

PRUDENTIAL BANCORP, INC.  
Form 10-Q  
August 09, 2016

**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, DC 20549**

**FORM 10-Q**

**(Mark One)**

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

**For the quarterly period ended June 30, 2016**

**OR**

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

**For the transition period from \_\_\_\_\_ to \_\_\_\_\_**

**Commission file number: 000-55084**

**Prudential Bancorp, Inc.**

(Exact Name of Registrant as Specified in Its Charter)

**Pennsylvania**  
(State or Other Jurisdiction of Incorporation or Organization)

**46-2935427**  
(I.R.S. Employer Identification No.)

**1834 West Oregon Avenue**

**19145**  
Zip Code

**Philadelphia, Pennsylvania**  
(Address of Principal Executive Offices)

**(215) 755-1500**

(Registrant's Telephone Number, Including Area Code)

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

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  No

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

Large accelerated filer

Accelerated filer

Non-accelerated filer  (Do not check if a smaller reporting company)

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock as of the latest practical date: as of July 31, 2016, 9,544,809 shares were issued and 8,045,544 were outstanding.

**PRUDENTIAL BANCORP, INC. AND SUBSIDIARIES**

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**PRUDENTIAL BANCORP, INC. AND SUBSIDIARIES****UNAUDITED CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION**

	June 30, 2016	September 30, 2015
	(Dollars in Thousands)	
<b>ASSETS</b>		
Cash and amounts due from depository institutions	\$ 2,180	\$ 2,150
Interest-bearing deposits	36,392	9,122
Total cash and cash equivalents	38,572	11,272
Investment and mortgage-backed securities available for sale (amortized cost— June 30, 2016, \$136,913; September 30, 2015, \$77,456)	138,683	77,483
Investment and mortgage-backed securities held to maturity (fair value— June 30, 2016, \$16,793; September 30, 2015, \$66,877)	15,488	66,384
Loans receivable—net of allowance for loan losses (June 30, 2016, \$3,269; September 30, 2015, \$2,930)	342,459	312,633
Accrued interest receivable	1,763	1,665
Real estate owned	207	869
Federal Home Loan Bank stock—at cost	2,387	369
Office properties and equipment—net	1,419	1,492
Bank owned life insurance	12,973	12,722
Prepaid expenses and other assets	1,863	1,325
Deferred tax assets-net	476	975
<b>TOTAL ASSETS</b>	<b>\$ 556,290</b>	<b>\$ 487,189</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>LIABILITIES:</b>		
<b>Deposits:</b>		
Noninterest-bearing	\$ 2,832	\$ 2,293
Interest-bearing	383,808	362,781
Total deposits	386,640	365,074
Advances from Federal Home Loan Bank	50,227	-
Accrued interest payable	1,015	1,291
Advances from borrowers for taxes and insurance	2,769	1,670
Accounts payable and accrued expenses	2,573	2,153

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Total liabilities	443,224	370,188
STOCKHOLDERS' EQUITY:		
Preferred stock, \$.01 par value, 10,000,000 shares authorized, none issued	-	-
Common stock, \$.01 par value, 40,000,000 shares authorized; 9,544,809 issued and 8,060,799 outstanding at June 30, 2016 and 9,544,809 issued and 8,449,625 outstanding at September 30, 2015	95	95
Additional paid-in capital	95,433	95,286
Unearned Employee Stock Ownership Plan shares	(4,644 )	(4,926 )
Treasury stock, at cost: 1,499,265 shares at June 30, 2016 and 1,095,184 at September 30, 2015	(21,013 )	(14,691 )
Retained earnings	42,263	41,219
Accumulated other comprehensive income	932	18
Total stockholders' equity	113,066	117,001
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 556,290	\$ 487,189

See notes to unaudited consolidated financial statements.

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## UNAUDITED CONSOLIDATED STATEMENTS OF OPERATIONS

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2016	2015	2016	2015
	(Dollars in Thousands, Except Per Share Data)			
<b>INTEREST INCOME:</b>				
Interest on loans	\$ 3,263	\$ 3,085	\$ 9,489	\$ 9,629
Interest on mortgage-backed securities	673	465	1,868	1,331
Interest and dividends on investments	529	487	1,517	1,587
Interest on interest-bearing assets	9	18	22	52
Total interest income	4,474	4,055	12,896	12,599
<b>INTEREST EXPENSE:</b>				
Interest on deposits	682	851	2,177	2,623
Interest on advances from Federal Home Loan Bank	142	-	296	-
Total interest expense	824	851	2,473	2,623
NET INTEREST INCOME	3,650	3,204	10,423	9,976
PROVISION FOR LOAN LOSSES	150	210	225	585
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	3,500	2,994	10,198	9,391
<b>NON-INTEREST INCOME:</b>				
Fees and other service charges	142	87	371	283
Gain on sale of loans, net	-	-	2	138
Gain on the sale of office properties	-	231	-	2,024
Gain on sale of investment securities (AFS)	161	-	161	-
Income from bank owned life insurance	83	84	251	261
Other	14	43	98	77
Total non-interest income	400	445	883	2,783
<b>NON-INTEREST EXPENSE:</b>				
Salaries and employee benefits	1,684	2,157	5,071	5,997

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Data processing	112	97	340	309
Professional services	230	303	750	923
Office occupancy	246	279	753	769
Director compensation	123	107	351	275
Deposit insurance	134	95	306	231
Advertising	17	37	55	140
Other	269	357	881	1,225
Total non-interest expense	2,815	3,432	8,507	9,869
INCOME BEFORE INCOME TAXES	1,085	7	2,574	2,305
INCOME TAXES:				
Current expense	308	(46 )	807	279
Deferred expense (benefit)	-	6	29	(193 )
Total income tax expense (benefit)	308	(40 )	836	86
NET INCOME	\$ 777	\$ 47	\$ 1,738	\$ 2,219
BASIC EARNINGS PER SHARE	\$ 0.10	\$ 0.01	\$ 0.23	\$ 0.26
DILUTED EARNINGS PER SHARE	\$ 0.10	\$ 0.01	\$ 0.23	\$ 0.26
DIVIDENDS PER SHARE	\$ 0.03	\$ 0.18	\$ 0.09	\$ 0.24

See notes to unaudited consolidated financial statements.



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## UNAUDITED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

	Three months ended June 30,		Nine months ended June 30,	
	2016 (Dollars in Thousands)	2015 (Dollars in Thousands)	2016 (Dollars in Thousands)	2015 (Dollars in Thousands)
Net income	\$ 777	\$ 47	\$ 1,738	\$ 2,219
Unrealized holding gains (losses) on available-for-sale securities	744	(1,145 )	1,897	452
Tax effect	(257 )	389	(645 )	(154 )
Reclassification adjustment for net gain on sale of securities realized in net income	(161 )	-	(161 )	-
Tax effect	55	-	55	-
Unrealized holding loss on interest rate swaps	(351 )	-	(351 )	-
Tax effect	119	-	119	-
Total other comprehensive income (loss)	149	(756 )	914	298
Comprehensive Income (loss)	\$ 926	\$ (709 )	\$ 2,652	\$ 2,517

See notes to unaudited consolidated financial statements.

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## UNAUDITED CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

	Common Stock	Additional Paid-In Capital	Unearned ESOP Shares	Treasury Stock	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity
(Dollars in Thousands, Except Per Share Data)							
BALANCE, OCTOBER 1, 2015	\$95	\$95,286	\$(4,926 )	\$(14,691)	\$41,219	\$ 18	\$ 117,001
Net income					1,738		1,738
Other comprehensive income						914	914
Dividends paid (\$0.09 per share)					(694 )		(694 )
Excess tax benefit from stock compensation plans		156					156
Issuance of treasury stock (74,665 shares)				862			862
Purchase of treasury stock (520,546 shares)				(7,824 )			(7,824 )
Treasury stock used for Recognition and Retention Plan (41,800 shares issued)		(640 )		640			-
Stock option expense		278					278
Recognition and Retention Plan expense		251					251
ESOP shares committed to be released (26,649 shares)		102	282				384
BALANCE, JUNE 30, 2016	\$95	\$95,433	\$(4,644 )	\$(21,013)	\$42,263	\$ 932	\$ 113,066

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	Additional Paid-In Stock Capital	Unearned ESOP Shares	Treasury Stock	Retained Earnings	Accumulated Other Comprehensive (Loss) Income	Total Stockholders' Equity
(Dollars in Thousands, Except Per Share Data)						
BALANCE, OCTOBER 1, 2014	\$95	\$94,397	\$ (5,302 )	\$ -	\$41,188	\$ (953 ) \$ 129,425
Net income				2,219		2,219
Other comprehensive income					298	298
Dividends paid (\$0.24 per share)				(2,111 )		(2,111 )
Excess tax benefit from stock compensation plans	118					118
Purchase of treasury stock (694,871 shares)			(8,853 )			(8,853 )
Stock option expense	241					241
Recognition and Retention Plan expense	173					173
ESOP shares committed to be released (26,638 shares)	201	282				483
BALANCE, JUNE 30, 2015	\$95	\$95,130	\$ (5,020 )	\$ (8,853 )	\$41,296	\$ (655 ) \$ 121,993

See notes to unaudited consolidated financial statements.

## PRUDENTIAL BANCORP, INC. AND SUBSIDIARIES

## UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS

	Nine Months Ended June 30,	
	2016	2015
	(Dollars in Thousands)	
<b>OPERATING ACTIVITIES:</b>		
Net income	\$ 1,738	\$ 2,219
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation	242	239
Net amortization (accretion) of premiums/discounts	11	(192 )
Provision for loan losses	225	585
Net amortization of deferred loan fees and costs	172	187
Share-based compensation expense for stock options and awards	529	414
Income from bank owned life insurance	(251 )	(261 )
Gain from sale of loans	(2 )	(138 )
Gain on sale of office properties	-	(2,024 )
Gain on sale of other real estate owned	(58 )	-
Gain on sale of investments	(161 )	-
Originations of loans held for sale	(450 )	(2,400 )
Proceeds from sale of loans held for sale	452	2,538
Compensation expense of ESOP	384	483
Deferred income tax expense (benefit)	29	(193 )
Changes in assets and liabilities which used cash:		
Accrued interest receivable	(98 )	32
Prepaid expenses and other assets	(898 )	532
Accrued interest payable	(276 )	(547 )
Accounts payable and accrued expenses	420	(41 )
Net cash provided by operating activities	2,008	1,433
<b>INVESTING ACTIVITIES:</b>		
Purchase of investment and mortgage-backed securities available for sale	(67,815 )	-
Purchase of corporate bonds available for sale	(20,466 )	(22,837 )
Loans originated or acquired	(59,918 )	(53,139 )
Principal collected on loans	29,488	55,943
Principal payments received on investment and mortgage-backed securities:		
Held-to-maturity	50,962	10,875
Available-for-sale	3,748	4,268
Proceeds from sale of investments and mortgage-backed securities AFS	25,161	-
Proceeds from redemption of FHLB stock	-	852
Purchase of FHLB stock	(2,018 )	-
Proceeds from sale of real estate owned	927	360

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Proceeds from sale of office properties	-	2,114
Purchases of equipment	(169 )	(400 )
Net cash used in investing activities	(40,100 )	(1,964 )
<b>FINANCING ACTIVITIES:</b>		
Net decrease in demand deposits, NOW accounts, and savings accounts	(4,411 )	(5,738 )
Net increase (decrease) in certificates of deposit	25,977	(9,184 )
Proceeds from FHLB advances	51,999	-
Repayment of FHLB advances	(1,772 )	(340 )
Increase in advances from borrowers for taxes and insurance	1,099	1,562
Cash dividends paid	(694 )	(2,111 )
Issuance of treasury stock	1,502	-
Purchase of treasury stock	(8,464 )	(8,853 )
Excess tax benefit related to stock compensation plans	156	118
Net cash provided by (used in) financing activities	65,392	(24,546 )
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	<b>27,300</b>	<b>(25,077 )</b>
<b>CASH AND CASH EQUIVALENTS—Beginning of period</b>	<b>11,272</b>	<b>45,382</b>
<b>CASH AND CASH EQUIVALENTS—End of period</b>	<b>\$ 38,572</b>	<b>\$ 20,305</b>
<b>SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:</b>		
Interest paid on deposits and advances from Federal Home Loan Bank	\$ 2,749	\$ 3,170
Income taxes paid	\$ 450	\$ 475
<b>SUPPLEMENTAL DISCLOSURE OF NONCASH ITEMS:</b>		
Real estate acquired in settlement of loans	\$ 207	\$ -

See notes to unaudited consolidated financial statements.

PRUDENTIAL BANCORP, INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

1. SIGNIFICANT ACCOUNTING POLICIES

Prudential Bancorp, Inc. (the “Company”) is a Pennsylvania corporation and the parent holding company for Prudential Saving Bank (the “Bank”). The Company is a registered bank holding company.

The Bank is a community-oriented Pennsylvania-chartered savings bank headquartered in South Philadelphia. The banking office network currently consists of the headquarters and main office and five full-service branch offices. Five of the banking offices are located in Philadelphia (Philadelphia County), and one is in Drexel Hill, Delaware County, Pennsylvania. The Bank maintains ATMs at all six of the banking offices. The Bank also provides on-line and mobile banking services.

The Bank is subject to regulation by the Pennsylvania Department of Banking and Securities (the “Department”), as its chartering authority and primary regulator, and by the Federal Deposit Insurance Corporation (the “FDIC”), which insures the Bank’s deposits up to applicable limits. As a bank holding company, Prudential is subject to the regulation of the Board of Governors of the Federal Reserve System.

On June 2, 2016, the Company announced the entering into of a definitive merger agreement with Polonia Bancorp, Inc. (“Polonia”); pending receipt of the necessary shareholder and regulatory approvals, Polonia will merge with and into the Company, and Polonia Bank, Polonia’s wholly owned subsidiary, will merge with and into the Bank.

**Basis of presentation** – The accompanying unaudited consolidated financial statements were prepared pursuant to the rules and regulations of the U. S. Securities and Exchange Commission (“SEC”) for interim information and therefore do not include all the information or footnotes necessary for a complete presentation of financial condition, results of operations, comprehensive income, changes in equity and cash flows in conformity with accounting principles generally accepted in the United States of America (“GAAP”). However, all normal recurring adjustments that, in the opinion of management, are necessary for a fair presentation of the financial statements have been included. The results for the three and nine months ended June 30, 2016 are not necessarily indicative of the results that may be expected for the fiscal year ending September 30, 2016, or any other period. These financial statements should be read in conjunction with the audited consolidated financial statements of the Company and the accompanying notes thereto

included in the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2015.

