of our bank subsidiary, Riverview Community Bank by the Office of the Comptroller of the Currency and of the Company by the Board of Governors of the Federal Reserve System, or other regulatory authorities, including the possibility that any such regulatory authority may, among other things, require the Company to increase its reserve for loan losses, write-down assets, change Riverview Community Bank’s regulatory capital position or affect the Company’s ability to borrow funds or maintain or increase deposits, which could adversely affect its liquidity and earnings; the Company’s compliance with regulatory enforcement actions entered into with its banking regulators and the possibility that noncompliance could result in the imposition of additional enforcement actions and additional requirements or restrictions on its operations; legislative or regulatory changes that adversely affect the Company’s business including changes in regulatory policies and principles, or the interpretation of regulatory capital or other rules; the Company’s ability to attract and retain deposits; further increases in premiums for deposit insurance; the Company’s ability to control operating costs and expenses; the use of estimates in determining fair value of certain of the Company’s assets, which estimates may prove to be incorrect and result in significant declines in valuation; difficulties in reducing risks associated with the loans on the Company’s balance sheet; staffing fluctuations in response to product demand or the implementation of corporate strategies that affect the Company’s workforce and potential associated charges; computer systems on which the Company depends could fail or experience a security breach; the Company’s ability to retain key members of its senior management team; costs and effects of litigation, including settlements and judgments; the Company’s ability to implement its business strategies; the Company’s ability to successfully integrate any assets, liabilities, customers, systems, and management personnel it may acquire into its operations and the Company’s ability to realize related revenue synergies and cost savings within expected time frames and any goodwill charges related thereto; increased competitive pressures among financial services companies; changes in consumer spending, borrowing and savings habits; the availability of resources to address changes in laws, rules, or regulations or to respond to regulatory actions; the Company’s ability to pay dividends on its common stock and interest or principal payments on its junior subordinated debentures; adverse changes in the securities markets; inability of key third-party providers to perform their obligations to us; changes in accounting policies and practices, as may be adopted by the financial institution regulatory agencies or the Financial Accounting Standards Board, including additional guidance and interpretation on accounting issues and details of the implementation of new accounting methods; other economic, competitive, governmental, regulatory, and technological factors affecting the Company’s operations, pricing, products and services and the other risks described from time to time in our filings with the Securities and Exchange Commission.

The Company cautions readers not to place undue reliance on any forward-looking statements. Moreover, you should treat these statements as speaking only as of the date they are made and based only on information then actually known to the Company. The Company does not undertake to revise any forward-looking statements to reflect the occurrence of anticipated or unanticipated events or circumstances after the date of such statements. These risks could cause our actual results for fiscal 2012 and beyond to differ materially from those expressed in any forward-looking statements by, or on behalf of, us, and could negatively affect the Company’s operating and stock price performance.

Part I. Financial Information
Item 1. Financial Statements (Unaudited)

RIVERVIEW BANCORP, INC. AND SUBSIDIARY

CONSOLIDATED BALANCE SHEETS
DECEMBER 31, 2011 AND MARCH 31, 2011

| (In thousands, except share and per share data) (Unaudited) | | December 31, 2011 | | March 31, 2011 |
|---|---|---|---|---|
| ASSETS | | | | |
| Cash (including interest-earning accounts of $23,146 and $37,349) | $ | 36,313 | $ | 51,752 |
| Certificates of deposit held for investment | | 42,718 | | 14,900 |
| Loans held for sale | | 659 | | 173 |
| Investment securities held to maturity, at amortized cost (fair value of $542 and $556) | | 493 | | 506 |
| Investment securities available for sale, at fair value (amortized cost of $8,123 and $8,514) | | 6,337 | | 6,320 |
| Mortgage-backed securities held to maturity, at amortized cost (fair value of $182 and $199) | | 177 | | 190 |
| Mortgage-backed securities available for sale, at fair value (amortized cost of $1,107 and $1,729) | | 1,146 | | 1,777 |
| Loans receivable (net of allowance for loan losses of $15,926 and $14,968) | | 678,626 | | 672,609 |
| Real estate and other personal property owned | | 20,667 | | 27,590 |
| Prepaid expenses and other assets | | 6,087 | | 5,887 |
| Accrued interest receivable | | 2,378 | | 2,523 |
| Federal Home Loan Bank stock, at cost | | 7,350 | | 7,350 |
| Premises and equipment, net | | 16,351 | | 16,100 |
| Deferred income taxes, net | | 594 | | 9,447 |
| Mortgage servicing rights, net | | 299 | | 396 |
| Goodwill | | 25,572 | | 25,572 |
| Core deposit intangible, net | | 157 | | 219 |
| Bank owned life insurance | | 16,406 | | 15,952 |
| TOTAL ASSETS | $ | 862,330 | $ | 859,263 |
| | | | | |
| LIABILITIES AND EQUITY | | | | |
| | | | | |
| LIABILITIES: | | | | |
| Deposit accounts | $ | 735,046 | $ | 716,530 |
| Accrued expenses and other liabilities | | 9,574 | | 9,396 |
| Advanced payments by borrowers for taxes and insurance | | 409 | | 680 |
| Junior subordinated debentures | | 22,681 | | 22,681 |
| Capital lease obligations | | 2,531 | | 2,567 |
| Total liabilities | | 770,241 | | 751,854 |
| | | | | |
| COMMITMENTS AND CONTINGENCIES (See Note 15) | | | | |
| | | | | |
| EQUITY: | | | | |
| Shareholders’ equity | | | | |
| | | - | | - |

