

WSFS FINANCIAL CORP  
Form 10-Q  
November 12, 2013  
Table of Contents

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 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 September 30, 2013

OR

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

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

Commission File Number 0-16668

**WSFS FINANCIAL CORPORATION**

(Exact name of registrant as specified in its charter)

Edgar Filing: WSFS FINANCIAL CORP - Form 10-Q

**Delaware**  
(State or other jurisdiction of

**22-2866913**  
(I.R.S. Employer

**Incorporation or organization)**

**Identification Number)**

**WSFS Bank Center, 500 Delaware**

**Avenue, Wilmington, Delaware**  
(Address of principal executive offices)

**19801**  
(Zip Code)

**(302) 792-6000**

**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 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 a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer  Accelerated filer   
Non-accelerated filer  (Do not check if 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 November 1, 2013

**Common Stock, par value \$.01 per share**  
(Title of Class)

**8,850,368**  
(Shares Outstanding)

**Table of Contents**

**WSFS FINANCIAL CORPORATION**

**FORM 10-Q**

**INDEX**

|                                      | Page   |
|--------------------------------------|--|
| <b>PART I. Financial Information</b> |  |
| Item 1.                              | Financial Statements (Unaudited)   |
|                                      | <u>Consolidated Statements of Operations for the Three and Nine Months Ended September 30, 2013 and 2012</u>           |
|                                      | 3  |
|                                      | <u>Consolidated Statements of Comprehensive Income for the Three and Nine Months Ended September 30, 2013 and 2012</u> |
|                                      | 4  |
|                                      | <u>Consolidated Statements of Condition as of September 30, 2013 and December 31, 2012</u>                             |
|                                      | 5  |
|                                      | <u>Consolidated Statements of Cash Flows for the Nine Months Ended September 30, 2013 and 2012</u>                     |
|                                      | 6  |
|                                      | <u>Notes to the Consolidated Financial Statements for the Three and Nine Months Ended September 30, 2013 and 2012</u>  |
|                                      | 7  |
| Item 2.                              | <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>                           |
|                                      | 37   |
| Item 3.                              | <u>Quantitative and Qualitative Disclosures About Market Risk</u>  |
|                                      | 50   |
| Item 4.                              | <u>Controls and Procedures</u>   |
|                                      | 50   |
| <b>PART II. Other Information</b>    |  |
| Item 1.                              | <u>Legal Proceedings</u>   |
|                                      | 50   |
| Item 1A.                             | <u>Risk Factors</u>  |
|                                      | 50   |
| Item 2.                              | <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>   |
|                                      | 51   |
| Item 3.                              | <u>Defaults upon Senior Securities</u>   |
|                                      | 51   |
| Item 4.                              | <u>Mine Safety Disclosure</u>  |
|                                      | 51   |
| Item 5.                              | <u>Other Information</u>   |
|                                      | 51   |
| Item 6.                              | <u>Exhibits</u>  |
|                                      | 51   |
|                                      | <u>Signatures</u>  |
|                                      | 52   |
| Exhibit 31.1                         | Certification of CEO Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002   |
| Exhibit 31.2                         | Certification of CFO Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002   |
| Exhibit 32                           | Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002  |
| Exhibit 101.INS                      | Instance Document  |
| Exhibit 101.SCH                      | Schema Document  |
| Exhibit 101.CAL                      | Calculation Linkbase Document  |
| Exhibit 101.LAB                      | Labels Linkbase Document   |
| Exhibit 101.PRE                      | Presentation Linkbase Document   |
| Exhibit 101.DEF                      | Definition Linkbase Document   |

**Table of Contents**

**WSFS FINANCIAL CORPORATION**  
**CONSOLIDATED STATEMENTS OF OPERATIONS**

Three Months Ended September 30, 2013  
2012  
2013  
2012  
(Unaudited)

(In Thousands, Except Per Share Data)

|  | 2013          | 2012          | 2013           | 2012           |
|--|---------------|---------------|----------------|----------------|
| <b>Interest income:</b>  |               |               |                |                |
| Interest and fees on loans   | \$ 32,708     | \$ 32,003     | \$ 96,268      | \$ 98,185      |
| Interest on mortgage-backed securities   | 3,527         | 4,344         | 10,726         | 14,953         |
| Interest on reverse mortgages  | 248           | 35            | 462            | (41)           |
| Interest and dividends on investment securities  | 546           | 123           | 999            | 376            |
| Other interest income  | 87            | 9             | 134            | 27             |
|  | <b>37,116</b> | <b>36,514</b> | <b>108,589</b> | <b>113,500</b> |
| <b>Interest expense:</b>   |               |               |                |                |
| Interest on deposits   | 1,673         | 3,237         | 5,513          | 10,652         |
| Interest on Federal Home Loan Bank advances  | 482           | 1,403         | 1,376          | 4,985          |
| Interest on federal funds purchased and securities sold under agreements to repurchase | 244           | 253           | 738            | 765            |
| Interest on trust preferred borrowings   | 339           | 369           | 1,005          | 1,114          |
| Interest on senior debt  | 943           | 353           | 2,830          | 353            |
| Interest on other borrowings   | 29            | 6             | 85             | 130            |
|  | <b>3,710</b>  | <b>5,621</b>  | <b>11,547</b>  | <b>17,999</b>  |
| Net interest income  | <b>33,406</b> | <b>30,893</b> | <b>97,042</b>  | <b>95,501</b>  |
| Provision for loan losses  | <b>1,969</b>  | <b>3,751</b>  | <b>5,880</b>   | <b>28,379</b>  |
| Net interest income after provision for loan losses                                    | <b>31,437</b> | <b>27,142</b> | <b>91,162</b>  | <b>67,122</b>  |
| <b>Noninterest income:</b>   |               |               |                |                |
| Credit/debit card and ATM income   | 6,374         | 5,738         | 18,231         | 17,031         |
| Deposit service charges  | 4,407         | 4,360         | 12,637         | 12,673         |
| Investment management and fiduciary revenue  | 3,836         | 3,258         | 11,623         | 9,716          |
| Reverse mortgage consolidation gain  | 3,801         |               | 3,801          |                |
| Mortgage banking activities, net   | 907           | 914           | 2,837          | 1,882          |
| Loan fee income  | 419           | 706           | 1,401          | 1,803          |
| Security gains, net  | 306           | 2,451         | 2,856          | 17,797         |
| Bank owned life insurance income   | 74            | 1,126         | 162            | 1,447          |
| Other income   | 2,618         | 1,195         | 6,807          | 3,149          |
|  | <b>22,742</b> | <b>19,748</b> | <b>60,355</b>  | <b>65,498</b>  |
| <b>Noninterest expenses:</b>   |               |               |                |                |
| Salaries, benefits and other compensation  | 17,648        | 16,942        | 53,086         | 49,840         |
| Occupancy expense  | 3,385         | 3,235         | 10,169         | 9,697          |
| Equipment expense  | 2,044         | 1,701         | 5,990          | 5,403          |
| Data processing and operations expenses  | 1,548         | 1,402         | 4,291          | 4,190          |
| FDIC expenses  | 959           | 1,384         | 3,067          | 4,262          |
| Professional fees  | 866           | 671           | 2,712          | 2,917          |

Edgar Filing: WSFS FINANCIAL CORP - Form 10-Q

|  |                  |                 |                  |                  |
|--|------------------|-----------------|------------------|------------------|
| Marketing expense                                      | 643              | 379             | 1,768            | 1,976            |
| Loan workout and OREO expenses                         | 492              | 2,115           | 1,432            | 4,902            |
| Other operating expense                                | 5,224            | 4,324           | 15,816           | 12,972           |
|  | 32,809           | 32,153          | 98,331           | 96,159           |
| Income before taxes                                    | 21,370           | 14,737          | 53,186           | 36,461           |
| Income tax provision                                   | 7,210            | 4,758           | 18,378           | 12,708           |
| <b>Net income</b>                                      | <b>14,160</b>    | <b>9,979</b>    | <b>34,808</b>    | <b>23,753</b>    |
| Dividends on preferred stock and accretion of discount | 332              | 693             | 1,633            | 2,077            |
| <b>Net income allocable to common stockholders</b>     | <b>\$ 13,828</b> | <b>\$ 9,286</b> | <b>\$ 33,175</b> | <b>\$ 21,676</b> |
| <b>Earnings per share:</b>                             |                  |                 |                  |                  |
| Basic  | \$ 1.57          | \$ 1.07         | \$ 3.77          | \$ 2.49          |
| Diluted  | \$ 1.54          | \$ 1.06         | \$ 3.72          | \$ 2.47          |

The accompanying notes are an integral part of these Consolidated Financial Statements.