***Use of Estimates in the Preparation of Financial Statements***—The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of income and expenses during the reporting period. The most significant estimates and assumptions in the Company's consolidated financial statements are recorded in the allowance for loan losses, deferred income taxes, other-than-temporary impairment, and the fair value measurement for financial instruments. Actual results could differ from those estimates.

***Share-Based Compensation*** – The Company accounts for stock-based compensation issued to employees, and where appropriate, non-employees, at fair value. Under fair value provisions, stock-based compensation cost is measured at the grant date based on the fair value of the award and is recognized as expense over the appropriate vesting period using the straight-line method. The amount of stock-based compensation recognized at any date must at least equal the portion of the grant date fair value of the award that is vested at that date and as a result it may be necessary to recognize the expense using a ratable method. Determining the fair value of stock-based awards at the date of grant requires judgment, including estimating the expected term of the stock options and the expected volatility of the Company's stock. In addition, judgment is required in estimating the amount of stock-based awards that are expected to be forfeited. If actual results differ significantly from these estimates or different key assumptions were used, it could have a material effect on the Company's consolidated financial statements.

Dividends with respect to non-vested share awards granted pursuant to the Company's 2008 Recognition and Retention Plan ("Plan") and held in the Trust (the "Trust") are held for the benefit of the recipients and are paid out proportionately by the Trust to the recipients of stock awards granted pursuant to the Plan as soon as practicable after the stock awards are earned. A recipient of a share award granted under the 2014 Stock Incentive Plan is not entitled to receive any dividends declared on the common stock subject to the award until earned.

**Treasury Stock** – Stock held in treasury by the Company is accounted for using the cost method, which treats stock held in treasury as a reduction to total stockholders' equity. During the nine month period ended June 30, 2016, the Company repurchased 520,546 shares at an approximate total cost of \$7.8 million and issued 74,665 shares for approximately cash received of \$862,000. In addition, the Company purchased 41,800 shares at an aggregate cost of \$640,000 out of treasury for the benefit of the Company's 2014 Stock Incentive Plan to fund the issuance of vesting restricted stock awards.

**FHLB Stock** – FHLB stock is classified as a restricted equity security because ownership is restricted and there is not an established market for its resale. FHLB stock is carried at cost and is evaluated for impairment when certain conditions warrant further consideration. Management concluded that the FHLB stock was not impaired at June 30, 2016.

### ***Recent Accounting Pronouncements***

In January 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU" or "Update") 2014-01, *Investments – Equity Method and Joint Ventures (Topic 323)*: Accounting for Investments in Qualified Affordable Housing Projects. The amendments in this Update permit reporting entities to make an accounting policy election to account for their investments in qualified affordable housing projects using the proportional amortization method if certain conditions are met. Under the proportional amortization method, an entity amortizes the initial cost of the investment in proportion to the tax credits and other tax benefits received and recognize the net investment performance in the income statement as a component of income tax expense (benefit). The amendments in this Update should be applied retrospectively to all periods presented. A reporting entity that uses the effective yield method to account for its investments in qualified affordable housing projects before the date of adoption may continue to apply the effective yield method for those preexisting investments. The amendments in this Update became effective for public business entities for annual periods and interim reporting periods within those annual periods, beginning after December 15, 2014. Early adoption is permitted. This ASU did not have a significant impact on the Company's financial statements.

In January 2014, the FASB issued ASU 2014-04, *Receivables – Troubled Debt Restructurings by Creditors (Subtopic 310-40)*: Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure. The amendments in this Update clarify that an in-substance repossession or foreclosure occurs, and a creditor is considered



to have received physical possession of residential real estate property collateralizing a consumer mortgage loan, upon either (1) the creditor obtaining legal title to the residential real estate property upon completion of a foreclosure or (2) the borrower conveying all interest in the residential real estate property to the creditor to satisfy that loan through completion of a deed in lieu of foreclosure or through a similar legal agreement. Additionally, the amendments require interim and annual disclosure of both (1) the amount of foreclosed residential real estate property held by the creditor and (2) the recorded investment in consumer mortgage loans collateralized by residential real estate property that are in the process of foreclosure according to requirements of the applicable jurisdiction. The amendments in this Update were effective for public business entities for annual periods, and interim periods within those annual periods, beginning after December 15, 2014. An entity can elect to adopt the amendments in this Update using either a modified retrospective transition method or a prospective transition method. This ASU did not have a significant impact on the Company's financial statements.

In May 2014, the FASB issued ASU 2014-09, *Revenue from Contracts with Customers (a new revenue recognition standard)*. The Update's core principle is that a company will recognize revenue to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In addition, this update specifies the accounting for certain costs to obtain or fulfill a contract with a customer and expands disclosure requirements for revenue recognition. This Update is effective, as a result of ASU 2015-14, for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. This ASU is not expected to have a significant impact on the Company's financial statements.

In June 2014, the FASB issued ASU 2014-12, *Compensation-Stock Compensation (Topic 718): Accounting for Share-Based Payments when the Terms of an Award Provide that a Performance Target Could Be Achieved After the Requisite Service Period*. The amendments require that a performance target that affects vesting and that could be achieved after the requisite service period be treated as a performance condition. The amendments in this Update are effective for annual periods and interim periods within those annual periods beginning after December 15, 2015. Earlier adoption is permitted. Entities may apply the amendments in this Update either (a) prospectively to all awards granted or modified after the effective date or (b) retrospectively to all awards with performance targets that are outstanding as of the beginning of the earliest annual period presented in the financial statements and to all new or modified awards thereafter. If retrospective transition is adopted, the cumulative effect of applying this Update as of the beginning of the earliest annual period presented in the financial statements should be recognized as an adjustment to the opening retained earnings balance at that date. Additionally, if retrospective transition is adopted, an entity may use hindsight in measuring and recognizing the compensation cost. This ASU is not expected to have a significant impact on the Company's financial statements.

In August 2014, the FASB issued ASU 2014-15, *Presentation of Financial Statements – Going Concern (Subtopic 205-40)*. The amendments in this Update provide guidance in accounting principles generally accepted in the United States of America about management's responsibility to evaluate whether there is substantial doubt about an entity's ability to continue as a going concern and to provide related footnote disclosures. The amendments in this Update are effective for the annual period ending after December 15, 2016, and for annual periods and interim periods thereafter. Early application is permitted. This ASU is not expected to have a significant impact on the Company's financial statements.

In November 2014, the FASB issued ASU 2014-16, *Derivatives and Hedging (Topic 815): Determining Whether the Host Contract in a Hybrid Financial Instrument Issued in the Form of a Share Is More Akin to Debt or to Equity (a consensus of the FASB Emerging Issues Task Force)*. This ASU clarifies how current U.S. GAAP should be interpreted in subjectively evaluating the economic characteristics and risks of a host contract in a hybrid financial instrument that is issued in the form of a share. Public business entities are required to implement the new requirements in fiscal years and interim periods within those fiscal years beginning after December 15, 2015. This ASU is not expected to have a significant impact on the Company's financial statements.

In November 2014, the FASB issued ASU 2014-17, *Business Combinations (Topic 805): Pushdown Accounting*. The amendments in this Update apply to the separate financial statements of an acquired entity and its subsidiaries that are a business or nonprofit activity (either public or nonpublic) upon the occurrence of an event in which an acquirer (an individual or an entity) obtains control of the acquired entity. An acquired entity may elect the option to apply pushdown accounting in the reporting period in which the change-in-control event occurs. If pushdown accounting is not applied in the reporting period in which the change-in-control event occurs, an acquired entity will have the option to elect to apply pushdown accounting in a subsequent reporting period to the acquired entity's most recent change-in-control event. The amendments in this Update were effective on November 18, 2014. After the effective date, an acquired entity was permitted to make an election to apply the guidance to future change-in-control events or to its most recent change-in-control event. This ASU did not have a significant impact on the Company's financial statements.

In January 2015, the FASB issued ASU 2015-01, *Income Statement –Extraordinary and Unusual Items*, as part of its initiative to reduce complexity in accounting standards. This Update eliminates from GAAP the concept of extraordinary items. The amendments in this Update are effective for annual periods, and interim periods within those annual periods, beginning after December 15, 2015. A reporting entity may apply the amendments prospectively. A reporting entity also may apply the amendments retrospectively to all prior periods presented in the financial statements. Early adoption is permitted provided that the guidance is applied from the beginning of the fiscal year of adoption. This ASU is not expected to have a significant impact on the Company’s financial statements.

In February 2015, the FASB issued ASU 2015-02, *Consolidation (Topic 810)*. The amendments in this Update affect reporting entities that are required to evaluate whether they should consolidate certain legal entities. All legal entities are subject to reevaluation under the revised consolidation model. Specifically, the amendments (1) modify the evaluation of whether limited partnerships and similar legal entities are variable interest entities (“VIEs”) or voting interest entities; (2) eliminate the presumption that a general partner should consolidate a limited partnership; (3) affect the consolidation analysis of reporting entities that are involved with VIEs, particularly those that have fee arrangements and related party relationships; and (4) provide a scope exception from consolidation guidance for reporting entities with interests in legal entities that are required to comply with or operate in accordance with requirements that are similar to those in Rule 2a-7 of the Investment Company Act of 1940 for registered money market funds. The amendments in this Update are effective for public business entities for fiscal years, and for interim periods within those fiscal years, beginning after December 15, 2015. For all other entities, the amendments in this Update are effective for fiscal years beginning after December 15, 2016, and for interim periods within fiscal years beginning after December 15, 2017. This ASU is not expected to have a significant impact on the Company’s financial statements.

In April 2015, the FASB issued ASU 2015-03, *Interest-Imputation of Interest (Subtopic 835-30)*, as part of its initiative to reduce complexity in accounting standards. To simplify presentation of debt issuance costs, the amendments in this Update require that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The recognition and measurement guidance for debt issuance costs are not affected by the amendments in this Update. For public business entities, the amendments in this Update are effective for financial statements issued for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years. For all other entities, the amendments in this Update are effective for financial statements issued for fiscal years beginning after December 15, 2015, and interim periods within fiscal years beginning after December 15, 2016. An entity should apply the new guidance on a retrospective basis, wherein the balance sheet of each individual period presented should be adjusted to reflect the period-specific effects of applying the new guidance. This ASU is not expected to have a significant impact on the Company’s financial statements.

In April 2015, the FASB issued ASU 2015-04, *Compensation – Retirement Benefits (Topic 715)*, as part of its initiative to reduce complexity in accounting standards. For an entity with a fiscal year-end that does not coincide with a month-end, the amendments in this Update provide a practical expedient that permits the entity to measure defined benefit plan assets and obligations using the month-end that is closest to the entity’s fiscal year-end and apply that practical expedient consistently from year to year. The practical expedient should be applied consistently to all plans if

an entity has more than one plan. The amendments in this Update are effective for public business entities for financial statements issued for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years. For all other entities, the amendments in this Update are effective for financial statements issued for fiscal years beginning after December 15, 2016, and interim periods within fiscal years beginning after December 15, 2017. Earlier application is permitted. This ASU is not expected to have a significant impact on the Company's financial statements.

In April 2015, the FASB issued ASU 2015-05, *Intangibles – Goodwill and Other – Internal-Use Software (Subtopic 350-40)*, as part of its initiative to reduce complexity in accounting standards. This guidance will help entities evaluate the accounting for fees paid by a customer in a cloud computing arrangement. The amendments in this Update provide guidance to customers about whether a cloud computing arrangement includes a software license. If a cloud computing arrangement includes a software license, then the customer should account for the software license element of the arrangement consistent with the acquisition of other software licenses. If a cloud computing arrangement does not include a software license, the customer should account for the arrangement as a service contract. For public business entities, the FASB decided that the amendments will be effective for annual periods, including interim periods within those annual periods, beginning after December 15, 2015. For all other entities, the amendments will be effective for annual periods beginning after December 15, 2015, and interim periods in annual periods beginning after December 15, 2016. Early adoption is permitted for all entities. This ASU is not expected to have a significant impact on the Company's financial statements.

In May 2015, the FASB issued ASU 2015-08, *Business Combinations - Pushdown Accounting - Amendment to SEC Paragraphs Pursuant to Staff Accounting Bulletin No. 115*. This ASU was issued to amend various SEC paragraphs pursuant to the issuance of Staff Accounting Bulletin No. 115 which deleted certain topics related to push down accounting in order to make the SEC's interpretive guidance consistent with current accounting and audit guidance. This ASU did not have a significant impact on the Company's financial statements.

In August 2015, the FASB issued ASU 2015-14, *Revenue from Contract with Customers (Topic 606)*. The amendments in this Update defer the effective date of ASU 2014-09 for all entities by one year. Public business entities, certain not-for-profit entities, and certain employee benefit plans should apply the guidance in ASU 2014-09 to annual reporting periods beginning after December 15, 2017, including interim reporting periods within that reporting period. All other entities should apply the guidance in ASU 2014-09 to annual reporting periods beginning after December 15, 2018, and interim reporting periods within annual reporting periods beginning after December 15, 2019. The Company is evaluating the effect of adopting this new accounting ASU.

In September 2015, the FASB issued ASU 2015-16, *Business Combinations (Topic 805)*. The amendments in this Update require that an acquirer recognizes adjustments to provisional amounts that are identified during the measurement period in the reporting period in which the adjustment amounts are determined. The amendments in this Update require that the acquirer record, in the same period's financial statements, the effect on earnings of changes in depreciation, amortization, or other income effects, if any, as a result of the change to the provisional amounts, calculated as if the accounting had been completed at the acquisition date. The amendments in this Update require an entity to present separately on the face of the income statement or disclose in the notes the portion of the amount recorded in current-period earnings by line item that would have been recorded in previous reporting periods if the adjustment to the provisional amounts had been recognized as of the acquisition date. For public business entities, the amendments in this Update are effective for fiscal years beginning after December 15, 2015, including interim periods within those fiscal years. For all other entities, the amendments in this Update are effective for fiscal years beginning after December 15, 2016, and interim periods within fiscal years beginning after December 15, 2017. This ASU is not expected to have a significant impact on the Company's financial statements.