| | | | | |
|---|---|---|---|---|
| Serial preferred stock, $.01 par value; 250,000 authorized, issued and outstanding: none | | | | |
| Common stock, $.01 par value; 50,000,000 authorized | | | | |
| December 31, 2011 – 22,471,890 issued and outstanding | | 225 | | 225 |
| March 31, 2011 – 22,471,890 issued and outstanding | | | | |
| Additional paid-in capital | | 65,621 | | 65,639 |
| Retained earnings | | 27,493 | | 43,193 |
| Unearned shares issued to employee stock ownership trust | | (619) | | (696) |
| Accumulated other comprehensive loss | | (1,153) | | (1,417) |
| Total shareholders' equity | | 91,567 | | 106,944 |
| | | | | |
| Noncontrolling interest | | 522 | | 465 |
| Total equity | | 92,089 | | 107,409 |
| TOTAL LIABILITIES AND EQUITY | $ | 862,330 | $ | 859,263 |

See notes to consolidated financial statements.

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RIVERVIEW BANCORP, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF OPERATIONS
FOR THE THREE AND NINE MONTHS ENDED DECEMBER 31, 2011 AND 2010
(In thousands, except share and per share data)
(Unaudited)

| | Three Months Ended December 31, | | Nine Months Ended December 31, | |
|---|---|---|---|---|
| | 2011 | 2010 | 2011 | 2010 |
| Interest Income: | | | | |
| Interest and fees on loans receivable | $9,669 | $ 10,593 | $29,764 | $ 32,458 |
| Interest on investment securities – taxable | 28 | 28 | 109 | 115 |
| Interest on investment securities – nontaxable | 11 | 14 | 35 | 43 |
| Interest on mortgage-backed securities | 12 | 21 | 41 | 70 |
| Other interest and dividends | 109 | 77 | 273 | 140 |
| Total interest and dividend income | 9,829 | 10,733 | 30,222 | 32,826 |
| | | | | |
| Interest Expense: | | | | |
| Interest on deposits | 1,061 | 1,567 | 3,449 | 5,232 |
| Interest on borrowings | 381 | 359 | 1,121 | 1,119 |
| Total interest expense | 1,442 | 1,926 | 4,570 | 6,351 |
| Net interest income | 8,387 | 8,807 | 25,652 | 26,475 |
| Less provision for loan losses | 8,100 | 1,600 | 11,850 | 4,575 |
| Net interest income after provision for loan losses | 287 | 7,207 | 13,802 | 21,900 |
| | | | | |
| Non-interest income: | | | | |
| Fees and service charges | 962 | 955 | 3,082 | 3,131 |
| Asset management fees | 568 | 520 | 1,763 | 1,533 |
| Net gain on sale of loans held for sale | 29 | 96 | 73 | 339 |
| Bank owned life insurance | 151 | 151 | 455 | 451 |
| Other | (180) | 142 | (107) | 696 |
| Total non-interest income | 1,530 | 1,864 | 5,266 | 6,150 |
| | | | | |
| Non-interest expense: | | | | |
| Salaries and employee benefits | 4,014 | 4,090 | 12,039 | 12,115 |
| Occupancy and depreciation | 1,211 | 1,208 | 3,540 | 3,497 |
| Data processing | 306 | 274 | 1,136 | 774 |
| Amortization of core deposit intangible | 20 | 23 | 62 | 72 |
| Advertising and marketing expense | 286 | 187 | 814 | 577 |
| FDIC insurance premium | 289 | 402 | 848 | 1,240 |
| State and local taxes | 150 | 184 | 410 | 502 |
| Telecommunications | 109 | 105 | 324 | 317 |
| Professional fees | 334 | 311 | 971 | 958 |
| Real estate owned expenses | 2,781 | 897 | 3,967 | 1,183 |
| Other | 692 | 572 | 2,083 | 1,695 |
| Total non-interest expense | 10,192 | 8,253 | 26,194 | 22,930 |

| | | | | |
|---|---|---|---|---|
| Income (loss) before income tax | (8,375 ) | 818 | (7,126 ) | 5,120 |
| Provision for income tax | 8,220 | 239 | 8,574 | 1,659 |
| Net income (loss) | $(16,595 ) | $ 579 | $(15,700 ) | $ 3,461 |
| | | | | |
| Earnings (loss) per common share: | | | | |
| Basic | $(0.74 ) | $ 0.03 | $(0.70 ) | $ 0.20 |
| Diluted | (0.74 ) | 0.03 | (0.70 ) | 0.20 |
| Weighted average number of shares outstanding: | | | | |
| Basic | 22,321,011 | 22,296,378 | 22,314,876 | 17,044,751 |
| Diluted | 22,321,011 | 22,297,043 | 22,314,876 | 17,044,751 |

See notes to consolidated financial statements.