Table of Contents

## WSFS FINANCIAL CORPORATION

## CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

|  | Three Months Ended<br>September 30,<br><b>2013</b> |           | Nine Months Ended<br>September 30,<br><b>2013</b> |           |
|--|--|-----------|---|-----------|
|  | 2012   | 2012      | 2012  | 2012      |
|  | (Unaudited)  |           | (Unaudited)                                       |           |
|  | (In Thousands)                                     |           | (In Thousands)                                    |           |
| Net Income   | <b>\$ 14,160</b>                                   | \$ 9,979  | <b>\$ 34,808</b>                                  | \$ 23,753 |
| Other comprehensive (loss) income:                           |  |           |   |           |
| Unrealized (losses) gains on securities available-for-sale   | <b>(4,901)</b>                                     | 15,341    | <b>(43,781)</b>                                   | 27,605    |
| Tax benefit (expense)  | <b>1,795</b>                                       | (5,783)   | <b>16,532</b>                                     | (10,440)  |
| Net of tax amount  | <b>(3,106)</b>                                     | 9,558     | <b>(27,249)</b>                                   | 17,165    |
| Reclassification adjustment for gains included in net income | <b>(306)</b>                                       | (2,451)   | <b>(2,856)</b>                                    | (17,797)  |
| Tax expense  | <b>116</b>   | 931       | <b>1,085</b>                                      | 6,763     |
| Net of tax amount  | <b>(190)</b>                                       | (1,520)   | <b>(1,771)</b>                                    | (11,034)  |
| Total other comprehensive (loss) income                      | <b>(3,296)</b>                                     | 8,038     | <b>(29,020)</b>                                   | 6,131     |
| Total comprehensive income                                   | <b>\$ 10,864</b>                                   | \$ 18,017 | <b>\$ 5,788</b>                                   | \$ 29,884 |

The accompanying notes are an integral part of these Consolidated Financial Statements.

**Table of Contents**

**WSFS FINANCIAL CORPORATION**  
**CONSOLIDATED STATEMENTS OF CONDITION**

|   | September 30,<br>2013                 | December 31,<br>2012 |
|---|---------------------------------------|----------------------|
|   | (Unaudited)                           |                      |
|   | (In Thousands, Except Per Share Data) |                      |
| <b>Assets</b>   |                                       |                      |
| Cash and due from banks   | \$ 96,021                             | \$ 93,629            |
| Cash in non-owned ATMs  | 406,227                               | 406,627              |
| Interest-bearing deposits in other banks  | 197                                   | 631                  |
| <b>Total cash and cash equivalents</b>  | <b>502,445</b>                        | 500,887              |
| Investment securities, available-for-sale   | 806,926                               | 907,955              |
| Investment securities, trading  |                                       | 12,590               |
| Loans held-for-sale   | 12,608                                | 12,758               |
| Loans, net of allowance for loan losses of \$41,431 at September 30, 2013 and \$43,922 at December 31, 2012 | 2,829,992                             | 2,723,916            |
| Reverse mortgage loans  | 40,095                                | (457)                |
| Bank-owned life insurance   | 63,077                                | 62,915               |
| Stock in Federal Home Loan Bank of Pittsburgh, at cost  | 33,876                                | 31,165               |
| Assets acquired through foreclosure   | 7,163                                 | 4,622                |
| Accrued interest receivable   | 9,833                                 | 9,652                |
| Premises and equipment  | 36,001                                | 38,257               |
| Goodwill  | 32,395                                | 28,146               |
| Intangible assets   | 7,146                                 | 5,174                |
| Other assets  | 61,099                                | 37,568               |
| <b>Total assets</b>   | <b>\$ 4,442,656</b>                   | <b>\$ 4,375,148</b>  |
| <b>Liabilities and Stockholders Equity</b>  |                                       |                      |
| <b>Liabilities:</b>   |                                       |                      |
| Deposits:   |                                       |                      |
| Noninterest-bearing demand  | \$ 609,115                            | \$ 631,026           |
| Interest-bearing demand   | 669,173                               | 538,195              |
| Money market  | 780,753                               | 933,901              |
| Savings   | 378,397                               | 389,977              |
| Time  | 256,397                               | 316,986              |
| Jumbo certificates of deposit - customer  | 251,764                               | 294,237              |
| <b>Total customer deposits</b>  | <b>2,945,599</b>                      | <b>3,104,322</b>     |
| Brokered deposits   | 175,599                               | 170,641              |
| <b>Total deposits</b>   | <b>3,121,198</b>                      | <b>3,274,963</b>     |
| Federal funds purchased and securities sold under agreements to repurchase                                  | 114,000                               | 110,000              |
| Federal Home Loan Bank advances   | 600,435                               | 376,310              |
| Trust preferred borrowings  | 67,011                                | 67,011               |
| Senior debt   | 55,000                                | 55,000               |
| Other borrowed funds  | 38,169                                | 28,945               |
| Bonds payable   | 26,340                                |                      |
| Accrued interest payable  | 3,254                                 | 1,099                |
| Other liabilities   | 43,298                                | 40,766               |

Edgar Filing: WSFS FINANCIAL CORP - Form 10-Q

|   |                     |              |
|---|---------------------|--------------|
| <b>Total liabilities</b>  | <b>4,068,705</b>    | 3,954,094    |
| <b>Stockholders Equity:</b>   |                     |              |
| Serial preferred stock \$0.01 par value, 7,500,000 shares authorized; issued 0 at September 30, 2013 and 52,625 issued at December 31, 2012 | \$                  | \$ 1         |
| Common stock \$0.01 par value, 20,000,000 shares authorized; issued 18,425,025 at September 30, 2013 and 18,354,055 at December 31, 2012    | <b>184</b>          | 184          |
| Capital in excess of par value  | <b>175,176</b>      | 222,978      |
| Accumulated other comprehensive (loss) / income   | <b>(16,077)</b>     | 12,943       |
| Retained earnings   | <b>462,948</b>      | 433,228      |
| Treasury stock at cost, 9,580,569 shares at September 30, 2013 and December 31, 2012  | <b>(248,280)</b>    | (248,280)    |
| <b>Total stockholders equity</b>  | <b>373,951</b>      | 421,054      |
| <b>Total liabilities and stockholders equity</b>  | <b>\$ 4,442,656</b> | \$ 4,375,148 |

The accompanying notes are an integral part of these Consolidated Financial Statements.