In January 2016, the FASB issued ASU 2016-01, *Financial Instruments – Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*. This Update applies to all entities that hold financial assets or owe financial liabilities and is intended to provide more useful information on the recognition, measurement, presentation, and disclosure of financial instruments. Among other things, this Update (a) requires equity investments (except those accounted for under the equity method of accounting or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income; (b) simplifies the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify impairment; (c) eliminates the requirement to disclose the fair value of financial instruments measured at amortized cost for entities that are not public business entities; (d) eliminates the requirement for public business entities to disclose the method(s) and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost on the balance sheet; (e) requires public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes; (f) requires an entity to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to measure the liability at fair value in accordance with the fair value option for financial instruments; (g) requires separate presentation of financial assets and financial liabilities by measurement category and form of financial asset (that is, securities or loans and receivables) on the balance sheet or the accompanying notes to the financial statements; and (h) clarifies that an entity should evaluate the need for a valuation allowance on a deferred tax asset related to available-for-sale securities in combination with the entity's other deferred tax assets. For public business entities, the amendments in this Update are effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. For all other entities including not-for-profit entities and employee benefit plans within the scope of Topics 960 through 965 on plan accounting, the amendments in this Update are effective for fiscal years beginning after December 15, 2018, and interim periods within fiscal years beginning after December 15, 2019. All entities that are not public business entities may adopt the amendments in this Update earlier as of the fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. The Company is currently evaluating the impact the adoption of the standard will have on the Company's financial position or results of operations.

In February 2016, the FASB issued ASU 2016-02, *Leases (Topic 842)*. The standard requires lessees to recognize the assets and liabilities that arise from leases on the balance sheet. A lessee should recognize in the statement of financial position a liability to make lease payments (the lease liability) and a right-of-use asset representing its right to use the underlying asset for the lease term. A short-term lease is defined as one in which: (a) the lease term is 12 months or less, and (b) there is not an option to purchase the underlying asset that the lessee is reasonably certain to exercise. For short-term leases, lessees may elect to recognize lease payments over the lease term on a straight-line basis. For public business entities, the amendments in this Update are effective for fiscal years beginning after December 15, 2018, and interim periods within those years. For all other entities, the amendments in this Update are effective for fiscal years beginning after December 15, 2019, and for interim periods within fiscal years beginning after December 15, 2020. The amendments should be applied at the beginning of the earliest period presented using a modified retrospective approach with earlier application permitted as of the beginning of an interim or annual reporting period. The Company is currently evaluating the impact of the adoption of the standard will have on the Company's financial position or results of operations.

In March 2016, the FASB issued ASU 2016-04, *Liabilities – Extinguishments of Liabilities (Subtopic 405-20)*. The standard provides that liabilities related to the sale of prepaid stored-value products within the scope of this Update are financial liabilities. The amendments in the Update provide a narrow scope exception to the guidance in Subtopic 405-20 to require that breakage for those liabilities be accounted for consistent with the breakage guidance in Topic 606. The amendments in this Update are effective for public business entities, certain not-for-profit entities, and certain employee benefit plans for financial statements issued for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. For all other entities, the amendments are effective for financial statements issued for fiscal years beginning after December 15, 2018, and interim periods within fiscal years beginning after December 15, 2019. Earlier application is permitted, including adoption in an interim period. This ASU is not expected to have a significant impact on the Company's financial statements.

In March 2016, the FASB issued ASU 2016-05, *Derivatives and Hedging (Topic 815)*. The amendments in this Update apply to all reporting entities for which there is a change in the counterparty to a derivative instrument that has been designated as a hedging instrument under Topic 815. The standards in this Update clarify that a change in the counterparty to a derivative instrument that has been designated as the hedging instrument under Topic 815 does not, in and of itself, require designation of that hedging relationship provided that all other hedge accounting criteria continue to be met. For public business entities, the amendments in this Update are effective for financial statements issued for fiscal years beginning after December 15, 2016, and interim periods within those fiscal years. For all other entities, the amendments in this ASU are effective for financial statements issued for fiscal years beginning after December 15, 2017, and interim periods within fiscal years beginning after December 15, 2018. An entity has an option to apply the amendments in this ASU on either a prospective basis or a modified retrospective basis. Early adoption is permitted, including adoption in an interim period. This ASU is not expected to have a significant impact on the Company's financial statements.



In March 2016, the FASB issued ASU 2016-06, *Derivatives and Hedging (Topic 815)*. The amendments apply to all entities that are issuers of or investors in debt instruments (or hybrid financial instruments that are determined to have a debt host) with embedded call (put) options. The amendments in this update clarify the requirements for assessing whether contingent call (put) options that can accelerate the payment of principal on debt instruments are clearly and closely related to their debt host. An entity performing the assessment under the amendments in this Update is required to assess the embedded call (put) options solely in accordance with the four-step decision sequence. For public business entities, the amendments in this Update are effective for financial statements issued for fiscal years beginning after December 15, 2016, and interim periods within those fiscal years. For entities other than public business entities, the amendments in this Update are effective for financial statements issued for fiscal years beginning after December 15, 2017, and interim periods within fiscal years beginning after December 15, 2018. Early adoption is permitted, including adoption in an interim period. This ASU is not expected to have a significant impact on the Company's financial statements.

In March 2016, the FASB issued ASU 2016-07, *Investments – Equity Method and Joint Ventures (Topic 323)*. The Update affects all entities that have an investment that becomes qualified for the equity method of accounting as a result of an increase in the level of ownership interest or degree of influence. The amendments in this Update eliminate the requirement that when an investment qualifies for use of the equity method as a result of an increase in the level of ownership interest or degree of influence, an investor must adjust the investment, results of operations, and retained earnings retroactively on a step-by-step basis as if the equity method had been in effect during all previous periods that the investment had been held. The amendments require that the equity method investor add the cost of acquiring the additional interest in the investee to the current basis of the investor's previously held interest and adopt the equity method of accounting as of the date the investment becomes qualified for equity method accounting. Therefore, upon qualifying for the equity method of accounting, no retroactive adjustment of the investment is required. The amendments in this Update require that an entity that has an available-for-sale equity security that becomes qualified for the equity method of accounting recognize through earnings the unrealized holding gain or loss in accumulated other comprehensive income at the date the investment becomes qualified for use of the equity method. The amendments in this Update are effective for all entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2016. The amendments should be applied prospectively upon their effective date to increases in the level of ownership interest or degree of influence that result in the adoption of the equity method. Earlier application is permitted. This ASU is not expected to have a significant impact on the Company's financial statements.

In March 2016, the FASB issued ASU 2016-08, *Revenue from Contracts with Customers (Topic 606)*. The amendments in this Update affect entities with transactions included within the scope of Topic 606, which includes entities that enter into contracts with customers to transfer goods or services (that are an output of the entity's ordinary activities) in exchange for consideration. The amendments in this update do not change the core principle of the guidance in Topic 606; they simply clarify the implementation guidance on principal versus agent considerations. The amendments in this Update are intended to improve the operability and understandability of the implementation guidance on principal versus agent considerations. The amendments in this Update affect the guidance in ASU 2014-09, *Revenue from Contracts with Customers (Topic 606)*, which is not yet effective. The effective date and transition requirements for the amendments in this Update are the same as the effective date and transition requirements of Update 2014-09. ASU No. 2015-14, *Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date*, defers the effective date of Update 2014-09 by one year. The Company is currently evaluating

the impact the adoption of the standard will have on the Company's financial position or results of operations.

In March 2016, the FASB issued ASU 2016-09, *Compensation – Stock Compensation (Topic 718)*. The amendments in this Update affect all entities that issue share-based payment awards to their employees. The standards in this Update provide simplification for several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as with equity or liabilities, and classification on the statement of cash flows. Some of the areas for simplification apply only to nonpublic entities. In addition to those simplifications, the amendments eliminate the guidance in Topic 718 that was indefinitely deferred shortly after the issuance of FASB Statement No. 123 (revised 2004), *Share-Based Payment*. This should not result in a change in practice because the guidance that is being superseded was never effective. For public business entities, the amendments in this Update are effective for annual periods beginning after December 15, 2016, and interim periods within those annual periods. For all other entities, the amendments are effective for annual periods beginning after December 15, 2017, and interim periods within annual periods beginning after December 15, 2018. Early adoption is permitted for any entity in any interim or annual period. This ASU is not expected to have a significant impact on the Company's financial statements.

In April 2016, the FASB issued ASU 2016-10, *Revenue from Contracts with Customers (Topic 606)*. The amendments in this Update affect entities with transactions included within the scope of Topic 606, which includes entities that enter into contracts with customers to transfer goods or services in exchange for consideration. The amendments in this Update do not change the core principle for revenue recognition in Topic 606. Instead, the amendments provide (1) more detailed guidance in a few areas and (2) additional implementation guidance and examples based on feedback the FASB received from its stakeholders. The amendments are expected to reduce the degree of judgment necessary to comply with Topic 606, which the FASB expects will reduce the potential for diversity arising in practice and reduce the cost and complexity of applying the guidance. The amendments in this Update affect the guidance in ASU 2014-09, *Revenue from Contracts with Customers (Topic 606)*, which is not yet effective. The effective date and transition requirements for the amendments in this Update are the same as the effective date and transition requirements in Topic 606 (and any other Topic amended by Update 2014-09). ASU 2015-14, *Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date*, defers the effective date of Update 2014-09 by one year. The Company is currently evaluating the impact the adoption of the standard will have on the Company's financial position and/or results of operations.

In May 2016, the FASB issued ASU 2016-11, *Revenue Recognition (Topic 605) and Derivative and Hedging (Topic 815)*, which rescinds SEC paragraphs pursuant to two SEC Staff Announcements at the March 3, 2016, Emerging Issues Task Force meeting. This ASU did not have a significant impact on the Company's financial statements

In May 2016, the FASB issued ASU 2016-12, *Revenue from Contracts with Customers (Topic 606)*, which among other things clarifies the objective of the collectability criterion in Topic 606, as well as certain narrow aspects of Topic 606. The amendments in this Update affect the guidance in ASU 2014-09, *Revenue from Contracts with Customers (Topic 606)*, which is not yet effective. The effective date and transition requirements for the amendments in this Update are the same as the effective date and transition requirements for Topic 606 (and any other Topic amended by Update 2014-09). ASU 2015-14, *Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date*, defers the effective date of Update 2014-09 by one year. This ASU is not expected to have a significant impact on the Company's financial statements

In June 2016, the FASB issued ASU 2016-13, *Financial Instruments-Credit Losses: Measurement of Credit Losses on Financial Instruments* ("ASU 2016-13"), which changes the impairment model for most financial assets. This ASU is intended to improve financial reporting by requiring timelier recording of credit losses on loans and other financial instruments held by financial institutions and other organizations. The underlying premise of the ASU is that financial assets measured at amortized cost should be presented at the net amount expected to be collected, through an allowance for credit losses that is deducted from the amortized cost basis. The allowance for credit losses should reflect management's current estimate of credit losses that are expected to occur over the remaining life of a financial asset. The income statement will be effected for the measurement of credit losses for newly recognized financial assets, as well as the expected increases or decreases of expected credit losses that have taken place during the period. ASU 2016-13 is effective for annual and interim periods beginning after December 15, 2019, and early adoption is permitted for annual and interim periods beginning after December 15, 2018. With certain exceptions, transition to the new requirements will be through a cumulative effect adjustment to opening retained earnings as of the beginning of the first reporting period in which the guidance is adopted. The Company is currently evaluating the impact the

adoption of the standard will have on the Company's financial position or results of operations.

**2.EARNINGS PER SHARE**

Basic earnings per common share is computed by dividing net income available to common shareholders by the weighted average number of shares of common stock outstanding, net of any treasury shares, during the period. Diluted earnings per share is calculated by dividing net income available to common shareholders by the weighted average number of shares of common stock outstanding, net of any treasury shares, after consideration of the potential dilutive effect of common stock equivalents, based upon the treasury stock method using an average market price for the period.

The calculated basic and diluted earnings per share are as follows:

	Three Months Ended June 30,			
	2016 Basic	Diluted	2015 Basic	Diluted
	(Dollars in Thousands Except Per Share Data)			
Net income	\$777	\$777	\$47	\$47
Weighted average shares outstanding	7,330,386	7,330,386	8,195,086	8,195,086
Effect of common stock equivalents	-	200,986	-	165,431
Adjusted weighted average shares used in earnings per share computation	7,330,386	7,531,372	8,195,086	8,360,517
Earnings per share - basic and diluted	\$0.10	\$0.10	\$0.01	\$0.01
	Nine Months Ended June 30,			
	2016 Basic	Diluted	2015 Basic	Diluted
	(Dollars in Thousands Except Per Share Data)			
Net income	\$1,738	\$1,738	\$2,219	\$2,219
Weighted average shares outstanding	7,442,956	7,442,956	8,539,207	8,539,207
Effect of common stock equivalents	-	210,125	-	158,303
Adjusted weighted average shares used in earnings per share computation	7,442,956	7,653,081	8,539,207	8,697,510
Earnings per share - basic and diluted	\$0.23	\$0.23	\$0.26	\$0.26

All exercisable stock options outstanding as of June 30, 2016 and 2015 had exercise prices below the then current per share market price for the Company's common stock and were considered dilutive for the earnings per share calculation.



### 3. ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)

The following table presents the changes in accumulated other comprehensive (loss) income by component, net of tax:

	Three Months Ended June 30,	
	2016	2015
	(Dollars in Thousands)	
	Unrealized gains (losses) on available for sale securities (a)	Unrealized gains (losses) on available for sale securities (a)
Beginning Balance	\$ 783	\$ 101
Other comprehensive income (loss) before reclassification	255	(756)
Amount reclassified from accumulated other comprehensive income (loss)	(106)	-
Total other comprehensive income (loss)	149	(756)
Ending Balance	\$ 932	\$ (655)

(a) All amounts are net of tax. Amounts in parentheses indicate debits.

	Nine Months Ended June 30,	
	2016	2015
	(Dollars in Thousands)	
	Unrealized gains (losses) on available for sale securities (a)	Unrealized gains (losses) on available for sale securities (a)
Beginning Balance	\$ 18	\$ (953)
Other comprehensive income before reclassification	\$ 1,020	-
Amount reclassified from accumulated other comprehensive income	(106)	298
Total other comprehensive income	914	298
Ending Balance	\$ 932	\$ (655)

(a) All amounts are net of tax. Amounts in parentheses indicate debits.