RIVERVIEW BANCORP, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF EQUITY
FOR THE NINE MONTHS ENDED DECEMBER 31, 2011 AND 2010

| (In thousands, except share data) (Unaudited) | Common Stock Shares | Common Stock Amount | Additional Paid-In Capital | Retained Earnings | Unearned Shares Issued to Employee Stock Ownership Trust | Accumulated Other Comprehensive Loss | Noncontrolling Interest | Total |
|---|---|---|---|---|---|---|---|---|
| Balance April 1, 2010 | 10,923,773 | $ 109 | $ 46,948 | $ 38,878 | $ (799) | $ (1,202) | $ 420 | $ 84,354 |
| Issuance of common stock (net) | 11,548,117 | 116 | 18,653 | - | - | - | - | 18,769 |
| Stock based compensation expense | - | - | 73 | - | - | - | - | 73 |
| Earned ESOP shares | - | - | (32) | - | 77 | - | - | 45 |
| | 22,471,890 | 225 | 65,642 | 38,878 | (722) | (1,202) | 420 | 103,241 |
| Comprehensive income: | | | | | | | | |
| Net income | - | - | - | 3,461 | - | - | - | 3,461 |
| Other comprehensive income, net of tax: | | | | | | | | |
| Unrealized holding loss on securities available for sale | - | - | - | - | - | (252) | - | (252) |
| Noncontrolling interest | - | - | - | - | - | - | 35 | 35 |
| Total comprehensive income | - | - | - | - | - | - | - | 3,244 |
| | | | | | | | | |
| Balance December 31, 2010 | 22,471,890 | $ 225 | $ 65,642 | $ 42,339 | $ (722) | $ (1,454) | $ 455 | $ 106,485 |
| | | | | | | | | |
| Balance April 1, 2011 | 22,471,890 | $ 225 | $ 65,639 | $ 43,193 | $ (696) | $ (1,417) | $ 465 | $ 107,409 |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Stock based compensation expense | - | - | 11 | - | - | - | - | 11 |
| Earned ESOP shares | - | - | (29) | - | 77 | - | - | 48 |
| | 22,471,890 | 225 | 65,621 | 43,193 | (619) | (1,417) | 465 | 107,468 |
| Comprehensive loss: | | | | | | | | |
| Net loss | - | - | - | (15,700) | - | - | - | (15,700) |
| Other comprehensive loss, net of tax: | | | | | | | | |
| Unrealized holding gain on securities available for sale | - | - | - | - | - | 264 | - | 264 |
| Noncontrolling interest | - | - | - | - | - | - | 57 | 57 |
| Total comprehensive loss | - | - | - | - | - | - | - | (15,379) |
| | | | | | | | | |
| Balance December 31, 2011 | 22,471,890 | 225 | 65,621 | 27,493 | (619) | (1,153) | 522 | 92,089 |

See notes to consolidated financial statements.

RIVERVIEW BANCORP, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE NINE MONTHS ENDED DECEMBER 31, 2011 AND 2010

| (In thousands) (Unaudited) | Nine Months Ended December 31, 2011 | Nine Months Ended December 31, 2010 |
|---|---|---|
| Cash flows from operating activities: | | |
| Net income (loss) | $ (15,700) | $ 3,461 |
| Adjustments to reconcile net income (loss) to cash provided by operating activities: | | |
| Depreciation and amortization | 1,429 | 1,470 |
| Provision for loan losses | 11,850 | 4,575 |
| Noncash expense related to ESOP | 48 | 45 |
| Provision for deferred income taxes | 8,717 | - |
| Decrease in deferred loan origination fees, net of amortization | (33) | (124) |
| Origination of loans held for sale | (2,858) | (10,711) |
| Proceeds from sales of loans held for sale | 2,399 | 10,517 |
| Stock based compensation expense | 11 | 73 |
| Writedown of real estate owned, net | 3,304 | 628 |
| Net (gain) loss on loans held for sale, sale of real estate owned, mortgage-backed securities, investment securities and premises and equipment | 233 | (713) |
| Income from bank owned life insurance | (455) | (451) |
| Changes in assets and liabilities: | | |
| Prepaid expenses and other assets | (353) | 1,614 |
| Accrued interest receivable | 145 | 351 |
| Accrued expenses and other liabilities | 342 | 3,018 |
| Net cash provided by operating activities | 9,079 | 13,753 |
| | | |
| Cash flows from investing activities: | | |
| Loan repayments (originations), net | (19,913) | 27,173 |
| Proceeds from call, maturity, or sale of investment securities available for sale | 5,000 | 9,990 |
| Principal repayments on investment securities available for sale | 392 | 203 |
| Principal repayments on investment securities held to maturity | 13 | 12 |
| Purchase of investment securities available for sale | (5,000) | (10,000) |
| Principal repayments on mortgage-backed securities available for sale | 622 | 794 |
| Principal repayments on mortgage-backed securities held to maturity | 13 | 65 |
| Purchase of certificates of deposit held for investment, net | (27,818) | (17,141) |
| Purchase of premises and equipment and capitalized software | (1,474) | (452) |
| Capitalized improvements related to real estate owned | (207) | (49) |
| Proceeds from sale of real estate owned and premises and equipment | 5,645 | 3,727 |
| Net cash provided by (used in) investing activities | (42,727) | 14,322 |
| | | |
| Cash flows from financing activities: | | |