**Table of Contents**

**WSFS FINANCIAL CORPORATION**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**

|  | Nine months ended<br>September 30, |                    |
|--|------------------------------------|--------------------|
|  | 2013                               | 2012               |
|  | (Unaudited)                        |                    |
|  | (In Thousands)                     |                    |
| <b>Operating activities:</b>   |                                    |                    |
| Net Income   | \$ 34,808                          | \$ 23,753          |
| Adjustments to reconcile net income to net cash provided by operating activities:  |                                    |                    |
| Provision for loan losses  | 5,880                              | 28,379             |
| Depreciation of premises and equipment   | 4,329                              | 3,803              |
| Amortization, net  | 8,575                              | 8,123              |
| (Increase) decrease in accrued interest receivable                                 | (181)                              | 1,451              |
| (Decrease) increase in other assets  | (6,126)                            | 8,726              |
| Origination of loans held-for-sale   | (178,819)                          | (137,298)          |
| Proceeds from sales of loans held-for-sale   | 191,831                            | 142,535            |
| Gain on mortgage banking activities, net   | (2,837)                            | (1,882)            |
| Gain on mark-to-market adjustment on trading securities                            | 125                                |                    |
| Security gains, net  | (2,981)                            | (17,797)           |
| Reverse mortgage consolidation gain  | (3,801)                            |                    |
| Stock-based compensation expense   | 2,294                              | 1,600              |
| Excess tax benefits from share-based payment arrangements                          | (266)                              | (99)               |
| Increase in accrued interest payable   | 2,155                              | 4,425              |
| Decrease in other liabilities  | (9,488)                            | (3,432)            |
| Loss on sale of assets acquired through foreclosure and valuation adjustments, net | 203                                | 2,891              |
| Increase in value of bank-owned life insurance                                     | (162)                              | (1,447)            |
| Decrease in capitalized interest, net  | (802)                              | (478)              |
| <b>Net cash provided by operating activities</b>                                   | <b>\$ 44,737</b>                   | <b>\$ 63,253</b>   |
| <b>Investing activities:</b>   |                                    |                    |
| Maturities of investment securities  | 510                                | 5,039              |
| Sale of investment securities available for sale                                   | 239,383                            | 616,254            |
| Purchase of investment securities available-for-sale                               | (255,277)                          | (751,363)          |
| Repayments of investment securities available-for-sale                             | 64,369                             | 101,729            |
| Disbursements for reverse mortgages  | (40)                               | (94)               |
| Proceeds from loan disposition   |                                    | 31,307             |
| Net increase in loans  | (121,589)                          | (38,190)           |
| Cash received in consolidation of reverse mortgage securitization trust            | 5,833                              |                    |
| Payment of bank-owned life insurance   |                                    | 2,021              |
| Acquisition of Array/Arrow, net of cash acquired                                   | (4,189)                            |                    |
| Net (increase) decrease in stock of Federal Home Loan Bank of Pittsburgh           | (2,711)                            | 5,585              |
| Sales of assets acquired through foreclosure, net                                  | 4,682                              | 11,789             |
| Investment in premises and equipment, net  | (1,948)                            | (5,747)            |
| <b>Net cash (used for) provided by investing activities</b>                        | <b>\$ (70,977)</b>                 | <b>\$ (21,670)</b> |
| <b>Financing activities:</b>   |                                    |                    |
| Net (decrease) increase in demand and saving deposits                              | (46,072)                           | 101,059            |
| Decrease in time deposits  | (103,062)                          | (58,991)           |

Edgar Filing: WSFS FINANCIAL CORP - Form 10-Q

|   |                   |                    |
|---|-------------------|--------------------|
| Increase (decrease) in brokered deposits  | 4,958             | (25,717)           |
| Receipts from FHLB advances   | 29,071,254        | 27,299,083         |
| Repayments of FHLB advances   | (28,847,129)      | (27,444,895)       |
| Receipts from federal funds purchased and securities sold under agreement to repurchase | 15,682,425        | 14,135,000         |
| Repayments of federal funds purchased and securities sold under agreement to repurchase | (15,678,425)      | (14,085,000)       |
| Repayment of unsecured debt   |                   | (30,000)           |
| Issuance of Senior Debt   |                   | 52,691             |
| Dividends paid  | (6,017)           | (5,115)            |
| Issuance of common stock and exercise of common stock options                           | 2,223             | 1,086              |
| Repurchase of common stock warrants   |                   | (1,800)            |
| Redemption of preferred stock   | (52,623)          |                    |
| Excess tax benefits from share-based payment arrangements                               | 266               | 99                 |
| <b>Net cash provided by (used for) financing activities</b>                             | <b>\$ 27,798</b>  | <b>\$ (62,500)</b> |
| Increase (decrease) in cash and cash equivalents  | 1,558             | (20,917)           |
| Cash and cash equivalents at beginning of period  | 500,887           | 468,017            |
| Cash and cash equivalents at end of period  | <b>\$ 502,445</b> | <b>\$ 447,100</b>  |
| <b>Supplemental Disclosure of Cash Flow Information:</b>                                |                   |                    |
| Cash paid for interest during the period  | \$ 9,392          | \$ 13,574          |
| Cash paid for income taxes, net   | 15,822            | 8,379              |
| Loans transferred to assets acquired through foreclosure                                | 7,427             | 9,290              |
| Net change in other comprehensive income  | (29,021)          | 6,131              |
| Fair value of assets acquired   | 12,817            |                    |
| Fair value of liabilities assumed   | 10,127            |                    |
| Fair value of assets consolidated   | 41,397            |                    |
| Fair value of liabilities consolidated  | 26,339            |                    |

The accompanying notes are an integral part of these Consolidated Financial Statements.

---

**Table of Contents**

**WSFS FINANCIAL CORPORATION**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2013**

**(UNAUDITED)**

**1. BASIS OF PRESENTATION**

Our Consolidated Financial Statements include the accounts of WSFS Financial Corporation ( the Company , our Company , we , our or us ), Wilmington Savings Fund Society, FSB ( WSFS Bank or the Bank ) and Montchanin Capital Management, Inc. ( Montchanin ). We also have one unconsolidated affiliate, WSFS Capital Trust III ( the Trust ). WSFS Bank has two fully-owned subsidiaries, WSFS Investment Group, Inc. ( WIG ) and Monarch Entity Services LLC ( Monarch ) and Montchanin has one wholly owned subsidiary, Cypress Capital Management, LLC ( Cypress ). In addition to the subsidiaries listed above, we also have one consolidated variable interest entity, SASCO 2002-RM1 ( SASCO ), which is a reverse mortgage securitization trust.

Founded in 1832, the Bank is one of the ten oldest banks continuously operating under the same name in the United States. We provide residential and commercial real estate, commercial and consumer lending services, as well as retail deposit and cash management services. In addition, we offer a variety of wealth management and trust services to personal and corporate customers through our Wealth Management division. Lending activities are funded primarily with customer deposits and borrowings. The Federal Deposit Insurance Corporation ( FDIC ) insures our customers' deposits to their legal maximums. We serve our customers primarily from our 51 offices located in Delaware (41), Pennsylvania (8), Virginia (1) and Nevada (1) and through our website at [www.wsfsbank.com](http://www.wsfsbank.com). Information on our website is not incorporated by reference into this quarterly report.

Amounts subject to significant estimates are items such as the allowance for loan losses and reserves for lending related commitments, goodwill, intangible assets, post-retirement benefit obligations, the fair value of financial instruments, investment in reverse mortgage, income taxes and other-than-temporary impairments ( OTTI ). Among other effects, changes to such estimates could result in future impairments of investment securities, goodwill and intangible assets and establishment of allowances for loan losses and lending related commitments as well as increased post-retirement benefits expense.

Our accounting and reporting policies conform with U.S. generally accepted accounting principles and prevailing practices within the banking industry for interim financial information and Rule 10-01 of the Securities and Exchange Commission ( SEC ) Regulation S-X. Rule 10-01 of Regulation S-X does not require us to include all information and notes for complete financial statements and prevailing practices within the banking industry. Operating results for the three and nine month periods ended September 30, 2013 are not necessarily indicative of the results that may be expected for any future quarters or for the year ending December 31, 2013. For further information, refer to the consolidated financial statements and the accompanying notes included in our Annual Report on Form 10-K for the year ended December 31, 2012 as filed with the SEC.

Whenever necessary, reclassifications have been made to prior period Consolidated Financial Statements to conform to the current period's presentation. All significant intercompany transactions were eliminated in consolidation.

**Table of Contents****2. EARNINGS PER SHARE**

The following table shows the computation of basic and diluted earnings per share:

|  | For the three months ended<br>September 30, |          | For the nine months ended<br>September 30, |           |
|--|---|----------|--|-----------|
|  | 2013  | 2012     | 2013                                       | 2012      |
|  | (In Thousands, Except Per Share Data)       |          |  |           |
| <b><u>Numerator:</u></b>   |   |          |  |           |
| Net income allocable to common stockholders  | \$ 13,828                                   | \$ 9,286 | \$ 33,175                                  | \$ 21,676 |
| <b><u>Denominator:</u></b>   |   |          |  |           |
| Denominator for basic earnings per share weighted average shares                                 | 8,828                                       | 8,712    | 8,804                                      | 8,702     |
| Effect of dilutive employee stock options and warrants   | 148   | 83       | 106  | 77        |
| Denominator for diluted earnings per share adjusted weighted average shares and assumed exercise | 8,976                                       | 8,795    | 8,910                                      | 8,779     |
| <b>Earnings per share:</b>   |   |          |  |           |
| <b>Basic:</b>  |   |          |  |           |
| Net income allocable to common stockholders  | \$ 1.57                                     | \$ 1.07  | \$ 3.77                                    | \$ 2.49   |
| <b>Diluted:</b>  |   |          |  |           |
| Net income allocable to common stockholders  | \$ 1.54                                     | \$ 1.06  | \$ 3.72                                    | \$ 2.47   |
| Outstanding common stock equivalents having no dilutive effect                                   | 402   | 338      | 557  | 361       |