	Three Months Ended June 30,		Affected Line Item in the Statement Where Net Income is Presented
	2016	2015	
Details about other comprehensive income	Amount Reclassified from Accumulated Other Comprehensive Income (a)	Amount Reclassified from Accumulated Other Comprehensive Income (a)	
Unrealized gains on available for sale securities	\$ 161	\$ -	Gain on sale of securities available for sale
	(55 )	-	Income taxes
	\$ 106	\$ -	Net of tax

(a) Amounts in parentheses indicate debits to net income

	Nine Months Ended June 30,		Affected Line Item in the Statement Where Net Income is Presented
	2016	2015	
Details about other comprehensive income	Amount Reclassified from Accumulated Other Comprehensive Income (a)	Amount Reclassified from Accumulated Other Comprehensive Income (a)	
Unrealized gains on available for sale securities	\$ 161	\$ -	Gain on sale of securities available for sale
	(55 )	-	Income taxes
	\$ 106	\$ -	Net of tax

(a) Amounts in parentheses indicate debits to net income

#### 4. INVESTMENT AND MORTGAGE-BACKED SECURITIES

The amortized cost and fair value of investment and mortgage-backed securities, with gross unrealized gains and losses, are as follows:

	June 30, 2016			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(Dollars in Thousands)			
<b>Securities Available for Sale:</b>				
U.S. government and agency obligations	\$25,985	\$ 63	\$ -	\$26,048
Mortgage-backed securities - U.S. government agencies	90,489	1,124	(81 )	91,532
Corporate bonds	20,433	621	-	21,054
Total debt securities available for sale	136,907	1,808	(81 )	138,634
FHLMC preferred stock	6	43	-	49
Total securities available for sale	\$136,913	\$ 1,851	\$ (81 )	\$138,683
<b>Securities Held to Maturity:</b>				
U.S. government and agency obligations	\$5,644	\$ 441	\$ -	\$6,085
Mortgage-backed securities - U.S. government agencies	9,844	864	-	10,708
Total securities held to maturity	\$15,488	\$ 1,305	\$ -	\$16,793

	September 30, 2015			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(Dollars in Thousands)			
<b>Securities Available for Sale:</b>				
U.S. government and agency obligations	\$18,988	\$ -	\$ (276 )	\$18,712
Mortgage-backed securities - U.S. government agencies	58,462	475	(225 )	58,712
Total debt securities available for sale	77,450	475	(501 )	77,424
FHLMC preferred stock	6	53	-	59
Total securities available for sale	\$77,456	\$ 528	\$ (501 )	\$77,483
<b>Securities Held to Maturity:</b>				
U.S. government and agency obligations	\$54,929	\$ 462	\$ (849 )	\$54,542
Mortgage-backed securities - U.S. government agencies	11,455	880	-	12,335
Total securities held to maturity	\$66,384	\$ 1,342	\$ (849 )	\$66,877

The following table shows the gross unrealized losses and related fair values of the Company's investment securities, aggregated by investment category and length of time that individual securities had been in a continuous loss position at June 30, 2016:

	Less than 12 months		More than 12 months		Total	
	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value
	(Dollars in Thousands)					
<b>Securities Available for Sale:</b>						
Mortgage-backed securities - U.S. government agencies	\$(3)	\$1,113	\$ (78 )	\$ 11,535	\$(81)	\$12,648
Total	\$(3)	\$1,113	\$ (78 )	\$ 11,535	\$(81)	\$12,648

The following table shows the gross unrealized losses and related fair values of the Company's investment securities, aggregated by investment category and length of time that individual securities had been in a continuous loss position at September 30, 2015:

	Less than 12 months		More than 12 months		Total	
	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value
(Dollars in Thousands)						
<b>Securities Available for Sale:</b>						
U.S. government and agency obligations	\$(85 )	\$4,910	\$(191 )	\$ 13,802	\$(276 )	\$18,712
Mortgage-backed securities - agency	(138)	22,173	(87 )	9,206	(225 )	31,379
Total securities available for sale	(223)	27,083	(278 )	23,008	(501 )	50,091
<b>Securities Held to Maturity:</b>						
U.S. government and agency obligations	-	-	(849 )	42,603	(849 )	42,603
Total securities held to maturity	-	-	(849 )	42,603	(849 )	42,603
<b>Total</b>	<b>\$(223)</b>	<b>\$27,083</b>	<b>\$(1,127 )</b>	<b>\$ 65,611</b>	<b>\$(1,350)</b>	<b>\$92,694</b>

Management evaluates securities for other-than-temporary impairment ("OTTI") at least once each quarter, and more frequently when economic or market concerns warrant such evaluation. The evaluation is based upon factors such as the creditworthiness of the issuers/guarantors, the underlying collateral, if applicable, and the continuing performance of the securities. Management also evaluates other facts and circumstances that may be indicative of an OTTI condition. This includes, but is not limited to, an evaluation of the type of security, the length of time and extent to which the fair value of the security has been less than cost, and the near-term prospects of the issuer.

The Company assesses whether a credit loss exists with respect to a security by considering whether (1) the Company has the intent to sell the security, (2) it is more likely than not that it will be required to sell the security before recovery has occurred, or (3) it does not expect to recover the entire amortized cost basis of the security. The Company bifurcates the OTTI impact on impaired securities where impairment in value was deemed to be other than temporary between the component representing credit loss and the component representing loss related to other factors. The portion of the fair value decline attributable to credit loss must be recognized through a charge to earnings. The credit component is determined by comparing the present value of the cash flows expected to be collected, discounted at the rate in effect before recognizing any OTTI, with the amortized cost basis of the debt security. The Company uses the cash flows expected to be realized from the security, which includes assumptions about interest rates, timing and severity of defaults, estimates of potential recoveries, the cash flow distribution from the security and other factors, then applies a discount rate equal to the effective yield of the security. The difference

between the present value of the expected cash flows and the amortized book value is considered a credit loss. The fair value of the security is determined using the same expected cash flows; the discount rate is a rate the Company determines from open market and other sources as appropriate for the particular security. The difference between the fair value and the security's remaining amortized cost is recognized in other comprehensive income (loss).

For both the three and nine months ended June 30, 2016 and 2015, the Company did not record any credit losses on investment securities through earnings.

**U.S. Agency Issued Mortgage-Backed Securities** - At June 30, 2016, there were three securities in a gross unrealized loss for less than 12 months while there were seven securities in a gross unrealized loss for more than 12 months at such date. These securities represent asset-backed issues that are issued or guaranteed by a U.S. Government sponsored agency or carry the full faith and credit of the United States through a government agency and are currently rated AAA by at least one bond credit rating agency. As a result, the Company does not consider these investments to be other-than-temporarily impaired at June 30, 2016.

The amortized cost and fair value of debt securities, 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.

The maturity table below excludes mortgage-backed securities because the contractual maturities of such securities are not indicative of actual maturities due to significant prepayments.

	June 30, 2016			
	Held to Maturity		Available for Sale	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
	(Dollars in Thousands)			
Due after one through five years	\$1,999	\$2,215	\$1,056	\$1,077
Due after five through ten years	645	645	21,377	21,977
Due after ten years	3,000	3,225	23,985	24,048
Total	\$5,644	\$6,085	\$46,418	\$47,102

During both three and nine month periods ended June 30, 2016, the Company sold five mortgage-back securities with an aggregate amortized cost of \$14.2 million and recognized an aggregate gain of \$153,000 (pre-tax). Also, during the same periods the Company had an aggregate of \$11.0 million of agency securities called at a price higher than the aggregated amortized cost and recorded a gain of \$8,000. No securities were sold during both the 2015 periods.

## 5. LOANS RECEIVABLE

Loans receivable consist of the following:

	June 30, 2016	September 30, 2015
	(Dollars in Thousands)	
One-to-four family residential	\$242,616	\$ 259,163
Multi-family residential	6,422	6,249
Commercial real estate	68,573	25,799
Construction and land development	34,020	38,953
Consumer	754	392
 Total loans	 352,385	 330,556
Undisbursed portion of loans-in-process	(8,443 )	(17,097 )
Deferred loan costs	1,786	2,104
Allowance for loan losses	(3,269 )	(2,930 )
 Net loans	 \$342,459	 \$ 312,633

The following table summarizes by loan segment the balance in the allowance for loan losses and the loans individually and collectively evaluated for impairment by loan segment at June 30, 2016:

	One- to-four family residential	Multi-family residential	Commercial real estate	Construction and land development	Consumer	Unallocated	Total
	(Dollars in Thousands)						
Allowance for Loan Losses:							
Individually evaluated for impairment	\$-	\$ -	\$ -	\$ -	\$ -	\$ -	\$-
Collectively evaluated for impairment	1,445	62	664	777	9	312	3,269
Total ending allowance balance	\$ 1,445	\$ 62	\$ 664	\$ 777	\$ 9	\$ 312	\$3,269
Loans:							
Individually evaluated for impairment	\$5,569	\$ 339	\$ 3,496	\$ 10,113	\$ -		\$19,517
Collectively evaluated for impairment	237,047	6,083	65,077	23,907	754		332,868
Total loans	\$242,616	\$ 6,422	\$ 68,573	\$ 34,020	\$ 754		\$352,385





The following table summarizes by loan segment the balance in the allowance for loan losses and the loans individually and collectively evaluated for impairment by loan segment at September 30, 2015:

	One- to-four family residential (Dollars in Thousands)	Multi-family residential	Commercial real estate	Construction and land development	Commercial business	Consumer	Unallocated	Total
Allowance for Loan Losses:								
Individually evaluated for impairment	\$-	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$-
Collectively evaluated for impairment	1,635	66	231	724	-	5	269	2,930
Total ending allowance balance	\$1,635	\$ 66	\$ 231	\$ 724	\$ -	\$ 5	\$ 269	\$2,930
Loans:								
Individually evaluated for impairment	\$4,206	\$ -	\$ 3,768	\$ 8,796	\$ -	\$ -		\$16,770
Collectively evaluated for impairment	254,957	6,249	22,031	30,157	-	392		313,786
Total loans	\$259,163	\$ 6,249	\$ 25,799	\$ 38,953	\$ -	\$ 392		\$330,556

The loan portfolio is segmented at a level that allows management to monitor both risk and performance. Management evaluates for potential impairment all construction loans, commercial real estate and commercial business loans and all loans more than 90 days delinquent as to principal and/or interest. Loans are considered to be impaired when, based on current information and events, it is probable that the Company will be unable to collect in full the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement.

Once the determination is made that a loan is impaired, the determination of whether a specific allocation of the allowance is necessary is generally measured by comparing the recorded investment in the loan to the fair value of the loan using one of the following three methods: (a) the present value of the expected future cash flows discounted at the loan's effective interest rate; (b) the loan's observable market price; or (c) the fair value of the collateral less selling costs. Management primarily utilizes the fair value of collateral method as a practically expedient alternative. On collateral method evaluations, any portion of the loan deemed uncollectible is charged-off against the loan loss allowance.

The following table presents impaired loans by class as of June 30, 2016, segregated by those for which a specific allowance was required and those for which a specific allowance was not required.



	Impaired Loans with Specific Allowance		Impaired Loans with No Specific Allowance		Total Impaired Loans
	Recorded Investment	Related Allowance	Recorded Investment	Recorded Investment	
One-to-four family residential	\$-	\$ -	\$ 5,569	\$ 5,569	\$ 5,914
Multi-family residential	-	-	339	339	339
Commercial real estate	-	-	3,496	3,496	3,496
Construction and land development	-	-	10,113	10,113	10,113
Total Loans	\$-	\$ -	\$ 19,517	\$ 19,517	\$ 19,862

The following table presents impaired loans by class as of September 30, 2015, segregated by those for which a specific allowance was required and those for which a specific allowance was not required.

	Impaired Loans with Specific Allowance		Impaired Loans with No Specific Allowance		Total Impaired Loans
	Recorded Investment	Related Allowance	Recorded Investment	Recorded Investment	
One-to-four family residential	\$-	\$ -	\$ 4,206	\$ 4,206	\$ 4,550
Commercial real estate	-	-	3,768	3,768	3,768
Construction and land development	-	-	8,796	8,796	8,796
Total Loans	\$-	\$ -	\$ 16,770	\$ 16,770	\$ 17,114

The following table presents the average recorded investment in impaired loans and related interest income recognized for the periods indicated:

	Three Months Ended June 30, 2016		
	Average Recorded Investment	Income Recognized on Accrual Basis	Income Recognized on Cash Basis
	(Dollars in Thousands)		
One-to-four family residential	\$ 5,052	\$ 14	\$ 30
Multi-family residential	341	6	-
Commercial real estate	3,595	35	-
Construction and land development	9,808	-	-
Total Loans	\$ 18,796	\$ 55	\$ 30

	Nine Months Ended June 30, 2016		
	Average Recorded Investment	Income Recognized on Accrual Basis	Income Recognized on Cash Basis
	(Dollars in Thousands)		
One-to-four family residential	\$ 4,978	\$ 89	\$ 78
Multi-family residential	346	18	-
Commercial real estate	3,667	74	12
Construction and land development	9,432	-	62
Total Loans	\$ 18,423	\$ 181	\$ 152

	Three Months Ended June 30, 2015		
	Average Recorded Investment	Income Recognized on Accrual Basis	Income Recognized on Cash Basis
	(Dollars in Thousands)		
One-to-four family residential	\$ 9,222	\$ 115	\$ 42
Multi-family residential	357	6	-
Commercial real estate	3,832	54	24
Construction and land development	7,977	109	65
Total Loans	\$ 21,388	\$ 284	\$ 131

	Nine Months Ended June 30, 2015		
	Average Recorded Investment	Income Recognized on Accrual Basis	Income Recognized on Cash Basis
	(Dollars in Thousands)		
One-to-four family residential	\$ 9,865	\$ 378	\$ 119
Multi-family residential	361	19	-
Commercial real estate	3,801	157	58
Construction and land development	7,728	318	129
Total Loans	\$ 21,755	\$ 872	\$ 306

Federal regulations and our policy require that the Company utilize an internal asset classification system as a means of reporting problem and potential problem assets. The Company has incorporated an internal asset classification system, consistent with Federal banking regulations, as a part of its credit monitoring system. Management currently classifies problem and potential problem assets as “special mention”, “substandard,” “doubtful” or “loss” assets. An asset is considered “substandard” if it is inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. “Substandard” assets include those characterized by the “distinct possibility” that the insured institution will sustain “some loss” if the deficiencies are not corrected. Assets classified as “doubtful” have all of the weaknesses inherent in those classified “substandard” with the added characteristic that the weaknesses present make “collection or liquidation in full,” on the basis of currently existing facts, conditions, and values, “highly questionable and improbable.” Assets classified as “loss” are those considered “uncollectible” and of such little value that their continuance as assets without the establishment of a specific loss reserve is not warranted. Assets which do not currently expose the insured institution to sufficient risk to warrant classification in one of the aforementioned categories but possess weaknesses are required to be designated “special mention.”