| | | |
|---|---|---|
| Net increase in deposit accounts | 18,516 | 8,701 |
| Proceeds from issuance of common stock, net | - | 18,769 |
| Proceeds from borrowings | 5,000 | 121,200 |
| Repayment of borrowings | (5,000) | (154,200) |
| Principal payments under capital lease obligation | (36) | (32) |
| Net decrease in advance payments by borrowers | (271) | (200) |
| Net cash provided by (used in) financing activities | 18,209 | (5,762) |
| | | |
| Net increase (decrease) in cash | (15,439) | 22,313 |
| Cash, beginning of period | 51,752 | 13,587 |
| Cash, end of period | $ 36,313 | $ 35,900 |
| | | |
| Supplemental disclosures of cash flow information: | | |
| Cash paid during the period for: | | |
| Interest | $ 3,481 | $ 5,343 |
| Income taxes | 830 | 255 |
| | | |
| Noncash investing and financing activities: | | |
| Transfer of loans to real estate owned, net | $ 2,108 | $ 21,278 |
| Fair value adjustment to securities available for sale | 399 | (382) |
| Income tax effect related to fair value adjustment | (135) | 130 |

See notes to consolidated financial statements.

RIVERVIEW BANCORP, INC. AND SUBSIDIARY
Notes to Consolidated Financial Statements
(Unaudited)

## 1. BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements were prepared in accordance with instructions for Quarterly Reports on 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 accounting principles generally accepted in the United States of America ("GAAP"). However, all adjustments that are, in the opinion of management, necessary for a fair presentation of the interim unaudited 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 financial statements included in the Riverview Bancorp, Inc. Annual Report on Form 10-K for the year ended March 31, 2011 ("2011 Form 10-K"). The results of operations for the nine months ended December 31, 2011 are not necessarily indicative of the results, which may be expected for the fiscal year ending March 31, 2012. The preparation of 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 financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

## 2. PRINCIPLES OF CONSOLIDATION

The accompanying consolidated financial statements include the accounts of Riverview Bancorp, Inc. ("Bancorp" or the "Company"); its wholly-owned subsidiary, Riverview Community Bank ("Bank"); the Bank's wholly-owned subsidiary, Riverview Services, Inc.; and the Bank's majority-owned subsidiary, Riverview Asset Management Corp. ("RAMCorp.") All inter-company transactions and balances have been eliminated in consolidation.

## 3. STOCK PLANS AND STOCK-BASED COMPENSATION

In July 1998, shareholders of the Company approved the adoption of the 1998 Stock Option Plan ("1998 Plan"). The 1998 Plan was effective October 1, 1998 and expired on October 1, 2008. Accordingly, no further option awards may be granted under the 1998 Plan; however, any awards granted prior to its expiration remain outstanding subject to their terms.

In July 2003, shareholders of the Company approved the adoption of the 2003 Stock Option Plan ("2003 Plan"). The 2003 Plan was effective July 2003 and will expire on the tenth anniversary of the effective date, unless terminated sooner by the Company's Board of Directors (the "Board"). Under the 2003 Plan, the Company may grant both incentive and non-qualified stock options to purchase up to 458,554 shares of its common stock to officers, directors and employees. Each option granted under the 2003 Plan has an exercise price equal to the fair market value of the Company's common stock on the date of grant, a maximum term of ten years and a vesting period from zero to five years. At December 31, 2011, there were options for 92,154 shares of the Company's common stock available for future grant under the 2003 Plan.

The following table presents information on stock options outstanding for the period shown.

| | Nine Months Ended December 31, 2011 |
|---|---|

| | Number of Shares | Weighted Average Exercise Price |
|---|---|---|
| Balance, beginning of period | 468,700 | $ 9.00 |
| Grants | - | - |
| Options exercised | - | - |
| Forfeited | (18,200 ) | 10.18 |
| Expired | - | - |
| Balance, end of period | 450,500 | $ 8.96 |

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The following table presents information on stock options outstanding for the periods shown, less estimated forfeitures.

| | Nine Months Ended December 31, 2011 | Nine Months Ended December 31, 2010 |
|---|---|---|
| Stock options fully vested and expected to vest: | | |
| Number | 449,575 | 463,675 |
| Weighted average exercise price | $ 8.96 | $ 9.05 |
| Aggregate intrinsic value (1) | $ - | $ - |
| Weighted average contractual term of options (years) | 5.24 | 5.84 |
| Stock options fully vested and currently exercisable: | | |
| Number | 441,800 | 445,300 |
| Weighted average exercise price | $ 9.06 | $ 9.22 |
| Aggregate intrinsic value (1) | $ - | $ - |
| Weighted average contractual term of options (years) | 5.19 | 6.09 |

(1) The aggregate intrinsic value of a stock options represents the total pre-tax intrinsic value (the amount by which the current market value of the underlying stock exceeds the exercise price) that would have been received by the option holders had all option holders exercised. This amount changes based on changes in the market value of the Company's common stock.

Stock-based compensation expense related to stock options for the nine months ended December 31, 2011 and 2010 was approximately $11,000 and $73,000, respectively. As of December 31, 2011, there was approximately $5,000 of unrecognized compensation expense related to unvested stock options, which will be recognized over the remaining vesting periods of the underlying stock options through December 2014.