**Table of Contents****3. INVESTMENT SECURITIES**

The following tables detail the amortized cost and the estimated fair value of our investment securities available-for-sale and trading securities:

|   | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Fair<br>Value     |
|---|-------------------|------------------------------|-------------------------------|-------------------|
|   | (In Thousands)    |                              |                               |                   |
| <b>Available-for-sale securities:</b>   |                   |                              |                               |                   |
| <b>September 30, 2013:</b>  |                   |                              |                               |                   |
| State and political subdivisions  | \$ 87,987         | \$ 224                       | \$ (4,879)                    | \$ 83,332         |
| U.S. Government and government sponsored enterprises ( GSE )                      | 41,670            | 131                          | (3)                           | 41,798            |
| Federal National Mortgage Association ( FNMA ) Mortgage-Backed Securities ( MBS ) | 379,721           | 518                          | (11,990)                      | 368,249           |
| Collateralized Mortgage Obligation ( CMO ) (1)                                    | 112,887           | 169                          | (4,585)                       | 108,471           |
| Federal Home Loan Mortgage Corporation ( FHLMC ) MBS                              | 109,482           | 38                           | (3,397)                       | 106,123           |
| Government National Mortgage Association ( GNMA ) MBS                             | 100,349           | 1,134                        | (2,530)                       | 98,953            |
|   | <b>\$ 832,096</b> | <b>\$ 2,214</b>              | <b>\$ (27,384)</b>            | <b>\$ 806,926</b> |
| <b>December 31, 2012</b>  |                   |                              |                               |                   |
| State and political subdivisions  | 3,120             | 89                           |                               | 3,209             |
| GSE   | 46,726            | 266                          | (2)                           | 46,990            |
| FNMA  | 396,910           | 9,588                        | (243)                         | 406,255           |
| CMO (1)   | 251,848           | 7,849                        | (301)                         | 259,396           |
| FHLMC   | 58,596            | 1,171                        | (117)                         | 59,650            |
| GNMA  | 129,288           | 3,221                        | (54)                          | 132,455           |
|   | <b>\$ 886,488</b> | <b>\$ 22,184</b>             | <b>\$ (717)</b>               | <b>\$ 907,955</b> |
| <b>Trading securities</b>   |                   |                              |                               |                   |
| <b>September 30, 2013:</b>  |                   |                              |                               |                   |
| CMO   | \$                | \$                           | \$                            | \$                |
| <b>December 31, 2012</b>  |                   |                              |                               |                   |
| CMO   | \$ 12,590         | \$                           | \$                            | \$ 12,590         |

(1) Includes agency CMO securities classified as available-for-sale

**Table of Contents**

The scheduled maturities of investment securities available-for-sale at September 30, 2013 and December 31, 2012 were as follows:

|                                       | Available-for-Sale |                   |
|---------------------------------------|--------------------|-------------------|
|                                       | Amortized<br>Cost  | Fair<br>Value     |
|                                       | (In Thousands)     |                   |
| <b>September 30, 2013</b>             |                    |                   |
| Within one year                       | \$ 22,860          | \$ 22,932         |
| After one year but within five years  | 32,661             | 32,465            |
| After five years but within ten years | 312,070            | 298,900           |
| After ten years                       | 464,505            | 452,629           |
|                                       | <b>\$ 832,096</b>  | <b>\$ 806,926</b> |
| <b>December 31, 2012</b>              |                    |                   |
| Within one year                       | \$ 19,001          | \$ 19,115         |
| After one year but within five years  | 28,855             | 29,034            |
| After five years but within ten years | 321,103            | 329,580           |
| After ten years                       | 517,529            | 530,226           |
|                                       | <b>\$ 886,488</b>  | <b>\$ 907,955</b> |

The portfolio of available-for-sale MBS includes 134 securities all of which are GSE securities with an amortized cost of \$702.4 million. All securities were AAA-rated at the time of purchase. All securities were re-evaluated for OTTI at September 30, 2013. The result of this evaluation showed no OTTI for the third quarter of 2013. The weighted average duration of MBS was 5.8 years at September 30, 2013.

MBS have expected maturities that differ from their contractual maturities. These differences arise because borrowers may have the right to call or prepay obligations with or without a prepayment penalty.

At September 30, 2013, investment securities with market values aggregating \$513.0 million were pledged as collateral for retail customer repurchase agreements, municipal deposits, and other obligations. From time to time, investment securities are also pledged as collateral for FHLB borrowings. There were no FHLB pledged investment securities at September 30, 2013.

During the first nine months of 2013, we sold \$239.9 million of investment securities categorized as available-for-sale for net gains of \$3.0 million. In the first nine months of 2012, proceeds from the sale of investment securities available-for-sale were \$616.3 million and resulted in net gains of \$17.7 million. The cost basis of all investment securities sales is based on the specific identification method.

As of September 30, 2013, our investment securities portfolio had remaining unamortized premiums of \$25.1 million and \$90,000 of unaccreted discounts.

At September 30, 2013, we owned investment securities totaling \$678.9 million in which the amortized cost basis exceeded fair value. Total unrealized losses on those securities were \$27.4 million at September 30, 2013. The temporary impairment is the result of changes in market interest rates subsequent to the purchase of the securities. Our investment portfolio is reviewed each quarter for indications of impairment. This review includes analyzing the length of time and the extent to which the fair value has been lower than the cost, the financial condition and near-term prospects of the issuer, including any specific events which may influence the operations of the issuer and our intent and ability to hold the investment for a period of time sufficient to allow for any anticipated recovery in the market. We evaluate our intent and ability to hold securities based upon our investment strategy for the particular type of security and our cash flow needs, liquidity position, capital adequacy and interest rate risk position. In addition, we do not have the intent to sell, nor is it more likely-than-not we will be required to sell these securities before we are able to recover the amortized cost basis.

During the first nine months of 2013, we purchased \$77.7 million of municipal bonds. The purpose was to improve return, diversify our investment portfolio and reduce our effective tax rate.



**Table of Contents**

For these investment securities with unrealized losses, the table below shows our gross unrealized losses and fair value by investment category and length of time that individual securities were in a continuous unrealized loss position at September 30, 2013.

|   | Less than 12 months |                  | 12 months or longer |                 | Total             |                  |
|---|---------------------|------------------|---------------------|-----------------|-------------------|------------------|
|   | Fair Value          | Unrealized Loss  | Fair Value          | Unrealized Loss | Fair Value        | Unrealized Loss  |
| (In Thousands)                                |                     |                  |                     |                 |                   |                  |
| <b>Available-for-sale</b>                     |                     |                  |                     |                 |                   |                  |
| State and political subdivisions              | \$ 59,470           | \$ 4,879         | \$                  | \$              | \$ 59,470         | \$ 4,879         |
| U.S Government and agencies                   |                     |                  | 2,003               | 3               | 2,003             | 3                |
| FNMA  | 331,949             | 11,840           | 4,060               | 150             | 336,009           | 11,990           |
| CMO   | 99,464              | 4,584            | 1,339               | 1               | 100,803           | 4,585            |
| FHLMC   | 105,539             | 3,397            |                     |                 | 105,539           | 3,397            |
| GNMA  | 75,096              | 2,530            |                     |                 | 75,096            | 2,530            |
| <b>Total temporarily impaired investments</b> | <b>\$ 671,518</b>   | <b>\$ 27,230</b> | <b>\$ 7,402</b>     | <b>\$ 154</b>   | <b>\$ 678,920</b> | <b>\$ 27,384</b> |

The table below shows our investment securities gross unrealized losses and fair value by investment category and length of time that individual securities were in a continuous unrealized loss position at December 31, 2012.