The following table presents the classes of the loan portfolio in which a formal risk weighting system is utilized summarized by the aggregate “Pass” and the criticized category of “special mention”, and the classified categories of “substandard”, “doubtful” and “loss” within the Company’s risk rating system as applied to the loan portfolio. The Company had no loans classified as “doubtful” or “loss” at either of the dates presented.

	June 30, 2016			Total Loans
	Pass	Special Mention	Substandard	
	(Dollars in Thousands)			
One-to-four family residential	\$2,655	\$ 1,693	\$ 1,221	\$5,569
Multi-family residential	6,084	-	338	6,422
Commercial real estate	64,884	949	2,740	68,573
Construction and land development	23,907	-	10,113	34,020
Total Loans	\$97,530	\$ 2,642	\$ 14,412	\$ 114,584

	September 30, 2015			Total Loans
	Pass	Special Mention	Substandard	
	(Dollars in Thousands)			
One-to-four family residential	\$ 1,348	\$ 2,107	\$ 751	\$4,206
Multi-family residential	5,898	351	-	6,249
Commercial real estate	22,005	965	2,829	25,799
Construction and land development	30,157	-	8,796	38,953
Total Loans	\$59,408	\$ 3,423	\$ 12,376	\$75,207

The Company evaluates the classification of one-to-four family residential and consumer loans primarily on a pooled basis. If the Company becomes aware that adverse or distressed conditions exist that may affect a particular single-family residential loan, the loan is downgraded following the above definitions of special mention, substandard, doubtful and loss.

The following table represents loans in which a formal risk rating system is not utilized, but loans are segregated between performing and non-performing based primarily on delinquency status. Non-performing loans that would be included in the table are those loans greater than 90 days past due as to principal and/or interest that do not have a designated risk rating.

	June 30, 2016		Total Loans
	Performing	Non- Performing	
	(Dollars in Thousands)		
One-to-four family residential	\$237,047	\$ -	\$237,047
Consumer	754	-	754
Total Loans	\$237,801	\$ -	\$237,801

	September 30, 2015		Total Loans
	Performing	Non- Performing	
	(Dollars in Thousands)		
One-to-four family residential	\$254,957	\$ -	\$254,957
Consumer	392	-	392
Total Loans	\$255,349	\$ -	\$255,349

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 due or overdue, as the case may be. The following table presents the loan categories of the loan portfolio summarized by the aging categories of performing and delinquent loans and nonaccrual loans:



	June 30, 2016						
		30-89 Days	90 Days + Past Due	90 Days+ Past Due and Accruing	Total Past Due and Accruing	Total Loans	Non- Accrual
	Current	Past Due	Past Due				
	(Dollars in Thousands)						
One-to-four family residential	\$235,673	\$ 2,310	\$ 3,233	\$ -	\$ 2,310	\$242,616	\$4,633
Multi-family residential	6,422	-	-	-	-	6,422	-
Commercial real estate	63,967	3,260	1,346	-	3,260	68,573	1,346
Construction and land development	23,907	-	10,113	-	-	34,020	10,113
Consumer	754	-	-	-	-	754	-
Total Loans	\$330,723	\$ 5,570	\$ 14,692	\$ -	\$ 5,570	\$352,385	\$16,092
	September 30, 2015						
		30-89 Days	90 Days + Past Due	90 Days+ Past Due and Accruing	Total Past Due and Accruing	Total Loans	Non- Accrual
	(Dollars in Thousands)						
One-to-four family residential	\$255,669	\$ 1,462	\$ 2,032	\$ -	\$ 1,462	\$259,163	\$3,547
Multi-family residential	6,249	-	-	-	-	6,249	-
Commercial real estate	25,114	504	181	-	504	25,799	1,589
Construction and land development	38,953	-	-	-	-	38,953	8,796
Consumer	392	-	-	-	-	392	-
Total Loans	\$326,377	\$ 1,966	\$ 2,213	\$ -	\$ 1,966	\$330,556	\$13,932

The allowance for loan losses is established through a provision for loan losses charged to expense. The Company maintains the allowance at a level believed to cover all known and inherent losses in the portfolio that are both probable and reasonable to estimate at each reporting date. Management reviews the allowance for loan losses no less than quarterly in order to identify these inherent losses and to assess the overall collection probability for the loan portfolio in view of these inherent losses. For each primary type of loan, a loss factor is established reflecting an estimate of the known and inherent losses in such loan type contained in the portfolio using both a quantitative analysis as well as consideration of qualitative factors. The evaluation process includes, among other things, an analysis of delinquency trends, non-performing loan trends, the level of charge-offs and recoveries, prior loss experience, total loans outstanding, the volume of loan originations, the type, size and geographic concentration of the Company's loans, the value of collateral securing the loans, the borrowers' ability to repay and repayment performance, the number of loans requiring heightened management oversight, local economic conditions and industry experience.



Commercial real estate loans entail significant additional credit risks compared to owner-occupied one-to-four family residential mortgage loans, as they generally involve large loan balances concentrated with single borrowers or groups of related borrowers. In addition, the payment experience on loans secured by income-producing properties typically depends on the successful operation of the related real estate project and/or business operation of the borrower who is, in some cases, also the primary occupant, and thus may be subject to a greater extent to the effects of adverse conditions in the real estate market and in the economy in general. Commercial business loans typically involve a higher risk of default than residential loans of like duration since their repayment is generally dependent on the successful operation of the borrower's business and the sufficiency of collateral, if any. Land acquisition, development and construction lending exposes the Company to greater credit risk than permanent mortgage financing. The repayment of land acquisition, development and construction loans depends upon the sale of the property to third parties or the availability of permanent financing upon completion of all improvements. These events may adversely affect the sale of the properties, potentially reducing both the borrowers' ability to make required payments as well as reducing the value of the collateral property. Such lending is additionally subject to the risk that if the estimate of construction cost proves to be inaccurate, the Company potentially will be compelled to advance additional funds to allow completion of the project. In addition, if the estimate of value proves to be inaccurate, the Company may be confronted with a project, when completed, having less value than the loan amount. If the Company is forced to foreclose on a project prior to completion, there is no assurance that the Company would be able to recover the entire unpaid portion of the loan.

The following table summarizes the primary segments of the allowance for loan losses. Activity in the allowance is presented for the three and nine month periods ended June 30, 2016 and 2015:

	Three Months Ended June 30, 2016						
	One- to four-family residential	Multi-family residential	Commercial real estate	Construction and land development	Consumer	Unallocated	Total
ALLL balance at December 31, 2015	\$ 1,511	\$ 43	\$ 428	\$ 773	\$ 7	\$ 276	\$ 3,038
Charge-offs	-	-	-	-	-	-	-
Recoveries	-	-	-	81	-	-	81
Provision	(66 )	19	236	(77 )	2	36	150
ALLL balance at June 30, 2016	\$ 1,445	\$ 62	\$ 664	\$ 777	\$ 9	\$ 312	\$ 3,269

	Nine Months Ended June 30, 2016						
	One- to four-family residential	Multi-family residential	Commercial real estate	Construction and land development	Consumer	Unallocated	Total
ALLL balance at September 30, 2015	\$ 1,635	\$ 66	\$ 231	\$ 724	\$ 5	\$ 269	\$ 2,930
Charge-offs	(11 )	-	-	-	-	-	(11 )

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Recoveries	93	-	32	-	-	-	125
Provision	(272 )	(4 )	401	53	4	43	225
ALLL balance at June 30, 2016	\$1,445	\$ 62	\$ 664	\$ 777	\$ 9	\$ 312	\$3,269

Three Months Ended June 30, 2015								
	One- to four-family residential	Multi-family residential	Commercial real estate	Construction and land development	Commercial business	Consumer	Unallocated	Total
(Dollars in Thousands)								
ALLL balance at March 31, 2015	\$ 1,545	\$ 51	\$ 207	\$ 545	\$ -	\$ 4	\$ 236	\$ 2,588
Charge-offs	(126 )	-	-	-	-	-	-	(126 )
Recoveries	1	-	-	-	-	-	-	1
Provision	219	9	8	(38 )	-	-	12	210
ALLL balance at June 30, 2015	\$ 1,639	\$ 60	\$ 215	\$ 507	\$ -	\$ 4	\$ 248	\$ 2,673

Nine Months Ended June 30, 2015								
	One- to four-family residential	Multi-family residential	Commercial real estate	Construction and land development	Commercial business	Consumer	Unallocated	Total
(Dollars in Thousands)								
ALLL balance at September 30, 2014	\$ 1,663	\$ 67	\$ 122	\$ 323	\$ 15	\$ 4	\$ 231	\$ 2,425
Charge-offs	(338 )	-	-	-	-	-	-	(338 )
Recoveries	1	-	-	-	-	-	-	1
Provision	313	(7 )	93	184	(15 )	-	17	585
ALLL balance at June 30, 2015	\$ 1,639	\$ 60	\$ 215	\$ 507	\$ -	\$ 4	\$ 248	\$ 2,673

The Company recorded a provision for loan losses in the amount of \$150,000 and \$225,000 for the three and nine months period ended June 30, 2016, compared to the \$210,000 provision for the three months and \$585,000 for the nine months ended June 30, 2015.

At June 30, 2016, the Company had ten loans aggregating \$7.8 million that were classified as troubled debt restructurings (“TDRs”). Three of such loans aggregating \$5.6 million as of June 30, 2016 were classified as non-performing as a result of not achieving a sufficiently long payment history, under the restructured terms, to justify returning the loans to performing (accrual) status. Two of these three loans totaling \$4.2 million (which are part of the Company’s largest lending relationship) are over 90 days past due resulting from the discontinuation of funding by the Company due to the re-negotiation of the projects’ cash flows. Three loans aggregating \$5.6 million related to the largest lending relationship are more than ninety days past due.

The Company did not restructure any debt during the three and nine month periods ended June 30, 2016 and 2015.



## 6. DEPOSITS

Deposits consist of the following major classifications:

	June 30, 2016		September 30, 2015	
	Amount	Percent	Amount	Percent
	(Dollars in Thousands)			
Money market deposit accounts	\$56,115	14.5 %	\$60,736	16.6 %
Interest-bearing checking accounts	34,909	9.0	35,649	9.8
Non interest-bearing checking accounts	2,832	0.7	2,293	0.6
Passbook, club and statement savings	70,767	18.3	70,355	19.3
Certificates maturing in six months or less	81,185	21.0	49,857	13.7
Certificates maturing in more than six months	140,832	36.5	146,184	40.0
Total	\$386,640	100.0 %	\$365,074	100.0 %

Certificates of \$250,000 and over totaled \$15.4 million as of June 30, 2016 and \$32.7 million as of September 30, 2015.

## 7. ADVANCES FROM FEDERAL HOME LOAN BANK

Pursuant to collateral agreement with the FHLB of Pittsburgh, advances are secured by qualifying first mortgage loans.

Type	Maturity Date	Amount	Coupon	Call Date
		(Dollars in Thousands)		
Fixed Rate -Advance	6-Jul-16	\$ 10,000	0.57 %	Not Applicable
Fixed Rate -Advance	13-Jul-16	\$ 10,000	0.54 %	Not Applicable
Fixed Rate -Advance	17-Nov-17	10,000	1.20 %	Not Applicable
Fixed Rate -Amortizing	1-Dec-17	3,009	1.16 %	Not Applicable
Fixed Rate -Advance	4-Dec-17	2,000	1.15 %	Not Applicable
Fixed Rate -Advance	16-Nov-18	7,500	1.40 %	Not Applicable
Fixed Rate -Advance	3-Dec-18	3,000	1.54 %	Not Applicable
Fixed Rate -Amortizing	18-Nov-19	4,718	1.53 %	Not Applicable
		\$ 50,227	1.02 %	(a)

(a) Weighted average coupon rate.

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## 8. DERIVATIVES

On April 6, 2006, the Company entered into an interest rate swap with a notional amount of \$10.0 million. The Company is hedging the benchmark index (LIBOR) in rolling 1-month FHLB advances with a receive float/pay fixed swap for a period of five years. The swap had a fair value loss position of \$170,000 at June 30, 2016.

On June 13, 2006, the Company entered into an interest rate swap with a notional amount to \$10.0 million. The Company is hedging the benchmark index (LIBOR) in rolling 1-month FHLB advances with a receive float/pay fixed swap for a period of five years. The swap had a fair value loss position of \$181,000 at June 30, 2016.

Both interest rate swaps are carried at fair value in accordance with FASB ASC 815 "Derivatives and Hedging."

## 9. INCOME TAXES

Items that gave rise to significant portions of deferred income taxes are as follows:

	June 30, 2016	September 30, 2015
	(Dollars in Thousands)	
Deferred tax assets:		
Allowance for loan losses	\$1,276	\$ 1,185
Nonaccrual interest	152	86
Accrued vacation	19	119
Capital loss carryforward	506	534
Split dollar life insurance	19	19
Post-retirement benefits	106	126
Unrealized loss on interest rate swaps	119	-
Employee benefit plans	499	530
Total deferred tax assets	2,696	2,599
Valuation allowance	(506 )	(534 )
Total deferred tax assets, net of valuation allowance	2,190	2,065
Deferred tax liabilities:		
Property	505	365
Unrealized gains on available for sale securities	602	10
Deferred loan fees	607	715

Total deferred tax liabilities	1,714	1,090
Net deferred tax assets	\$476	\$ 975

The Company establishes a valuation allowance for deferred tax assets when management believes that the use of the deferred tax assets is not likely to be fully realized through a carry back to taxable income in prior years or future reversals of existing taxable temporary differences, and/or to a lesser extent, future taxable income. The tax deduction generated by the redemption of the shares of a mutual fund held by the Bank and the subsequent impairment charge on the assets acquired through the redemption in kind are considered capital losses and can only be utilized to the extent of capital gains recognized over a five year period, resulting in the establishment of a valuation allowance for the carryforward period. The valuation allowance totaled \$506,000 at June 30, 2016, and \$534,000 at September 30, 2015.



There is currently no liability for uncertain tax positions and no known unrecognized tax benefits. The Company recognizes, when applicable, interest and penalties related to unrecognized tax benefits in the provision for income taxes in the Consolidated Statements of Operations as a component of income tax expense. The Company's federal and state income tax returns for taxable years through September 30, 2012 have been closed for purposes of examination by the Internal Revenue Service and the Pennsylvania Department of Revenue.