The fair value of each stock option granted is estimated on the date of grant using the Black-Scholes based stock option valuation model. The fair value of all awards is amortized on a straight-line basis over the requisite service periods, which are generally the vesting periods. The expected life of options granted represents the period of time that they are expected to be outstanding. The expected life is determined based on historical experience with similar options, giving consideration to the contractual terms and vesting schedules. Expected volatility was estimated at the date of grant based on the historical volatility of the Company's common stock. Expected dividends are based on dividend trends and the market value of the Company's common stock at the time of grant. The risk-free interest rate for periods within the contractual life of the options is based on the U.S. Treasury yield curve in effect at the time of the grant. During the nine months ended December 31, 2010, the Company granted 18,000 stock options. The weighted average fair value of stock options granted during the nine months ended December 31, 2010 was $0.83. There were no stock options granted for the nine months ended December 31, 2011.

The Black-Scholes model uses the assumptions listed in the following table:

| | Risk Free Interest Rate | Expected Life (years) | Expected Volatility | Expected Dividends |
|---|---|---|---|---|

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Fiscal 2011 | 2.47 | % | 6.25 | 44.98 | % | 2.73 | % |

4. EARNINGS PER SHARE

Basic earnings per share ("EPS") is computed by dividing net income or loss applicable to common stock by the weighted average number of common shares outstanding during the period, without considering any dilutive items. Diluted EPS is computed by dividing net income or loss applicable to common stock 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. Common stock equivalents arise from assumed conversion of outstanding stock options. Shares owned by the Company's Employee Stock Ownership Plan ("ESOP") that have not been allocated are not considered to be outstanding for the purpose of computing earnings per share. For the three and nine months ended December 31, 2011, stock options for 451,000 and 458,000 shares, respectively, of common stock were excluded in computing diluted EPS because they were antidilutive. For the three and nine months ended December 31, 2010, stock options for 465,000 and 466,000 shares, respectively, of common stock were excluded in computing diluted EPS because they were antidilutive.

| | Three Months Ended December 31, 2011 | Three Months Ended December 31, 2010 | Nine Months Ended December 31, 2011 | Nine Months Ended December 31, 2010 |
|---|---|---|---|---|
| Basic EPS computation: | | | | |
| Numerator-net income (loss) | $(16,595,000) | $579,000 | $(15,700,000) | $3,461,000 |
| Denominator-weighted average common shares outstanding | 22,321,011 | 22,296,378 | 22,314,876 | 17,044,751 |
| Basic EPS | $(0.74) | $0.03 | $(0.70) | $0.20 |
| Diluted EPS computation: | | | | |
| Numerator-net income (loss) | $(16,595,000) | $579,000 | $(15,700,000) | $3,461,000 |
| Denominator-weighted average common shares outstanding | 22,321,011 | 22,296,378 | 22,314,876 | 17,044,751 |
| Effect of dilutive stock options | - | 665 | - | - |
| Weighted average common shares and common stock equivalents | 22,321,011 | 22,297,043 | 22,314,876 | 17,044,751 |
| Diluted EPS | $(0.74) | $0.03 | $(0.70) | $0.20 |

## 5. INVESTMENT SECURITIES

The amortized cost and fair value of investment securities held to maturity consisted of the following (in thousands):

| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Estimated Fair Value |
|---|---|---|---|---|
| December 31, 2011 | | | | |
| Municipal bonds | $493 | $49 | $- | $542 |
| | | | | |
| March 31, 2011 | | | | |
| Municipal bonds | $506 | $50 | $- | $556 |

The contractual maturities of investment securities held to maturity are as follows (in thousands):

| December 31, 2011 | Amortized Cost | Estimated Fair Value |
|---|---|---|
| Due in one year or less | $- | $- |
| Due after one year through five years | - | - |
| Due after five years through ten years | 493 | 542 |
| Due after ten years | - | - |
| Total | $493 | $542 |

The amortized cost and fair value of investment securities available for sale consisted of the following (in thousands):

| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Estimated Fair Value |
|---|---|---|---|---|
| December 31, 2011 | | | | |
| Trust preferred | $2,974 | $- | $(1,786) | $1,188 |
| Agency securities | 5,000 | - | - | 5,000 |

| | | | | |
|---|---|---|---|---|
| Municipal bonds | 149 | - | - | 149 |
| Total | $8,123 | $- | $(1,786) | $6,337 |
| | | | | |
| March 31, 2011 | | | | |
| Trust preferred | $2,974 | $- | $(2,058) | $916 |
| Agency securities | 5,000 | - | (136) | 4,864 |
| Municipal bonds | 540 | - | - | 540 |
| Total | $8,514 | $- | $(2,194) | $6,320 |

The contractual maturities of investment securities available for sale are as follows (in thousands):

| December 31, 2011 | Amortized Cost | Estimated Fair Value |
|---|---|---|
| Due in one year or less | $- | $- |
| Due after one year through five years | 5,000 | 5,000 |
| Due after five years through ten years | - | - |
| Due after ten years | 3,123 | 1,337 |
| Total | $8,123 | $6,337 |

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The fair value of temporarily impaired securities, the amount of unrealized losses and the length of time these unrealized losses existed are as follows (in thousands):

| | Less than 12 months | | 12 months or longer | | Total | |
|---|---|---|---|---|---|---|
| | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses |
| December 31, 2011 | | | | | | |
| Trust preferred | $- | $- | $1,188 | $(1,786) | $1,188 | $(1,786) |
| March 31, 2011 | | | | | | |
| Trust preferred | $- | $- | $916 | $(2,058) | $916 | $(2,058) |
| Agency securities | 4,864 | (136) | - | - | 4,864 | (136) |
| Total | $4,864 | $(136) | $916 | $(2,058) | $5,780 | $(2,194) |

At December 31, 2011, the Company had a single collateralized debt obligation which is secured by trust preferred securities issued by 18 other financial institution holding companies, which we refer to as a pooled trust preferred security. The Company holds the mezzanine tranche of this security. Four of the issuers in this pool have defaulted (representing 40% of the remaining collateral), and seven others are currently in deferral (31% of the remaining collateral). The Company has estimated an expected default rate of 44% for the security. The expected default rate was estimated based primarily on an analysis of the financial condition of the underlying financial institution holding companies and their subsidiary banks. There was no excess subordination on this security.