|   | Less than 12 months |                 | 12 months or longer |                 | Total             |                 |
|---|---------------------|-----------------|---------------------|-----------------|-------------------|-----------------|
|   | Fair Value          | Unrealized Loss | Fair Value          | Unrealized Loss | Fair Value        | Unrealized Loss |
| (In Thousands)                                |                     |                 |                     |                 |                   |                 |
| <b>Available-for-sale</b>                     |                     |                 |                     |                 |                   |                 |
| State and political subdivisions              | \$                  | \$              | \$                  | \$              | \$                | \$              |
| U.S Government and agencies                   | 2,008               | 2               |                     |                 | 2,008             | 2               |
| FNMA  | 43,696              | 243             |                     |                 | 43,696            | 243             |
| CMO   | 40,358              | 268             | 1,364               | 33              | 41,722            | 301             |
| FHLMC   | 13,884              | 117             |                     |                 | 13,884            | 117             |
| GNMA  | 10,029              | 54              |                     |                 | 10,029            | 54              |
| <b>Total temporarily impaired investments</b> | <b>\$ 109,975</b>   | <b>\$ 684</b>   | <b>\$ 1,364</b>     | <b>\$ 33</b>    | <b>\$ 111,339</b> | <b>\$ 717</b>   |



---

**Table of Contents**

**4. ALLOWANCE FOR LOAN LOSSES AND CREDIT QUALITY INFORMATION**

**Allowance for Loan Losses**

We maintain an allowance for loan losses and charge losses to this allowance when such losses are realized. We established our allowance for loan losses in accordance with guidance provided in the SEC's Staff Accounting Bulletin 102 (SAB 102). The determination of the allowance for loan losses requires significant judgment reflecting our best estimate of impairment related to specifically identified impaired loans as well as probable loan losses in the remaining loan portfolio. Our evaluation is based upon a continuing review of these portfolios. The following are included in our allowance for loan losses:

Specific reserves for impaired loans

Allowances for pools of homogenous loans based on historical loss experience

Adjustments for qualitative and environmental factors

Allowance for model estimation and complexity risk

Specific reserves are established for impaired loans where we have identified significant conditions or circumstances related to specific credits that indicate losses are probable. Unless loans are well-secured and collection is imminent, all loans that are 90 days past due are deemed impaired. Reserves for impaired loans are generally charged-off within 90 days of impairment recognition. Estimated losses are based on collateral values, estimates of future cash flows, or market valuations.

Allowances for pooled homogeneous loans, that are not deemed impaired, are based on historical loss experience. Estimated losses for pooled portfolios are determined differently for commercial loan pools and retail loan pools. Commercial loans are pooled into the following segments: Business Loans (Commercial and Industrial Loans), Commercial Real Estate Owner-Occupied, Commercial Real Estate Investor, and Construction Loans. Each pool is further segmented by internally assessed risk ratings. Loan losses for commercial loans are estimated by determining the probability of default and expected loss severity upon default. Probability of default is calculated based on the historical rate of migration to impaired status during the last fourteen quarters. This was an increase of one quarter over the previous period's analysis. This adjustment provides a more representative period and accurate estimation of the allowance at the current point in this credit cycle. Loss severity is calculated as the actual loan losses (net of recoveries) on impaired loans in the respective pool during the same time frame. Retail loans are pooled into the following segments: residential mortgage loans, home equity secured loans, and all other consumer loans. Pooled reserves for retail loans are calculated based solely on the previous three year average loss rate.

Qualitative and environmental adjustment factors are taken into consideration when determining the above reserve estimates or core reserves. These adjustment factors are based upon our evaluation of various current internal and external conditions including:

Assessment of current underwriting policies, staff, and portfolio mix

Internal trends of delinquency, nonaccrual and criticized loans by segment

Assessment of risk rating accuracy, control and regulatory assessments/environment

General economic conditions locally and nationally

Market trends impacting collateral values

Competitive environment as it could impact loan structure and underwriting

The above factors are based on their relative standing compared to the period which historic losses are used in core reserve estimates and current directional trends. Each individual qualitative and environmental factor in our model can add or subtract to core reserves.

The final component of our allowance for loan losses is a reserve for model estimation and complexity risk. The calculation of reserves is generally quantitative; however, qualitative estimates of valuations and risk assessment are necessary. We increased our calculated reserves by 2% to account for model estimation and complexity risk as of September 30, 2013 and December 31, 2012.

Our loan officers and risk managers meet at least quarterly to discuss and review the conditions and risks associated with individual problem loans. In addition, various regulatory agencies and loan review consultants periodically review our loan ratings and allowance for loan losses.

**Table of Contents**

The following tables provide the activity of our allowance for loan losses and loan balances for three and nine months ended September 30, 2013 and 2012:

|  | Commercial     | Owner -<br>Occupied<br>Commercial | Commercial<br>Mortgages | Construction | Residential | Consumer   | Complexity<br>Risk (1) | Total        |
|--|----------------|-----------------------------------|-------------------------|--------------|-------------|------------|------------------------|--------------|
|  | (in thousands) |                                   |                         |              |             |            |                        |              |
| <b>Three months ended<br/>September 30, 2013</b>   |                |                                   |                         |              |             |            |                        |              |
| Allowance for loan losses                          |                |                                   |                         |              |             |            |                        |              |
| Beginning balance                                  | \$ 12,967      | \$ 8,049                          | \$ 6,345                | \$ 3,952     | \$ 3,230    | \$ 6,137   | \$ 814                 | \$ 41,494    |
| Charge-offs  | (1,172)        | (31)                              | (103)                   | (4)          | (290)       | (1,343)    |                        | (2,943)      |
| Recoveries   | 273            | 55                                | 333                     | 21           | 10          | 219        |                        | 911          |
| Provision (credit)                                 | 594            | (23)                              | 345                     | (380)        | 364         | 1,071      | (2)                    | 1,969        |
| Ending balance                                     | \$ 12,662      | \$ 8,050                          | \$ 6,920                | \$ 3,589     | \$ 3,314    | \$ 6,084   | \$ 812                 | \$ 41,431    |
| <b>Nine months ended<br/>September 30, 2013</b>    |                |                                   |                         |              |             |            |                        |              |
| Allowance for loan losses                          |                |                                   |                         |              |             |            |                        |              |
| Beginning balance                                  | \$ 13,663      | \$ 6,108                          | \$ 8,079                | \$ 6,456     | \$ 3,124    | \$ 5,631   | \$ 861                 | \$ 43,922    |
| Charge-offs  | (2,311)        | (68)                              | (1,824)                 | (1,344)      | (985)       | (4,153)    |                        | \$ (10,685)  |
| Recoveries   | 900            | 100                               | 442                     | 106          | 51          | 715        |                        | \$ 2,314     |
| Provision (credit)                                 | 410            | 1,910                             | 223                     | (1,629)      | 1,124       | 3,891      | (49)                   | \$ 5,880     |
| Ending balance                                     | \$ 12,662      | \$ 8,050                          | \$ 6,920                | \$ 3,589     | \$ 3,314    | \$ 6,084   | \$ 812                 | \$ 41,431    |
| <b>Period-end allowance<br/>allocated to:</b>      |                |                                   |                         |              |             |            |                        |              |
| Loans individually evaluated<br>for impairment     | \$ 2,004       | \$ 945                            | \$ 1,995                | \$           | \$ 995      | \$ 12      | \$                     | \$ 5,951     |
| Loans collectively evaluated<br>for impairment     | 10,658         | 7,105                             | 4,925                   | 3,589        | 2,319       | 6,072      | 812                    | 35,480       |
| Ending balance                                     | \$ 12,662      | \$ 8,050                          | \$ 6,920                | \$ 3,589     | \$ 3,314    | \$ 6,084   | \$ 812                 | \$ 41,431    |
| <b>Period-end loan balances<br/>evaluated for:</b> |                |                                   |                         |              |             |            |                        |              |
| Loans individually evaluated<br>for impairment     | \$ 5,833       | \$ 12,568                         | \$ 8,894                | \$ 274       | \$ 17,360   | \$ 4,400   | \$                     | \$ 49,329(2) |
| Loans collectively evaluated<br>for impairment     | 748,106        | 777,297                           | 704,895                 | 102,347      | 211,595     | 283,645    |                        | \$ 2,827,885 |
| Ending balance                                     | \$ 753,939     | \$ 789,865                        | \$ 713,789              | \$ 102,621   | \$ 228,955  | \$ 288,045 | \$                     | \$ 2,877,214 |

- (1) Represents the portion of the allowance for loan losses established to account for the inherent complexity and uncertainty of estimates.  
 (2) The difference between this amount and nonaccruing loans at September 30, 2013 represents accruing troubled debt restructured loans.