## 10. STOCK COMPENSATION PLANS

The Company maintains an employee stock ownership plan ("ESOP") for substantially all of its full-time employees. The ESOP purchased 427,057 shares (on a converted basis) of the Company's common stock for an aggregate cost of approximately \$4.5 million in fiscal 2005. The ESOP purchased an additional 255,564 shares during December 2013 and an additional 30,100 shares at the beginning January 2014, of the Company's common stock for an aggregate cost of approximately \$3.1 million. The shares were purchased with the proceeds of loans from the Company. Shares of the Company's common stock purchased by the ESOP are held in a suspense account until released for allocation to participants as the loans are repaid. Shares are allocated to each eligible participant based on the ratio of each such participant's compensation, as defined in the ESOP, to the total compensation of all eligible plan participants. As the unearned shares are released from the suspense account, the Company recognizes compensation expense equal to the fair value of the ESOP shares during the periods in which they become committed to be released. To the extent that the fair value of the ESOP shares released differs from the cost of such shares, the difference is charged or credited to equity as additional paid-in capital. As of June 30, 2016, the ESOP held 697,270 shares of which a total of 243,734 shares were allocated to participants' accounts. For the three months ended June 30, 2016 and 2015, the Company recognized \$129,000 for both periods in compensation expense related to the ESOP. For nine months ended June 30, 2016 and 2015, the Company recognized \$394,000 and \$337,000, respectively, in compensation expense related to the ESOP.

The Company maintains the 2008 Recognition and Retention Plan ("2008 RRP") which is administered by a committee of the Board of Directors of the Company. The RRP provides for the grant of shares of common stock of the Company to officers, employees and directors of the Company. In order to fund the grant of shares under the RRP, the RRP Trust purchased 213,528 shares (on a converted basis) of the Company's common stock in the open market for approximately \$2.5 million, at an average purchase price per share of \$11.49 as part of the 2008 RRP. The Company made sufficient contributions to the RRP Trust to fund these purchases. As of June 30, 2016, all the shares, with exception of 7,093 shares that had been forfeited, had been awarded as part of the 2008 RRP. Shares subject to awards under the 2008 RRP generally vest at the rate of 20% per year over five years. During February 2015, shareholders approved the 2014 Stock Incentive Plan (the "2014 SIP"). As part of the 2014 SIP, a maximum of 285,655 shares can be awarded as restricted stock awards or units, of which 235,500 shares were awarded during February 2015 of which 90,055 shares had been forfeited as of June 30, 2016.

Compensation expense related to the shares subject to restricted stock awards granted is recognized ratably over the five-year vesting period in an amount which totals the grant date fair value multiplied by the number of shares subject to the grant. During the three and nine months ended June 30, 2016, an aggregate of \$87,000 and \$329,000,

respectively, was recognized in compensation expense for the 2008 RRP and the grants pursuant to the 2014 SIP. Income tax benefits of \$30,000 and \$112,000, respectively, were recognized for the three and nine months ended June 30, 2016. During the three and nine months ended June 30, 2015, \$154,000 and \$262,000, respectively, was recognized in compensation expense for the 2008 RRP and the grants pursuant to the 2014 SIP. An income tax benefit of \$52,000 and \$89,000, respectively, was recognized for the three and nine months ended June 30, 2015. At June 30, 2016, approximately \$2.3 million in additional compensation expense for the shares awarded which remained outstanding related to the 2008 RRP and for the 2014 SIP remained unrecognized. At June 30, 2015, approximately \$2.8 million in additional compensation expense for the shares awarded related to the 2008 RRP and the 2014 SIP remained unrecognized.

A summary of the Company's non-vested stock award activity for the nine months ended June 30, 2016 and 2015 is presented in the following tables:

	Nine Months Ended June 30, 2016	
	Number of Shares (1)	Weighted Average Grant Date Fair Value
Nonvested stock awards at October 1, 2015	241,428	\$ 11.74
Granted	-	-
Forfeited	(30,180 )	11.55
Vested	(55,279 )	11.59
Nonvested stock awards at the June 30, 2016	155,969	\$ 11.83

	Nine Months Ended June 30, 2015	
	Number of Shares	Weighted Average Grant Date Fair Value
Nonvested stock awards at October 1, 2014	38,055	\$ 8.07
Granted	235,500	12.23
Forfeited	-	-
Vested	(10,314 )	8.22
Nonvested stock awards at the June 30, 2015	263,241	\$ 11.79

The Company maintains the 2008 Stock Option Plan (the "2008 Option Plan") which authorizes the grant of stock options to officers, employees and directors of the Company to acquire shares of common stock with an exercise price at least equal to the fair market value of the common stock on the grant date. Options generally become vested and exercisable at the rate of 20% per year over five years and are generally exercisable for a period of ten years after the grant date. A total of 533,808 shares of common stock were approved for future issuance pursuant to the 2008 Stock Option Plan. As of June 30, 2016, all of the options had been awarded under the 2008 Option Plan. As of June 30, 2016, 467,758 options (on a converted basis) were vested under the 2008 Option Plan. The 2014 SIP reserved up to 714,145 shares for issuance pursuant to options. Options to purchase 608,737 shares were awarded during February 2015, 605,000 shares pursuant to the 2014 SIP and the remainder pursuant to the 2008 Option Plan. As of June 30, 2016, the 2008 Option Plan had forfeited options covering 18,866 shares and the 2014 SIP had forfeited options covering 126,000 shares.

A summary of the status of the Company's stock options under the 2008 Option Plan and the 2014 SIP as of June 30, 2016 and 2015 are presented below:

	Nine Months Ended June 30, 2016	
	Number of Shares	Weighted Average Exercise Price
Outstanding at October 1, 2015	1,074,430	\$ 11.92
Granted	-	-
Exercised	(89,358 )	11.61
Forfeited	(80,476 )	11.52
Outstanding at June 30, 2016	904,596	\$ 11.99
Exercisable at June 30, 2016	489,679	\$ 11.45

	Nine Months Ended June 30, 2015	
	Number of Shares	Weighted Average Exercise Price
Outstanding at October 1, 2014	530,084	\$ 10.86
Granted	608,737	12.23
Exercised	-	-
Forfeited	-	-
Outstanding at June 30, 2015	1,138,821	\$ 11.59
Exercisable at June 30, 2015	445,147	\$ 11.37

The weighted average remaining contractual term was approximately 5.9 years for options outstanding as of June 30, 2016.

The estimated fair value of options granted during fiscal 2009 was \$2.98 per share, \$2.92 for options granted during fiscal 2010, \$3.34 for options granted during fiscal 2013, \$4.67 for the options granted during fiscal 2014 and \$4.58 for options granted during fiscal 2015. The fair value for grants made in fiscal 2015 was estimated on the date of grant using the Black-Scholes pricing model with the following assumptions: an exercise and fair value of \$12.23, expected term of seven years, volatility rate of 38.16%, interest rate of 1.62% and a yield of 0.98%.

During the three and nine months ended June 30, 2016, \$106,000 and \$322,000, respectively, was recognized in compensation expense for options granted pursuant to the 2008 Option Plan and the 2014 SIP. Tax benefits of \$36,000 and \$44,000, respectively, were recognized for the three and nine months ended June 30, 2016. During the

three and nine months ended June 30, 2015, \$158,000 and \$268,000, respectively, was recognized in compensation expense for options granted pursuant to the 2008 Option Plan and the 2014 SIP. Tax benefits of \$54,000 and \$91,000, respectively, were recognized for the three and nine months ended June 30, 2015.

At June 30, 2016, there was approximately \$1.8 million in additional compensation expense to be recognized for awarded options which remained outstanding and unvested at such date. The weighted average period over which this expense will be recognized is approximately 3.7 years.

11. COMMITMENTS AND CONTINGENT LIABILITIES

At June 30, 2016, the Company had \$10.8 million in outstanding commitments to originate fixed loans with market interest rates ranging from 3.75% to 5.00%. At September 30, 2015, the Company had \$2.5 million in outstanding commitments to originate fixed and variable-rate loans with market interest rates ranging from 4.25% to 5.25%. The aggregate undisbursed portion of loans-in-process amounted to \$8.0 million at June 30, 2016 and \$17.0 million at September 30, 2015.

The Company also had commitments under unused lines of credit of \$3.7 million as of June 30, 2016 and \$6.1 million as of September 30, 2015 and letters of credit outstanding of \$2.0 million as of June 30, 2016 and \$2.6 million as of September 30, 2015.

Among the Company's contingent liabilities are exposures to limited recourse arrangements with respect to the Company's sales of whole loans and participation interests. At June 30, 2016, the exposure, which represents a portion of credit risk associated with the interests sold, amounted to \$33,000. This exposure is for the life of the related loans and payables, on our proportionate share, as actual losses are incurred.

The Company is involved in various legal proceedings occurring in the ordinary course of business. Management of the Company, based on discussions with litigation counsel, believes that such proceedings will not have a material adverse effect on the financial condition, operations or cash flows of the Company. However, there can be no assurance that any of the outstanding legal proceedings to which the Company is a party will not be decided adversely to the Company's interests and not have a material adverse effect on the financial condition and operations of the Company.

12. FAIR VALUE MEASUREMENT

The fair value estimates presented herein are based on pertinent information available to management as of June 30, 2016 and September 30, 2015, respectively. Although management is not aware of any factors that would significantly affect the fair value amounts, such amounts have not been comprehensively revalued for purposes of these financial statements since that date and, therefore, current estimates of fair value may differ significantly from the amounts presented herein.

Generally accepted accounting principles used in the United States establish a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimizes the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value.

The three broad levels of hierarchy are as follows:

Level 1 Quoted prices in active markets for identical assets or liabilities.

Level 2 Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

Those assets as of June 30, 2016 which are to be measured at fair value on a recurring basis are as follows:

	Category Used for Fair Value Measurement			
	Level 1	Level 2	Level 3	Total
(Dollars in Thousands)				
Assets:				
Securities available for sale:				
U.S. Government and agency obligations	\$ -	\$ 26,048	\$ -	\$ 26,048
Mortgage-backed securities - U.S. Government agencies	-	91,532	-	91,532
Corporate bonds	-	21,054	-	21,054
FHLMC preferred stock	49	-	-	
Total	\$ 49	\$ 138,634	\$ -	\$ 138,634
Liabilities				
Interest rate swap contracts	\$ -	\$ 351	\$ -	\$ 351
Total	\$ -	\$ 351	\$ -	\$ 351

Those assets as of September 30, 2015 which are measured at fair value on a recurring basis are as follows:

	Category Used for Fair Value Measurement			
	Level 1	Level 2	Level 3	Total
(Dollars in Thousands)				
Assets:				
Securities available for sale:				
U.S. Government and agency obligations	\$ -	\$ 18,712	\$ -	\$ 18,712
Mortgage-backed securities - U.S. Government agencies	-	58,712	-	58,712
FHLMC preferred stock	59	-	-	59
Total	\$ 59	\$ 77,424	\$ -	\$ 77,483

Certain assets are measured at fair value on a nonrecurring basis; that is, the instruments are not measured at fair value on an ongoing basis but are subject to fair value adjustments in certain circumstances (for example, when there is evidence of impairment). The Company measures impaired loans and real estate owned at fair value on a non-recurring basis.

### Impaired Loans



The Company considers loans to be impaired when it becomes more likely than not that the Company will be unable to collect all amounts due in accordance with the contractual terms of the loan agreements. Collateral dependent impaired loans are based on the fair value of the collateral which is based on appraisals and would be categorized as Level 2 measurement. In some cases, adjustments are made to the appraised values for various factors including the age of the appraisal, age of the comparable included in the appraisal, and known changes in the market and in the collateral. These adjustments are based upon unobservable inputs, and therefore, the fair value measurement has been categorized as a Level 3 measurement. These loans are reviewed for impairment and written down to their net realizable value by charges against the allowance for loan losses. The collateral underlying these loans had a fair value in excess of \$19.5 million as of June 30, 2016.

Real Estate Owned

Once an asset is determined to be uncollectible, the underlying collateral is generally repossessed and reclassified to foreclosed real estate and repossessed assets. These repossessed assets are carried at the lower of cost or fair value of the collateral, based on independent appraisals, less cost to sell and would be categorized as Level 2 measurement. In some cases, adjustments are made to the appraised values for various factors including age of the appraisal, age of the comparable included in the appraisal, and known changes in the market and in the collateral. As a result, the evaluations are based upon unobservable inputs, and therefore, the fair value measurement has been categorized as a Level 3 measurement.

**Summary of Non-Recurring Fair Value Measurements**

At June 30, 2016 (Dollars in Thousands)				
	Level 1	Level 2	Level 3	Total
Impaired loans	\$-	\$ -	\$19,517	\$19,517
Real estate owned	-	-	207	207
Total	\$-	\$ -	\$19,724	\$19,724

At September 30, 2015 (Dollars in Thousands)				
	Level 1	Level 2	Level 3	Total
Impaired loans	\$-	\$ -	\$16,770	\$16,770
Real estate owned	-	869	-	869
Total	\$-	\$ 869	\$16,770	\$17,639

The following table provides information describing the valuation processes used to determine nonrecurring fair value measurements categorized within Level 3 of the fair value hierarchy:

At June 30, 2016 (Dollars in Thousands)				
	Fair Value	Valuation Technique	Unobservable Input	Range/ Weighted Ave.
Impaired loans	\$19,517	Property appraisals (1) (3)	Management discount for selling costs, property type and market volatility (2)	10% discount
Real estate owned	\$207	Property appraisals (1)(3)	Management discount for selling costs, property type and market volatility (2)	10% discount

At September 30, 2015 (Dollars in Thousands)				
	Fair Value	Valuation Technique	Unobservable Input	Range/ Weighted Ave.
Impaired loans	\$ 16,770	Property appraisals (1) (3)	Management discount for selling costs, property type and market volatility (2)	10% discount
Real estate owned	\$ 869	Property appraisals (1)(3)	Management discount for selling costs, property type and market volatility (2)	10% discount

(1) Fair value is generally determined through independent appraisals of the underlying collateral, which generally includes various Level 3 inputs, which are not identifiable.

Appraisals may be adjusted by management for qualitative factors such as economic conditions and estimated (2) liquidation expenses. The range and weighted average of liquidation expenses and other appraisal adjustments are presented as a percent of the appraisal.

(3) Includes qualitative adjustments by management and estimated liquidation expenses.