During the three and nine months ended December 31, 2011, the Company determined that there was no additional other than temporary impairment ("OTTI") charge on the above pooled trust preferred security. The Company does not intend to sell this security and it is not more likely than not that the Company will be required to sell the security before the anticipated recovery of the remaining amortized cost basis.

To determine the component of gross OTTI related to credit losses, the Company compared the amortized cost basis of the OTTI security to the present value of the revised expected cash flows, discounted using the current pre-impairment yield. The revised expected cash flow estimates are based primarily on an analysis of default rates, prepayment speeds and third-party analytical reports. Significant judgment of management is required in this analysis that includes, but is not limited to, assumptions regarding the ultimate collectibility of principal and interest on the underlying collateral.

## 6. MORTGAGE-BACKED SECURITIES

Mortgage-backed securities held to maturity consisted of the following (in thousands):

| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Estimated Fair Value |
|---|---|---|---|---|
| December 31, 2011 | | | | |
| FHLMC mortgage-backed securities | $72 | $4 | $- | $76 |
| FNMA mortgage-backed securities | 105 | 1 | - | 106 |
| Total | $177 | $5 | $- | $182 |
| March 31, 2011 | | | | |

| | | | | |
|---|---|---|---|---|
| FHLMC mortgage-backed securities | $78 | $4 | $- | $82 |
| FNMA mortgage-backed securities | 112 | 5 | - | 117 |
| Total | $190 | $9 | $- | $199 |

The contractual maturities of mortgage-backed securities classified as held to maturity are as follows (in thousands):

| December 31, 2011 | Amortized Cost | Estimated Fair Value |
|---|---|---|
| Due in one year or less | $- | $- |
| Due after one year through five years | 4 | 4 |
| Due after five years through ten years | - | - |
| Due after ten years | 173 | 178 |
| Total | $177 | $182 |

Mortgage-backed securities held to maturity with an amortized cost of $71,000 and $76,000 and a fair value of $73,000 and $80,000 at December 31, 2011 and March 31, 2011, respectively, were pledged as collateral for governmental public funds held by the Bank. Mortgage-backed securities held to maturity with an amortized cost of $93,000 and $98,000 and a fair value of $96,000 and $103,000 at December 31, 2011 and March 31, 2011, respectively, were pledged as collateral for treasury tax and loan funds held by the Bank.

Mortgage-backed securities available for sale consisted of the following (in thousands):

| December 31, 2011 | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Estimated Fair Value |
|---|---|---|---|---|
| Real estate mortgage investment conduits | $343 | $11 | $- | $354 |
| FHLMC mortgage-backed securities | 754 | 27 | - | 781 |
| FNMA mortgage-backed securities | 10 | 1 | - | 11 |
| Total | $1,107 | $39 | $- | $1,146 |
| March 31, 2011 | | | | |
| Real estate mortgage investment conduits | $421 | $12 | $- | $433 |
| FHLMC mortgage-backed securities | 1,270 | 34 | - | 1,304 |
| FNMA mortgage-backed securities | 38 | 2 | - | 40 |
| Total | $1,729 | $48 | $- | $1,777 |

The contractual maturities of mortgage-backed securities available for sale are as follows (in thousands):

| December 31, 2011 | Amortized Cost | Estimated Fair Value |
|---|---|---|
| Due in one year or less | $- | $- |
| Due after one year through five years | 868 | 902 |
| Due after five years through ten years | - | - |
| Due after ten years | 239 | 244 |
| Total | $1,107 | $1,146 |

Mortgage-backed securities available for sale with an amortized cost of $861,000 and $178,000 and a fair value of $895,000 and $187,000 at December 31, 2011 and March 31, 2011, respectively, were pledged as collateral for government public funds held by the Bank. Mortgage-backed securities available for sale with an amortized cost of $71,000 and $128,000 and a fair value of $72,000 and $131,000 at December 31, 2011 and March 31, 2011, respectively, were pledged as collateral for treasury tax and loan funds held by the Bank.

## 7. LOANS RECEIVABLE

Loans receivable, excluding loans held for sale, consisted of the following (in thousands):

| | December 31, 2011 | March 31, 2011 |
|---|---|---|
| Commercial and construction | | |
| Commercial business | $86,759 | $85,511 |
| Other real estate mortgage (1) | 448,288 | 461,955 |
| Real estate construction | 27,544 | 27,385 |
| Total commercial and construction | 562,591 | 574,851 |
| | | |
| Consumer | | |
| Real estate one-to-four family | 129,780 | 110,437 |
| Other installment | 2,181 | 2,289 |
| Total consumer | 131,961 | 112,726 |
| | | |
| Total loans | 694,552 | 687,577 |

| | | |
|---|---|---|
| Less: Allowance for loan losses | 15,926 | 14,968 |
| Loans receivable, net | $678,626 | $672,609 |

(1) Other real estate mortgage consists of commercial real estate, land and multi-family loan portfolios

The Company's loan portfolio has very little exposure to sub-prime mortgage loans since the Company has not historically engaged in this type of lending.