**Table of Contents**

The following table provides the activity of the allowance for loan losses and loan balances for the three and nine months ended September 30, 2012:

|  | Commercial     | Owner<br>Occupied<br>Commercial | Commercial<br>Mortgages | Construction | Residential | Consumer   | Complexity<br>Risk (1) | Total        |
|--|----------------|---------------------------------|-------------------------|--------------|-------------|------------|------------------------|--------------|
|  | (In Thousands) |                                 |                         |              |             |            |                        |              |
| <b>Three months ended</b>                      |                |                                 |                         |              |             |            |                        |              |
| <b>September 30, 2012</b>                      |                |                                 |                         |              |             |            |                        |              |
| Allowance for loan losses                      |                |                                 |                         |              |             |            |                        |              |
| Beginning balance                              | \$ 9,891       | \$ 4,091                        | \$ 9,618                | \$ 5,307     | \$ 6,265    | \$ 10,341  | \$ 916                 | \$ 46,429    |
| Charge-offs                                    | (1,281)        | (926)                           | (709)                   | (676)        | (705)       | (2,573)    |                        | (6,870)      |
| Recoveries                                     | 455            | 184                             | 18                      | 1,314        | 113         | 204        |                        | 2,288        |
| Provision                                      | (127)          | (4)                             | (2,281)                 | (810)        | 2,690       | 4,300      | (17)                   | 3,751        |
| Ending balance                                 | \$ 8,938       | \$ 3,345                        | \$ 6,646                | \$ 5,135     | \$ 8,363    | \$ 12,272  | \$ 899                 | \$ 45,598    |
| <b>Nine months ended</b>                       |                |                                 |                         |              |             |            |                        |              |
| <b>September 30, 2012</b>                      |                |                                 |                         |              |             |            |                        |              |
| Allowance for loan losses                      |                |                                 |                         |              |             |            |                        |              |
| Beginning balance                              | \$ 15,067      | \$ 9,235                        | \$ 7,556                | \$ 4,074     | \$ 6,544    | \$ 10,604  | \$                     | \$ 53,080    |
| Charge-offs                                    | (11,316)       | (3,614)                         | (5,600)                 | (10,680)     | (3,344)     | (5,494)    |                        | (40,048)     |
| Recoveries                                     | 1,305          | 190                             | 382                     | 1,642        | 171         | 497        |                        | 4,187        |
| Provision                                      | 3,882          | (2,466)                         | 4,308                   | 10,099       | 4,992       | 6,665      | 899                    | 28,379       |
| Ending balance                                 | \$ 8,938       | \$ 3,345                        | \$ 6,646                | \$ 5,135     | \$ 8,363    | \$ 12,272  | \$ 899                 | \$ 45,598    |
| <b>Period-end allowance</b>                    |                |                                 |                         |              |             |            |                        |              |
| <b>allocated to:</b>                           |                |                                 |                         |              |             |            |                        |              |
| Loans individually evaluated<br>for impairment | \$ 1,244       | \$ 222                          | \$ 90                   | \$ 94        | \$ 1,199    | \$ 24      | \$                     | \$ 2,873     |
| Loans collectively evaluated<br>for impairment | 7,694          | 3,123                           | 6,556                   | 5,041        | 7,164       | 12,248     | 899                    | 42,725       |
| Ending balance                                 | \$ 8,938       | \$ 3,345                        | \$ 6,646                | \$ 5,135     | \$ 8,363    | \$ 12,272  | \$ 899                 | \$ 45,598    |
| <b>Period-end loan balances</b>                |                |                                 |                         |              |             |            |                        |              |
| <b>evaluated for:</b>                          |                |                                 |                         |              |             |            |                        |              |
| Loans individually evaluated<br>for impairment | \$ 3,579       | \$ 13,324                       | \$ 5,875                | \$ 2,620     | \$ 18,072   | \$ 6,694   | \$                     | \$ 50,164(2) |
| Loans collectively evaluated<br>for impairment | 694,626        | 737,670                         | 598,681                 | 111,557      | 232,270     | 276,791    |                        | 2,651,595    |
| Ending balance                                 | \$ 698,205     | \$ 750,994                      | \$ 604,556              | \$ 114,177   | \$ 250,342  | \$ 283,485 | \$                     | \$ 2,701,759 |

- (1) Represents the portion of the allowance for loan losses established to account for the inherent complexity and uncertainty of estimates.  
(2) The difference between this amount and nonaccruing loans at September 30, 2012, represents accruing troubled debt restructured loans.

**Table of Contents****Nonaccrual and Past Due Loans**

The following tables show our nonaccrual and past due loans at the dates indicated:

| September 30, 2013<br>(In Thousands) | Greater Than                                 |   |   | Total Past<br>Due<br>And Still<br>Accruing | Accruing<br>Current<br>Balances | Nonaccrual<br>Loans | Total<br>Loans |
|--------------------------------------|--|---|---|--|---------------------------------|---------------------|----------------|
|                                      | 30 59 Days<br>Past Due and<br>Still Accruing | 60 89<br>Days<br>Past Due and<br>Still Accruing | 90 Days<br>Past Due<br>and<br>Still<br>Accruing |  |                                 |                     |                |
| <b>Commercial</b>                    | \$ 13,212                                    | \$  | \$  | \$ 13,212                                  | \$ 735,077                      | \$ 5,650            | \$ 753,939     |
| <b>Owner-Occupied commercial</b>     | 6,474  |   |   | 6,474                                      | 770,823                         | 12,568              | 789,865        |
| <b>Commercial mortgages</b>          | 22   |   |   | 22   | 705,077                         | 8,690               | 713,789        |
| <b>Construction</b>                  |  |   |   |  | 102,347                         | 274                 | 102,621        |
| <b>Residential</b>                   | 3,672  | 1,073   | 658   | 5,403                                      | 215,113                         | 8,439               | 228,955        |
| <b>Consumer</b>                      | 1,138  | 468   |   | 1,606                                      | 283,890                         | 2,549               | 288,045        |
| <b>Total</b>                         | \$ 24,518                                    | \$ 1,541  | \$ 658  | \$ 26,717                                  | \$ 2,812,327                    | \$ 38,170           | \$ 2,877,214   |
| <b>% of Total Loans</b>              | <b>0.85%</b>                                 | <b>0.06%</b>                                    | <b>0.02%</b>                                    | <b>0.93%</b>                               | <b>97.74%</b>                   | <b>1.33%</b>        | <b>100%</b>    |

| December 31, 2012<br>(In Thousands) | Greater Than                                       |   |   | Total Past<br>Due<br>And Still<br>Accruing | Accruing<br>Current<br>Balances | Nonaccrual<br>Loans | Total<br>Loans |
|-------------------------------------|--|---|---|--|---------------------------------|---------------------|----------------|
|                                     | 30 59 Days<br>Past Due<br>and<br>Still<br>Accruing | 60 89<br>Days<br>Past Due<br>and<br>Still<br>Accruing | 90 Days<br>Past Due<br>and<br>Still<br>Accruing |  |                                 |                     |                |
| <b>Commercial</b>                   | \$ 1,214   | \$  | \$  | \$ 1,214                                   | \$ 698,416                      | \$ 4,861            | \$ 704,491     |
| <b>Owner-Occupied commercial</b>    | 1,264  |   |   | 1,264                                      | 755,316                         | 14,001              | 770,581        |
| <b>Commercial mortgages</b>         |  |   |   |  | 618,731                         | 12,634              | 631,365        |
| <b>Construction</b>                 | 269  | 70  |   | 339  | 131,489                         | 1,547               | 133,375        |
| <b>Residential</b>                  | 5,383  | 606   | 786   | 6,775                                      | 226,863                         | 9,989               | 243,627        |
| <b>Consumer</b>                     | 971  | 526   |   | 1,497                                      | 282,776                         | 4,728               | 289,001        |
| <b>Total</b>                        | \$ 9,101   | \$ 1,202  | \$ 786  | \$ 11,089                                  | \$ 2,713,591                    | \$ 47,760           | \$ 2,772,440   |
| <b>% of Total Loans</b>             | <b>0.33%</b>                                       | <b>0.04%</b>  | <b>0.03%</b>                                    | <b>0.40%</b>                               | <b>97.88%</b>                   | <b>1.72%</b>        | <b>100%</b>    |