The fair value of financial instruments has been determined by the Company using available market information and appropriate valuation methodologies. However, considerable judgment is necessarily required to interpret market data to develop the estimates of fair value. Accordingly, the estimates presented herein are not necessarily indicative of the amounts the Company could realize in a current market exchange. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts.

	Carrying Amount	Fair Value	Fair Value Measurements at <b>June 30, 2016</b>		
			(Level 1)	(Level 2)	(Level 3)
(Dollars in Thousands)					
<b>Assets:</b>					
Cash and cash equivalents	\$38,572	\$38,572	\$38,572	\$-	\$-
Investment and mortgage-backed securities available for sale	138,683	138,683	49	138,634	-
Investment and mortgage-backed securities held to maturity	15,488	16,793	-	16,793	-
Loans receivable, net	342,459	344,478	-	-	344,478
Accrued interest receivable	1,763	1,763	1,763	-	-
Federal Home Loan Bank stock	2,387	2,387	2,387	-	-
Bank owned life insurance	12,973	12,973	12,973	-	-
<b>Liabilities:</b>					
Checking accounts	37,741	37,741	37,741	-	-
Money market deposit accounts	56,115	56,115	56,115	-	-
Passbook, club and statement savings accounts	70,767	70,767	70,767	-	-
Certificates of deposit	222,017	224,396	-	-	224,396
Advances from Federal Home Loan Bank	50,227	50,222	-	-	50,222
Accrued interest payable	1,015	1,015	1,015	-	-
Advances from borrowers for taxes and insurance	2,769	2,769	2,769	-	-
Interest rate swap contracts	351	351	-	351	-

	Carrying Amount	Fair Value	Fair Value Measurements at September 30, 2015		
			(Level 1)	(Level 2)	(Level 3)
(Dollars in Thousands)					
<b>Assets:</b>					
Cash and cash equivalents	\$ 11,272	\$ 11,272	\$ 11,272	\$ -	\$ -
Investment and mortgage-backed securities available for sale	77,483	77,483	59	77,424	-
Investment and mortgage-backed securities held to maturity	66,384	66,877	-	66,877	-
Loans receivable, net	312,633	312,613	-	-	312,613
Accrued interest receivable	1,665	1,665	1,665	-	-
Federal Home Loan Bank stock	369	369	369	-	-
Bank owned life insurance	12,722	12,722	12,722	-	-
<b>Liabilities:</b>					
Checking accounts	37,942	37,942	37,942	-	-
Money market deposit accounts	60,736	60,736	60,736	-	-
Passbook, club and statement savings accounts	70,355	70,355	70,355	-	-
Certificates of deposit	196,041	199,639	-	-	199,639
Accrued interest payable	1,291	1,291	1,291	-	-
Advances from borrowers for taxes and insurance	1,670	1,670	1,670	-	-

**Cash and Cash Equivalents**—For cash and cash equivalents, the carrying amount is a reasonable estimate of fair value.

**Investments and Mortgage-Backed Securities**—The fair value of investment securities and mortgage-backed securities is based on quoted market prices, dealer quotes, and prices obtained from independent pricing services.

**Loans Receivable**—The fair value of loans is estimated based on present value using the current market rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities. The carrying value that fair value is compared to is net of the allowance for loan losses and other associated premiums and discounts. Due to the significant judgment involved in evaluating credit quality, loans are classified within Level 3 of the fair value hierarchy.

**Accrued Interest Receivable** – For accrued interest receivable, the carrying amount is a reasonable estimate of fair value.

**Federal Home Loan Bank (FHLB) Stock**—Although FHLB stock is an equity interest in an FHLB, it is carried at cost because it does not have a readily determinable fair value as its ownership is restricted and it lacks a market. The estimated fair value approximates the carrying amount.

**Bank Owned Life Insurance**—The fair value of bank owned life insurance is based on the cash surrender value obtained from an independent advisor that is derivable from observable market inputs.

**Checking Accounts, Money Market Deposit Accounts, Passbook Accounts, Club Accounts, Statement Savings Accounts, and Certificates of Deposit**—The fair value of passbook accounts, club accounts, statement savings accounts, checking accounts, and money market deposit accounts is the amount reported in the financial statements. The fair value of certificates of deposit is based on market rates currently offered for deposits of similar remaining maturity.

**Advances from Federal Home Loan Bank**—The fair value of advances from FHLB is the amount payable on demand at the reporting date.

**Accrued Interest Payable** – For accrued interest payable, the carrying amount is a reasonable estimate of fair value.

**Interest rate swaps** – The fair values of the interest rate swap contracts are based upon the estimated amount the Company would receive or pay to terminate the contracts.

**Advances from borrowers for taxes and insurance** – For advances from borrowers for taxes and insurance, the carrying amount is a reasonable estimate of fair value.

**Commitments to Extend Credit and Letters of Credit**—The majority of the Bank’s commitments to extend credit and letters of credit carry current market interest rates if converted to loans. Because commitments to extend credit and letters of credit are generally unassignable by either the Bank or the borrower, they only have value to the Bank and the borrower. The estimated fair value approximates the recorded deferred fee amounts, which are not significant.

### **13. PENDING ACQUISITION**

On June 2, 2016, the Company entered into an Agreement and Plan of Merger (the “Merger Agreement”) with Polonia Bancorp. Pursuant to the Merger Agreement, Polonia Bancorp will merge with and into the Company (the “Merger”) and Polonia Bancorp’s wholly owned subsidiary, Polonia Bank, a federally chartered savings bank, will merge with and into the Bank.

Pursuant to the Merger Agreement, at the effective time of the Merger, each outstanding share of Polonia Bancorp common stock will be converted into the right to receive, at the election of the Polonia Bancorp shareholder (subject to certain conditions, including conditions relating to pro-ration): (i) 0.7591 of a share of Company common stock (the “Exchange Ratio”) or (ii) \$11.28 in cash (the “Per Share Cash Consideration” and collectively with the Exchange Ratio, the “Merger Consideration”). The election of shares of Company stock or cash will be subject to pro-ration such that 50% of the issued and outstanding shares of Polonia Bancorp common stock will be exchanged for Company common stock and 50% will be exchanged for cash. Options to purchase Polonia Bancorp common stock outstanding at the effective time of the Merger will fully vest and be exchanged for a cash payment equal to the difference, if positive, between the Per Share Cash Consideration under the Merger Agreement and the corresponding exercise price of such option.

The Merger Consideration is subject to adjustment in certain limited situations. In the event that Polonia Bancorp Consolidated Stockholders' Equity, as calculated in accordance with the terms of the Merger Agreement, is less than \$37.4 million as of the Final Statement Date, as defined in the Merger Agreement, then the Exchange Ratio and the Per Share Cash Consideration will be adjusted downward to reflect the amount of the difference between \$37.4 million and the Polonia Bancorp Consolidated Stockholders' Equity. The Merger Consideration is subject to potential upward adjustment to reflect the after-tax impact of certain recoveries experienced by Polonia Bancorp, if any, achieved prior to the Final Statement Date as specified in the Merger Agreement. In such situation, the Exchange Ratio and the Per Share Cash Consideration, as they may have been adjusted downward as noted above, will be correspondingly adjusted to reflect the amount of such after-tax recoveries.

Consummation of the Merger is subject to customary closing conditions, including, without limitation, the approval of the Merger Agreement by the Polonia Bancorp shareholders by the requisite shareholder vote and the receipt of all required regulatory approvals.



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

The following discussion should be read in conjunction with our unaudited consolidated financial statements included elsewhere in this Form 10-Q and with our Annual Report on Form 10-K for the year ended September 30, 2015 (the "Form 10-K").

**Overview.** Prudential Bancorp, Inc. (the "Company") was formed by Prudential Bancorp, Inc. of Pennsylvania to become the successor holding company for Prudential Savings Bank (the "Bank") as a result of the second-step conversion completed in October 2013. The Company's results of operations are primarily dependent on the results of the Bank, which is a wholly owned subsidiary of the Company. The Company's results of operations depend to a large extent on net interest income, which primarily is the difference between the income earned on its loan and securities portfolios and the cost of funds, which is the interest paid on deposits and borrowings. Results of operations are also affected by our provisions for loan losses, non-interest income (which includes impairment charges) and non-interest expense. Non-interest expense principally consists of salaries and employee benefits, office occupancy expense, depreciation, data processing expense, payroll taxes and other expense. Our results of operations are also significantly affected by general economic and competitive conditions, particularly changes in interest rates, government policies and actions of regulatory authorities. Future changes in applicable laws, regulations or government policies may materially impact our financial condition and results of operations. The Bank is subject to regulation by the Federal Deposit Insurance Corporation (the "FDIC") and the Pennsylvania Department of Banking and Securities (the "Department"). The Bank's main office is in Philadelphia, Pennsylvania, with five additional full-service banking offices located in Philadelphia and Delaware Counties in Pennsylvania. The Bank's primary business consists of attracting deposits from the general public and using those funds together with borrowings to originate loans and to invest primarily in U.S. Government and agency securities and mortgage-backed securities. In November 2005, the Bank formed PSB Delaware, Inc., a Delaware corporation, as a subsidiary of the Bank. In March 2006, all mortgage-backed securities then owned by the Company's predecessor were transferred to PSB Delaware, Inc. PSB Delaware, Inc.'s activities are included as part of the consolidated financial statements.

**Critical Accounting Policies.** In reviewing and understanding financial information for the Company, you are encouraged to read and understand the significant accounting policies used in preparing our financial statements. These policies are described in Note 1 of the notes to our unaudited consolidated financial statements included in Item 1 hereof as well as in Note 2 to our audited consolidated financial statements included in the Form 10-K. The accounting and financial reporting policies of the Company conform to accounting principles generally accepted in the United States of America ("U.S. GAAP") and to general practices within the banking industry. Accordingly, the financial statements require certain estimates, judgments and assumptions, which are believed to be reasonable, based upon the information available. These estimates and assumptions affect the reported amounts of assets and liabilities as well as contingent assets and contingent liabilities at the date of the financial statements and the reported amounts of income and expenses during the periods presented. The following accounting policies comprise those that management believes are the most critical to aid in fully understanding and evaluating our reported financial results. These policies require numerous estimates or economic assumptions that may prove inaccurate or may be subject to variations which may significantly affect our reported results and financial condition for the period or in future

periods.

*Allowance for Loan Losses.* The allowance for loan losses is established through a provision for loan losses charged to expense. Losses are charged against the allowance for loan losses when management believes that the collectability in full of the principal of a loan is unlikely. Subsequent recoveries are added to the allowance. The allowance for loan losses is maintained at a level that management considers adequate to provide for estimated losses and impairments based upon an evaluation of known and inherent losses in the loan portfolio that are both probable and reasonable to estimate. Loan impairment is evaluated based on the fair value of collateral or estimated net realizable value. It is the policy of management to provide for losses on unidentified loans in its portfolio in addition to criticized and classified loans.

Management monitors its allowance for loan losses at least quarterly and makes adjustments to the allowance through the provision for loan losses as economic conditions and other pertinent factors indicate. The quarterly review and adjustment of the qualitative factors employed in the allowance methodology and the updating of historic loss experience allow for timely reaction to emerging conditions and trends. In this context, a series of qualitative factors are used in a methodology as a measurement of how current circumstances are affecting the loan portfolio. Included in these qualitative factors are:

- Levels of past due, classified, criticized and non-accrual loans, troubled debt restructurings and loan modifications;
  - Nature and volume of loans;
- Changes in lending policies and procedures, underwriting standards, collections, charge-offs and recoveries and for commercial loans, the level of loans being approved with exceptions to the Bank's lending policy;
  - Experience, ability and depth of management and staff;
  - National and local economic and business conditions, including various market segments;
  - Quality of the Company's loan review system and the degree of Board oversight;
  - Concentrations of credit and changes in levels of such concentrations; and
  - Effect of external factors on the level of estimated credit losses in the current portfolio.

In determining the allowance for loan losses, management has established a general pooled allowance. Values assigned to the qualitative factors and those developed from historic loss experience provide a dynamic basis for the calculation of reserve factors for both pass-rated loans (the general pooled allowance) and those for criticized and classified loans. The amount of the specific allowance is determined through a loan-by-loan analysis of certain large dollar commercial real estate loans, construction and land development loans and multi-family loans. Loans not individually reviewed are evaluated as a group using reserve factor percentages based on historical loss experience and the qualitative factors described above. In determining the appropriate level of the general pooled allowance, management makes estimates based on internal risk ratings, which take into account such factors as debt service coverage, loan-to-value ratios and external factors. Estimates are periodically measured against actual loss experience.

This evaluation is inherently subjective as it requires material estimates including, among others, exposure at default, the amount and timing of expected future cash flows on impaired loans, value of collateral, estimated losses on our commercial, construction and residential loan portfolios and historical loss experience. All of these estimates may be susceptible to significant change.

While management uses the best information available to make loan loss allowance evaluations, adjustments to the allowance may be necessary based on changes in economic and other conditions or changes in accounting guidance. In addition, the Department and the FDIC, as an integral part of their examination processes, periodically review our allowance for loan losses. The Department and the FDIC may require the recognition of adjustments to the allowance for loan losses based on their judgment of information available to them at the time of their examination. To the extent that actual outcomes differ from management's estimates, additional provisions to the allowance for loan losses may be required that would adversely affect earnings in future periods.

*Investment and mortgage-backed securities available for sale.* Where quoted prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. If quoted market prices are not available, then fair values are estimated using quoted prices of securities with similar characteristics or discounted cash flows and are classified within Level 2 of the fair value hierarchy. In certain cases where there is limited activity or less transparency around inputs to the valuation, securities are classified within Level 3 of the valuation hierarchy, although there were no securities with that classification as of June 30, 2016 or September 30, 2015.

Management evaluates securities for other-than-temporary impairment at least on a quarterly basis, and more frequently when economic or market concerns warrant such evaluation. The Company determines whether the unrealized losses are temporary or not in accordance with U.S. GAAP. The evaluation is based upon factors such as the creditworthiness of the issuers/guarantors, the underlying collateral, if applicable, and the continuing performance of the securities. In addition, the Company also considers the likelihood that the security will be required to be sold because of regulatory concerns, our internal intent not to dispose of the security prior to maturity and whether the entire cost basis of the security is expected to be recovered. In determining whether the cost basis will be recovered, management evaluates other facts and circumstances that may be indicative of an “other-than-temporary” impairment condition. This includes, but is not limited to, an evaluation of the type of security, length of time and extent to which the fair value has been less than cost, and near-term prospects of the issuer.