Most of the Bank's business activity is with customers located in the states of Washington and Oregon. Loans and extensions of credit outstanding at one time to one borrower or a group of related borrowers are generally limited by federal regulation to 15% of the Bank's shareholders' equity, excluding accumulated other comprehensive loss. As of December 31, 2011 and March 31, 2011, the Bank had no loans to any one borrower in excess of the regulatory limit.

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8. ALLOWANCE FOR LOAN LOSSES

Allowance for loan loss: The allowance for loan losses is maintained at a level sufficient to provide for probable loan losses based on evaluating known and inherent risks in the loan portfolio. The allowance is provided based upon the Company's ongoing quarterly assessment of the pertinent factors underlying the quality of the loan portfolio. These factors include changes in the size and composition of the loan portfolio, delinquency levels, actual loan loss experience, current economic conditions and detailed analysis of individual loans for which full collectibility may not be assured. The detailed analysis includes techniques to estimate the fair value of loan collateral and the existence of potential alternative sources of repayment. The allowance consists of specific, general and unallocated components. The specific component relates to loans that are considered impaired. For loans that are classified as impaired, an allowance is established when the discounted cash flows, or collateral value or observable market price, of the impaired loan is lower than the carrying value of that loan. The general component covers non-impaired loans based on the Company's risk rating system and historical loss experience adjusted for qualitative factors. An unallocated component is maintained to cover uncertainties that the Company believes have resulted in losses that have not yet been allocated to specific elements of the general component. Such factors include uncertainties in economic conditions and in identifying triggering events that directly correlate to subsequent loss rates, changes in appraised value of underlying collateral, risk factors that have not yet manifested themselves in loss allocation factors and historical loss experience data that may not precisely correspond to the current portfolio or economic conditions. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general losses in the portfolio. The appropriate allowance level is estimated based upon factors and trends identified by the Company at the time the consolidated financial statements are prepared.

Commercial business, commercial real estate, multi-family, construction and land loans are considered to have a higher degree of credit risk than one-to-four family residential loans, and tend to be more vulnerable to adverse conditions in the real estate market and deteriorating economic conditions. While the Company believes the estimates and assumptions used in its determination of the allowance are reasonable, there can be no assurance that such estimates and assumptions will not be proven incorrect in the future, that the actual amount of future provisions will not exceed the amount of past provisions, or that any increased provisions that may be required will not adversely impact our financial condition and results of operations. In addition, bank regulators periodically review the Company's allowance for loan losses and may require the Company to increase its provision for loan losses or recognize additional loan charge-offs. An increase in the Company's allowance for loan losses or loan charge-offs as required by these regulatory authorities may have a material adverse effect on its financial condition and results of operations.

Loss factors are based on the Company's historical loss experience with additional consideration and adjustments made for changes in economic conditions, changes in the amount and composition of the loan portfolio, delinquency rates, changes in collateral values, seasoning of the loan portfolio, duration of current business cycle, a detailed analysis of impaired loans and other factors as deemed appropriate. These factors are evaluated on a quarterly basis. Loss rates used by the Company are affected as changes in these factors increase or decrease from quarter to quarter. The Company also considers Bank regulatory examination results, findings of its third-party independent credit reviewers and internal credit department analysis in its quarterly evaluation of the allowance for loan losses.

The following tables present a reconciliation of the allowance for loan losses (in thousands):

| Three months ended December 31, 2011 | Commercial Business | Commercial Real Estate | Land | Multi-Family | Real Estate Construction | Consumer | Unallocated | Total |
|---|---|---|---|---|---|---|---|---|

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Beginning balance | $ 1,675 | $ 4,432 | $2,486 | $1,785 | $ 1,060 | $1,577 | $ 1,657 | $14,672 |
| Provision for loan losses | 1,120 | (489 ) | 6,731 | 754 | (517 ) | 493 | 8 | 8,100 |
| Charge-offs | (692 ) | - | (4,302 ) | (1,505 ) | - | (385 ) | - | (6,884 ) |
| Recoveries | 5 | - | 33 | - | - | - | - | 38 |
| Ending balance | $ 2,108 | $ 3,943 | $4,948 | $1,034 | $ 543 | $1,685 | $ 1,665 | $15,926 |

| Nine months ended December 31, 2011 | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Beginning balance | $1,822 | $4,744 | $2,003 | $2,172 | $820 | $1,339 | $2,068 | $14,968 |
| Provision for loan losses | 1,775 | (694 ) | 9,093 | 1,226 | (277 ) | 1,130 | (403 ) | 11,850 |
| Charge-offs | (1,502 ) | (107 ) | (6,181 ) | (2,364 ) | - | (794 ) | - | (10,948 ) |
| Recoveries | 13 | - | 33 | - | - | 10 | - | 56 |
| Ending balance | $2,108 | $3,943 | $4,948 | $1,034 | $543 | $1,685 | $1,665 | $15,926 |

| | Three Months Ended December 31, 2010 | Nine Months Ended December 31, 2010 |
|---|---|---|
| Beginning balance | $ 19,029 | $ 21,642 |
| Provision for losses | 1,600 | 4,575 |
| Charge-offs | (3,170) | (8,778) |
| Recoveries | 4 | 24 |
| Ending balance | $ 17,463 | $ 17,463 |

| At December 31, 2010 | Commercial Business | Commercial Real Estate | Land | Multi-Family | Real Estate Construction | Consumer | Unallocated | Total |
|---|---|---|---|---|---|---|---|---|
| Ending balance | $ 2,188 | $ 4,954 | $2,675 | $2,091 | $ 2,041 | $ 1,539 | $ 1,975 | $17,463 |