**Table of Contents****Impaired Loans**

The following tables provide an analysis of our impaired loans at September 30, 2013 and December 31, 2012:

| September 30, 2013        | Ending<br>Loan<br>Balances | Loans with<br>No<br>Specific<br>Reserve<br>(1) | Loans with<br>Specific<br>Reserve | Related<br>Specific<br>Reserve | Contractual<br>Principal<br>Balances | Average<br>Loan<br>Balances |
|---------------------------|----------------------------|--|-----------------------------------|--------------------------------|--------------------------------------|-----------------------------|
| (In Thousands)            |                            |  |                                   |                                |                                      |                             |
| <b>Commercial</b>         | <b>\$ 5,833</b>            | <b>\$ 2,288</b>                                | <b>\$ 3,545</b>                   | <b>\$ 2,004</b>                | <b>\$ 13,728</b>                     | <b>\$ 5,062</b>             |
| Owner-Occupied commercial | 12,568                     | 5,723  | 6,845                             | 945                            | 14,911                               | 13,167                      |
| Commercial mortgages      | 8,894                      | 2,896  | 5,998                             | 1,995                          | 19,494                               | 9,887                       |
| Construction              | 274                        | 274  |                                   |                                | 16,012                               | 1,261                       |
| Residential               | 17,360                     | 9,680  | 7,680                             | 995                            | 19,726                               | 18,091                      |
| Consumer                  | 4,400                      | 4,272  | 128                               | 12                             | 5,091                                | 5,712                       |
| <b>Total</b>              | <b>\$ 49,329</b>           | <b>\$ 25,133</b>                               | <b>\$ 24,196</b>                  | <b>\$ 5,951</b>                | <b>\$ 88,962</b>                     | <b>\$ 53,180</b>            |

| December 31, 2012         | Ending<br>Loan<br>Balances | Loans with<br>No<br>Specific<br>Reserve (1) | Loans with<br>Specific<br>Reserve | Related<br>Specific<br>Reserve | Contractual<br>Principal<br>Balances | Average<br>Loan<br>Balances |
|---------------------------|----------------------------|---|-----------------------------------|--------------------------------|--------------------------------------|-----------------------------|
| (In Thousands)            |                            |   |                                   |                                |                                      |                             |
| <b>Commercial</b>         | <b>\$ 4,861</b>            | <b>\$ 1,598</b>                             | <b>\$ 3,263</b>                   | <b>\$ 2,100</b>                | <b>\$ 12,060</b>                     | <b>\$ 4,993</b>             |
| Owner-Occupied commercial | 14,001                     | 13,827                                      | 174                               | 1                              | 18,658                               | 16,856                      |
| Commercial mortgages      | 12,634                     | 5,422                                       | 7,212                             | 1,887                          | 22,192                               | 10,233                      |
| Construction              | 1,547                      | 1,172                                       | 375                               | 28                             | 17,711                               | 11,239                      |
| Residential               | 18,483                     | 11,053                                      | 7,430                             | 919                            | 20,771                               | 16,917                      |
| Consumer                  | 6,329                      | 5,635                                       | 694                               | 16                             | 7,265                                | 4,514                       |
| <b>Total</b>              | <b>\$ 57,855</b>           | <b>\$ 38,707</b>                            | <b>\$ 19,148</b>                  | <b>\$ 4,951</b>                | <b>\$ 98,657</b>                     | <b>\$ 64,752</b>            |

(1) Reflects loan balances at their remaining book balance.

Interest income of \$234,000 and \$706,000 was recognized on impaired loans during the three and nine months ended September 30, 2013, respectively.

## **Table of Contents**

### **Credit Quality Indicators**

Below is a description of each of our risk ratings for all commercial loans:

*Pass.* These borrowers presently show no current or potential problems and their loans are considered fully collectible.

*Special Mention.* Borrowers have potential weaknesses that deserve management's close attention. Borrowers in this category may be experiencing adverse operating trends, for example, declining revenues or margins, high leverage, tight liquidity, or increasing inventory without increasing sales. These adverse trends can have a potential negative effect on the borrower's repayment capacity. These assets are not adversely classified and do not expose the Bank to significant risk that would warrant a more severe rating. Borrowers in this category may also be experiencing significant management problems, pending litigation, or other structural credit weaknesses.

*Substandard.* Borrowers have well-defined weaknesses that require extensive oversight by management. Borrowers in this category may exhibit one or more of the following: inadequate debt service coverage, unprofitable operations, insufficient liquidity, high leverage, and weak or inadequate capitalization. Relationships in this category are not adequately protected by the sound financial worth and paying capacity of the obligor or the collateral pledged on the loan, if any. The distinct possibility exists that the Bank will sustain some loss if the deficiencies are not corrected.

*Doubtful.* Borrowers have well-defined weaknesses inherent in the Substandard category with the added characteristic that the possibility of loss is extremely high. Current circumstances in the credit relationship make collection or liquidation in full highly questionable. A doubtful asset has some pending event that may strengthen the asset that defers the loss classification. Such impending events include: perfecting liens on additional collateral, obtaining collateral valuations, an acquisition or liquidation preceding, proposed merger, or refinancing plan.

*Loss.* Borrowers are uncollectible or of such negligible value that continuance as a bankable asset is not supportable. This classification does not mean that the asset has absolutely no recovery or salvage value, but rather that it is not practical to defer writing off this asset even though partial recovery may be recognized sometime in the future.

### **Residential and Consumer Loans**

The residential and consumer loan portfolios are monitored on an ongoing basis using delinquency information and loan type as credit quality indicators. These credit quality indicators are assessed in the aggregate in these relatively homogeneous portfolios. Loans that are greater than 90 days past due are generally considered nonperforming and placed in nonaccrual status.

**Table of Contents**

The following tables provide an analysis of problem loans, by credit risk profile using internally assigned risk ratings, as of September 30, 2013 and December 31, 2012

|  | Commercial        |                   | Owner-Occupied Commercial |                   | Commercial Mortgages |                   | Construction      |                   | Total Commercial    |                   |                     |             |  |
|--|-------------------|-------------------|---------------------------|-------------------|----------------------|-------------------|-------------------|-------------------|---------------------|-------------------|---------------------|-------------|--|
|  | Sept. 30 2013     | Dec. 31 2012      | Sept. 30 2013             | Dec. 31 2012      | Sept. 30 2013        | Dec. 31 2012      | Sept. 30 2013     | Dec. 31 2012      | September 30, 2013  | December 31, 2012 | Amount              | %           |  |
| <b>Risk Rating:</b>                                    |                   |                   |                           |                   |                      |                   |                   |                   |                     |                   |                     |             |  |
| Special mention  | \$ 17,148         | \$ 14,611         | \$ 15,433                 | \$ 27,398         | \$ 9,239             | \$ 29,267         | \$ 1,567          | \$ 2,453          | \$ 43,387           | \$                | 73,729              |             |  |
| Substandard:   |                   |                   |                           |                   |                      |                   |                   |                   |                     |                   |                     |             |  |
| Accrual  | 58,944            | 63,074            | 38,792                    | 44,899            | 6,156                | 6,222             | 2,907             | 5,755             | 106,930             |                   | 119,950             |             |  |
| Nonaccrual   | 2,105             | 1,598             | 5,723                     | 13,827            | 2,896                | 5,422             | 274               | 1,172             | 10,902              |                   | 22,019              |             |  |
| Doubtful / Nonaccrual                                  | 3,545             | 3,263             | 6,845                     | 174               | 5,998                | 7,212             |                   | 375               | 16,280              |                   | 11,024              |             |  |
| <b>Total Special Mention, Substandard and Doubtful</b> | <b>81,742</b>     | <b>82,546</b>     | <b>66,793</b>             | <b>86,298</b>     | <b>24,289</b>        | <b>48,123</b>     | <b>4,748</b>      | <b>9,755</b>      | <b>177,499</b>      | <b>8%</b>         | <b>226,722</b>      | <b>10%</b>  |  |
| <b>Pass</b>  | <b>672,197</b>    | <b>621,945</b>    | <b>723,072</b>            | <b>684,283</b>    | <b>689,500</b>       | <b>583,242</b>    | <b>97,873</b>     | <b>123,620</b>    | <b>2,182,715</b>    | <b>92%</b>        | <b>2,013,090</b>    | <b>90%</b>  |  |
| <b>Total Commercial Loans</b>                          | <b>\$ 753,939</b> | <b>\$ 704,491</b> | <b>\$ 789,865</b>         | <b>\$ 770,581</b> | <b>\$ 713,789</b>    | <b>\$ 631,365</b> | <b>\$ 102,621</b> | <b>\$ 133,375</b> | <b>\$ 2,360,214</b> | <b>100%</b>       | <b>\$ 2,239,812</b> | <b>100%</b> |  |