In addition, certain assets are measured at fair value on a non-recurring basis; that is, the instruments are not measured at fair value on an ongoing basis but are subject to fair value adjustments in certain circumstances (for example, when there is evidence of impairment). The Company measures impaired loans and investment securities, both available-for-sale (“AFS”) and held-to-maturity (“HTM”), at fair value on a non-recurring basis.

Valuation techniques and models utilized for measuring financial assets and liabilities are reviewed and validated by the Company at least quarterly.

*Income Taxes.* The Company accounts for income taxes in accordance with U.S. GAAP. The Company records deferred income taxes that reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Management exercises significant judgment in the evaluation of the amount and timing of the recognition of the resulting tax assets and liabilities. The judgments and estimates required for the evaluation are updated based upon changes in business factors and the tax laws. If actual results differ from the assumptions and other considerations used in estimating the amount and timing of tax recognized, there can be no assurance that additional expenses will not be required in future periods.

In evaluating our ability to recover deferred tax assets, we consider all available positive and negative evidence, including our past operating results and our forecast of future taxable income. In determining future taxable income, we make assumptions for the amount of taxable income, the reversal of temporary differences and the implementation of feasible and prudent tax planning strategies. These assumptions require us to make judgments about our future taxable income and are consistent with the plans and estimates we use to manage our business. Any reduction in estimated future taxable income may require us to record an additional valuation allowance against our deferred tax assets. An increase in the valuation allowance would result in additional income tax expense in the period and could have a significant impact on our future earnings.

U.S. GAAP prescribes a minimum probability threshold that a tax position must meet before a financial statement benefit is recognized. The Company recognizes, when applicable, interest and penalties related to unrecognized tax benefits in the provision for income taxes in the consolidated income statement. Assessment of uncertain tax positions requires careful consideration of the technical merits of a position based on management’s analysis of tax regulations and interpretations. Significant judgment may be involved in the assessment of the tax position.

**Forward-looking Statements.** This Quarterly Report on Form 10-Q contains “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. These statements include, but are not limited to, expectations or predictions of future financial or business performance, conditions relating to the Company and Polonia Bancorp, or other effects of the proposed merger of the Company and Polonia Bancorp. These forward-looking statements include statements with respect to the Company’s beliefs, plans, objectives, goals,

expectations, anticipations, estimates and intentions, that are subject to significant risks and uncertainties, and are subject to change based on various factors (some of which are beyond the Company's control). The words "may," "could," "should," "would," "will," "believe," "anticipate," "estimate," "expect," "intend," "plan" and similar expressions are intended forward-looking statements.

In addition to factors previously disclosed in the reports filed by the Company with the Securities and Exchange commission (“SEC”) and those identified elsewhere in this Form 10-Q, the following factors, among others, could cause actual results to differ materially from forward looking statements or historical performance: the ability to obtain regulatory approvals and satisfy other closing conditions to the merger, including approval by shareholders of Polonia; delay in closing the merger; difficulties and delays in integrating the Polonia business or fully realizing anticipated cost savings and other benefits of the merger; business disruptions following the merger; the strength of the United States economy in general and the strength of the local economies in which the Company and Polonia conduct their operations; general economic conditions; legislative and regulatory changes; monetary and fiscal policies of the federal government; changes in tax policies, rates and regulations of federal, state and local tax authorities; changes in interest rates, deposit flows, the cost of funds, demand for loan products, demand for financial services, competition, changes in the quality or composition of the Company’s loan, investment and mortgage-backed securities portfolios; changes in accounting principles, policies or guidelines and other economic, competitive, governmental and technological factors affecting the Company’s operations, markets, products, services and fees; and the success of the Company at managing the risks involved in the foregoing.

The Company does not undertake to update any forward-looking statement, whether written or oral, that may be made from time to time by or on behalf of the Company to reflect events or circumstances occurring after the date of this Form 10-Q.

For a complete discussion of the assumptions, risks and uncertainties related to our business, readers are encouraged to review the Company’s filings with the SEC, including the “Risk Factors” section in the Company’s most recent Annual Report on Form 10-K, as supplemented by its quarterly or other reports subsequently filed with the SEC.

**Market Overview.** Although the economy slowly improved during 2015 and 2016, we still view the current environment as challenging.

The Company continues to focus on the credit quality of its customers, closely monitoring the financial status of borrowers throughout the Company’s markets, gathering information, working on early detection of potential problems, taking pre-emptive steps where necessary and performing the analysis required to maintain adequate reserves for loan losses.

Despite the current market and economic conditions, the Company continues to maintain capital well in excess of regulatory requirements.

The following discussion provides further details on the financial condition of the Company at June 30, 2016 and September 30, 2015, and the results of operations for the three and nine months ended June 30, 2016 and 2015.

#### **COMPARISON OF FINANCIAL CONDITION AT JUNE 30, 2016 AND SEPTEMBER 30, 2015**

At June 30, 2016, the Company had total assets of \$556.3 million, as compared to \$487.2 million at September 30, 2015, an increase of 14.2%. Cash and cash equivalents increased \$27.3 million to \$38.6 million at June 30, 2016, compared to \$11.3 million at September 30, 2015, due to maintaining sufficient liquid assets to fund the cash portion of the merger consideration in the previously assumed pending merger with Polonia Bancorp, Inc. (“Polonia Bancorp”). At June 30, 2016, net loans receivable increased to \$342.5 million from \$312.6 million at September 30, 2015. The increase in net loans receivable was primarily due to a \$42.8 million increase in commercial real estate loans, partially offset by a \$21.4 million reduction in the balance of one-to-four family loans and construction and land development loans. During this nine-month period, the Company increased its available-for-sale investment portfolio by \$61.2 million, while experiencing a \$50.9 million reduction in investment securities held-to-maturity, primarily due to securities being called. As part of the growth of the investment securities portfolio pursuant to an investment leverage strategy, the Company purchased \$15.0 million of mortgage-backed securities and \$10.0 million of corporate securities, funding the purchase with mix-termed FHLB advances.

Total liabilities increased by \$73.0 million to \$443.2 million at June 30, 2016 from \$370.2 million at September 30, 2015. Total deposits increased \$21.6 million primarily in short-term certificate of deposits. At June 30, 2016, the Company maintained FHLB advances of \$50.2 million with variable maturities of which \$35.0 million was \$25.0 million was used to fund the Company’s investment leverage strategy noted above.



Total stockholders' equity decreased by \$3.9 million to \$113.1 million at June 30, 2016 from \$117.0 million at September 30, 2015. The decrease was primarily due to the \$7.8 million expended in the acquisition of treasury stock in connection with the Company's previously announced stock repurchase program. As of June 30, 2016, the Company had repurchased 665,733 shares under its current program leaving 184,267 shares remaining; only limited repurchases have been effected since early March 2016 due to the pending merger with Polonia Bancorp. This decrease was partially offset by \$1.7 million in net income during the nine months ended June 30, 2016 combined with a \$914,000 after-tax increase in the unrealized gain on the available-for-sale securities portfolio and the fair value of interest rate swaps.

### **COMPARISON OF RESULTS OF OPERATIONS FOR THE THREE AND NINE MONTHS ENDED JUNE 30, 2016 AND 2015**

**Net income.** The Company recognized net income of 777,000, or \$0.10 per basic share and per diluted share, for the quarter ended June 30, 2016 as compared to \$47,000, or \$0.01 per basic and diluted share, for the same quarter in 2015. For the nine months ended June 30, 2016, the Company recognized net income of \$1.7 million or \$0.23 per basic and per diluted share, as compared to net income of \$2.2 million, or \$0.26 per basic share and per diluted share, for the comparable period in 2015. The three and nine months ended June 30, 2015 included onetime gains on sale of real estate of \$231,000 and \$2.0 million, respectively, related to the sale of two branch offices.

**Net interest income.** For the three months ended June 30, 2016, net interest income increased to \$3.7 million as compared to \$3.2 million for the same period in 2015. The increase reflected a \$419,000 or 10.3% increase in interest income combined with a decrease of \$27,000 or 3.2% in interest paid on deposits and borrowings. The Company increased borrowings from the FHLB during the third quarter of fiscal 2016 in connection with the implementation of its previously announced leverage strategy (initially implemented in the prior quarter) to increase the level of its earning assets. During the quarter ended June 30, 2016, the Company had an average balance of borrowings of \$44.2 million with a weighted average cost of 1.30%, an increase of \$44.0 million from the average balance of borrowings during the same period in 2015. The total weighted average cost of funds decreased 11 basis points to 0.78% for the June 30, 2016 quarter, from 0.89% for the same period in 2015.

For the nine months ended June 30, 2016, net interest income increased to \$10.4 million as compared to \$10.0 million for the same period in 2015. The increase reflected a \$297,000 or 2.4% increase in interest income combined with a decrease of \$150,000 or 5.7% in interest paid on deposits and borrowings. The Company's borrowings from the FHLB also increased during the nine months ended June 30, 2016 in connection with the leverage strategy implemented during the second quarter of fiscal 2016. The Company had an average balance of borrowings of \$30.2 million with a weighted average yield of 1.30% during the nine months ended June 30, 2016, an increase of \$30.0 million from the level of average borrowings during the same period in 2015. The total weighted average cost of funds decreased 10 basis points to 0.81% for the same months ended June 30, 2016, from 0.91% for the same period in 2015.

For the three months ended June 30, 2016, the net interest margin was 2.81% compared to 2.65% for the same period in fiscal 2015. For the nine months ended June 30, 2016, the net interest margin was 2.74% as compared to 2.67% for the same period in 2015. The net interest margin increased during the first nine months of fiscal 2016 primarily due to the results of the Company's efforts in reducing its overall cost of funds.

**Average balances, net interest income, and yields earned and rates paid.** The following table shows for the periods indicated the total dollar amount of interest earned from average interest-earning assets and the resulting yields, as well as the interest expense on average interest-bearing liabilities and the resulting costs, expressed both in dollars and rates, the interest rate spread and the net interest margin. Average yields and rates have been annualized. Tax-exempt income and yields have not been adjusted to a tax-equivalent basis. All average balances are based on monthly balances. Management does not believe that the monthly averages differ significantly from what the daily averages would be.

	Three Months Ended June 30, 2016			2015			Average Yield/Rate (1)		
	Average Balance	Interest	Average Yield/Rate (1)	Average Balance	Interest	Average Yield/Rate (1)			
	(Dollars in Thousands)								
Interest-earning assets:									
Investment securities	\$51,070	\$529	2.91	% \$77,804	\$487	2.51	%		
Mortgage-backed securities	129,557	673	2.62	65,198	465	2.86			
Loans receivable(2)	334,410	3,263	3.96	320,877	3,085	3.86			
Other interest-earning assets	12,450	9	0.29	27,134	18	0.28			
Total interest-earning assets	527,487	4,474	3.44	491,013	4,055	3.31			
Cash and non interest-bearing balances	1,781			2,009					
Other non interest-earning assets	20,950			21,111					
Total assets	\$550,218			\$514,133					
Interest-bearing liabilities:									
Savings accounts	\$73,031	18	0.10	\$75,673	52	0.28			
Money market deposit and NOW accounts	91,884	34	0.15	97,171	83	0.34			
Certificates of deposit	218,857	629	1.17	206,422	715	1.39			
Total deposits	383,772	681	0.72	379,266	850	0.91			
Advances from Federal Home Loan Bank	44,200	142	1.30	221	-	0.00			
Advances from borrowers for taxes and insurance	2,131	1	0.19	2,300	1	0.18			
Total interest-bearing liabilities	430,103	824	0.78	381,787	851	0.90			
Non interest-bearing liabilities:									
Non interest-bearing demand accounts	2,795			2,129					
Other liabilities	1,752			2,662					
Total liabilities	434,650			386,578					
Stockholders' equity	115,568			127,555					
Total liabilities and stockholders' equity	\$550,218			\$514,133					
Net interest-earning assets	\$97,384			\$109,226					
Net interest income; interest rate spread		\$3,650	2.66	%	\$3,204	2.41	%		
Net interest margin(3)			2.81	%		2.62	%		
Average interest-earning assets to average interest-bearing liabilities			122.64%			128.61%			

(1) Yields and rates for the three month periods are annualized.

(2) Includes non-accrual loans. Calculated net of unamortized deferred fees, undisbursed portion of loans-in-process and the allowance for loan losses.

(3) Equals net interest income divided by average interest-earning assets.



	Nine Months Ended June 30, 2016			2015			Average Yield/Rate (1)		
	Average Balance	Interest	Average Yield/Rate (1)	Average Balance	Interest	Average Yield/Rate (1)			
	(Dollars in Thousands)								
Interest-earning assets:									
Investment securities	\$60,356	\$1,517	2.69	% \$82,797	\$1,587	2.56	%		
Mortgage-backed securities	111,126	1,868	2.59	59,291	1,331	3.00			
Loans receivable(2)	323,830	9,489	3.90	325,782	9,629	3.95			
Other interest-earning assets	10,511	22	0.28	31,539	52	0.22			
Total interest-earning assets	505,823	12,896	3.40	499,409	12,599	3.37			
Cash and non interest-bearing balances	1,887			2,164					
Other non interest-earning assets	19,929			19,193					
Total assets	\$527,639			\$520,766					
Interest-bearing liabilities:									
Savings accounts	\$72,786	65	0.12	\$75,662	161	0.28			
Money market deposit and NOW accounts	91,928	129	0.19	99,318	257	0.35			
Certificates of deposit	208,560	1,981	1.27	210,089	2,202	1.40			
Total deposits	373,274	2,175	0.78	385,069	2,620	0.91			
Advances from Federal Home Loan Bank	30,245	296	1.30	217	-	0.00			
Advances from borrowers for taxes and insurance	1,971	2	0.14	2,057	3	0.19			
Total interest-bearing liabilities	405,490	2,473	0.81	387,343	2,623	0.91			
Non interest-bearing liabilities:									
Non interest-bearing demand accounts	2,724			2,247					
Other liabilities	3,661			3,089					
Total liabilities	411,875			392,679					
Stockholders' equity	115,764			128,087					
Total liabilities and stockholders' equity	\$527,639			\$520,766					
Net interest-earning assets	\$100,333			\$112,066					
Net interest income; interest rate spread		\$10,423	2.58	%	\$9,976	2.47	%		
Net interest margin(3)			2.74	%		2.67	%		
Average interest-earning assets to average interest-bearing liabilities			125.44%			128.93%			