The following tables present an analysis of loans receivable and allowance for loan losses, which were evaluated individually and collectively for impairment at the dates indicated (in thousands):

| | Allowance for loan losses | | | Recorded investment in loans | | |
|---|---|---|---|---|---|---|
| December 31, 2011 | Individually Evaluated for Impairment | Collectively Evaluated for Impairment | Total | Individually Evaluated for Impairment | Collectively Evaluated for Impairment | Total |
| Commercial business | $1,007 | $1,101 | $2,108 | $10,983 | $75,776 | $86,759 |
| Commercial real estate | 1,602 | 2,341 | 3,943 | 25,603 | 332,897 | 358,500 |
| Land | 2,958 | 1,990 | 4,948 | 22,403 | 23,099 | 45,502 |
| Multi-family | 511 | 523 | 1,034 | 8,708 | 35,578 | 44,286 |
| Real estate construction | 354 | 189 | 543 | 10,221 | 17,323 | 27,544 |
| Consumer | 184 | 1,501 | 1,685 | 2,449 | 129,512 | 131,961 |
| Unallocated | - | 1,665 | 1,665 | - | - | - |
| Total | $6,616 | $9,310 | $15,926 | $80,367 | $614,185 | $694,552 |
| March 31, 2011 | | | | | | |
| Commercial business | $207 | $1,615 | $1,822 | $3,382 | $82,129 | $85,511 |
| Commercial real estate | 59 | 4,685 | 4,744 | 8,976 | 355,712 | 364,688 |
| Land | - | 2,003 | 2,003 | 2,695 | 52,563 | 55,258 |
| Multi-family | 1,779 | 393 | 2,172 | 8,000 | 34,009 | 42,009 |
| Real estate construction | - | 820 | 820 | 4,206 | 23,179 | 27,385 |
| Consumer | - | 1,339 | 1,339 | - | 112,726 | 112,726 |
| Unallocated | - | 2,068 | 2,068 | - | - | - |
| Total | $2,045 | $12,923 | $14,968 | $27,259 | $660,318 | $687,577 |

Non-accrual loans: Loans are reviewed regularly and it is the Company's general policy that a loan is past due when it is 30 days to 89 days delinquent. In general, when a loan is 90 days delinquent or when collection of principal or interest appears doubtful, it is placed on non-accrual status, at which time the accrual of interest ceases and a reserve for unrecoverable accrued interest is established and charged against operations. Payments received on non-accrual loans are applied to reduce the outstanding principal balance on a cash-basis method. As a general practice, a loan is not removed from non-accrual status until all delinquent principal, interest and late fees have been brought current and the borrower has demonstrated a history of performance based upon the contractual terms of the note. Interest income foregone on non-accrual loans was $1.6 million and $1.7 million during the nine months ended December 31, 2011 and 2010, respectively.

The following tables present an analysis of past due loans at the dates indicated (in thousands):

| December 31, 2011 | 30-89 Days Past Due | 90 Days and Greater (Non-Accrual) | Total Past Due | Current | Total Loans Receivable | Recorded Investment Over 90 Days and Accruing |
|---|---|---|---|---|---|---|
| Commercial business | $2,539 | $2,998 | $5,537 | $81,222 | $86,759 | $- |
| Commercial real estate | 9,296 | 8,931 | 18,227 | 340,273 | 358,500 | - |
| Land | 5,599 | 14,503 | 20,102 | 25,400 | 45,502 | - |
| Multi-family | 442 | 598 | 1,040 | 43,246 | 44,286 | - |
| Real estate construction | 6,734 | 3,429 | 10,163 | 17,381 | 27,544 | - |
| Consumer | 3,631 | 1,578 | 5,209 | 126,752 | 131,961 | - |
| Total | $28,241 | $32,037 | $60,278 | $634,274 | $694,552 | $- |

| March 31, 2011 | 30-89 Days Past Due | 90 Days and Greater (Non-Accrual) | Total Past Due | Current | Total Loans Receivable | Recorded Investment Over 90 Days and Accruing |
|---|---|---|---|---|---|---|
| Commercial business | $1,415 | $2,871 | $4,286 | $81,225 | $85,511 | $- |
| Commercial real estate | 2,112 | 1,385 | 3,497 | 361,191 | 364,688 | - |
| Land | - | 2,904 | 2,904 | 52,354 | 55,258 | - |
| Multi-family | - | - | - | 42,009 | 42,009 | - |
| Real estate construction | - | 4,206 | 4,206 | 23,179 | 27,385 | - |
| Consumer | 4,271 | 957 | 5,228 | 107,498 | | |