Consumer credit exposure credit risk profile based on payment activity (dollars in thousands):

|                   | Residential       |                   | Consumer          |                   | Total Residential and Consumer |             |                   |             |
|-------------------|-------------------|-------------------|-------------------|-------------------|--------------------------------|-------------|-------------------|-------------|
|                   | Sept. 30 2013     | Dec. 31 2012      | Sept. 30 2013     | Dec. 31 2012      | September 30, 2013             |             | December 31, 2012 |             |
|                   | Amount            | Amount            | Amount            | Amount            | Amount                         | Percent     | Amount            | Percent     |
| Nonperforming (1) | \$ 17,360         | \$ 18,483         | \$ 4,401          | \$ 6,329          | \$ 21,761                      | 4%          | \$ 24,812         | 5%          |
| Performing        | 211,595           | 225,144           | 283,644           | 282,672           | 495,239                        | 96%         | 507,816           | 95%         |
| <b>Total</b>      | <b>\$ 228,955</b> | <b>\$ 243,627</b> | <b>\$ 288,045</b> | <b>\$ 289,001</b> | <b>\$ 517,000</b>              | <b>100%</b> | <b>\$ 532,628</b> | <b>100%</b> |

(1) Includes \$10.8 million as of September 30, 2013 and 10.1 million as of December 31, 2012 of troubled debt restructured mortgages and home equity installment loans that are performing in accordance with modified terms and are accruing interest.



**Table of Contents****Troubled Debt Restructurings (TDR)**

The balance of TDRs at September 30, 2013 and December 31, 2012 was \$26.6 million and \$22.0 million, respectively. The balance at September 30, 2013 included approximately \$15.5 million in nonaccrual status and \$11.1 million in accrual status compared to \$11.9 million in nonaccrual status and \$10.1 million in accrual status at December 31, 2012. Approximately \$1.0 million and \$936,000 in related reserves have been established for these loans at September 30, 2013 and December 31, 2012, respectively.

During the nine months ended September 30, 2013, the terms of 21 loans were modified in TDRs, 5 of which were commercial loans that had already been placed on nonaccrual. The remaining loans represented residential and consumer loans. Our concessions on restructured loans consisted mainly of forbearance agreements, reduction in interest rates or extensions of maturities. Principal balances are generally not forgiven by us when a loan is modified as a TDR. Nonaccruing restructured loans remain in nonaccrual status until there has been a period of sustained repayment performance, typically six months.

The following table presents loans identified as TDRs during the three and nine months ended September 30, 2013 and 2012:

| (In Thousands)              | Three<br>Months Ended<br>September 30,<br>2013 | Three<br>Months Ended<br>September 30,<br>2012 | Nine<br>Months Ended<br>September 30,<br>2013 | Nine<br>Months Ended<br>September 30,<br>2012 |
|-----------------------------|--|--|---|---|
| <b>Commercial</b>           | \$ 6,800                                       | \$ 710   | \$ 6,824                                      | \$ 9,986                                      |
| <b>Commercial mortgages</b> | 108  |  | 1,169   |   |
| <b>Construction</b>         |  |  |   | 378   |
| <b>Residential</b>          | 207  | 2,779  | 806   | 4,170   |
| <b>Consumer</b>             | 256  | 2,165  | 973   | 2,312   |
| <b>Total</b>                | \$ 7,371                                       | \$ 5,654                                       | \$ 9,772                                      | \$ 16,846                                     |

The TDRs described in the table above increased our allowance for loan losses by \$37,000 through allocation of a related reserve, and resulted in charge-offs of \$363,000 during the nine months ended September 30, 2013, compared to increased reserves of \$357,000 and charge-offs of \$8.1 million for the same period of 2012.

There was one residential TDR in the amount of \$130,000 which defaulted (defined as past due 90 days) during the three and nine months ended September 30, 2013, that was restructured within the last twelve months prior to September 30, 2013.

**Table of Contents****5. REVERSE MORTGAGE LOANS AND RELATED ASSETS AND LIABILITIES**

Reverse mortgage loans are contracts in which a homeowner borrows against the equity in his/her home and receives cash in one lump sum payment, a line of credit, fixed monthly payments for either a specific term or for as long as the homeowner lives in the home, or a combination of these options. Since reverse mortgages are nonrecourse obligations, the loan repayments are generally limited to the sale proceeds of the borrower's residence and the mortgage balance consists of cash advanced, interest compounded over the life of the loan and some may include a premium which represents a portion of the shared appreciation in the home's value, if any, or a percentage of the value of the residence.

In 1993, we acquired a pool of reverse mortgages from the FDIC and another lender. In 1994, we purchased Providential Home Income Plan, Inc., a California-based reverse mortgage lender. In November 2002, substantially the entire WSFS reverse mortgage portfolio was sold. In addition to cash payment for the loans, we received \$10 million in BBB rated mortgage-backed securities (Class B) which we classified as trading and an option to acquire up to 49.9% of the Class O certificates issued in connection with mortgage-backed securities by SASCO 2002 RM-1 (SASCO). These mortgage-backed securities were part of a larger issuance of securities backed, in part, by the sold reverse mortgages. Subsequently we negotiated to purchase 100% of the SASCO Class O certificates for \$2.5 million. This transaction closed in July, 2011.

During the third quarter of 2013, we obtained the right to execute a clean-up call on the underlying collateral. This event triggered us to consolidate the assets and liabilities of the securitization trust, SASCO on our balance sheet in accordance with ASC 810, *Consolidation*. As a result, we consolidated \$40.5 million of reverse mortgage loans, \$5.8 million of cash, \$885,000 of MBS and \$38.8 million of debt all at fair value. Our existing investment in reverse mortgages was combined with the consolidated reverse mortgage loans for a total of \$40.1 million at September 30, 2013. The average loan-to-value for these loans is approximately 45%, the average age of the borrowers is 92 years old and there is, in the view of management, significant overcollateralization in the portfolio.

The value of the reverse mortgages is calculated by a third party model that uses the income approach as described in ASC 820-10-35-32. The model is a present value cash flow model, consistent with ASC 820-10-55-5 which describes the components of a present value measurement. The model incorporates the projected cash flows of the notes (including payouts and collections) and then discounts these cash flows using a rate that is commensurate with the risk adjusted rate. The inputs to the model reflect our expectations of what other market participants would use in pricing this asset in a current transaction and therefore is consistent with ASC 820 that requires an exit price methodology for determining fair value.

To value these securities as of September 30, 2013 we used a proprietary model and actual cash flow information to estimate future cash flows. There are three main drivers of cash flows: 1) Prepayments; 2) House Price Appreciation (HPA) forecasts and 3) Interest Rates.

- 1) **Prepayments** — one year look-back comparing the actual cash flows to the forecasted cash flows based on the assumptions used. The base case prepayment represents the average payoff rates for proprietary reverse mortgages by borrower age, using approximately ten years of historical data. We have used 50% of the base case forecasted cash flows to reflect recent prepayment activity.
- 2) **House Price Appreciation** — Consistent with other reverse mortgage analyses from various market sources, we forecast a 2% decline in housing prices in the next year and a 2% recovery in the following year. We believe this forecast continues to be appropriate given the nature of reverse mortgage collateral and historical under-performance to the broad housing market.
- 3) **Interest Rates** — As of September 30, 2013 the forward rates on one month LIBOR are consistent with the assumptions used for future interest rates (one month LIBOR ramping up to 3% over ten years).

The net present value of the projected cash flow depends on the discount rate used. We use a discount rate of 18.7% in valuing expected net cash flows. If the discount rate was decreased by 1%, the net present value would increase by \$890,000. If the discount rate was increased by 1%, the net present value would decrease by \$850,000.

The fair values listed above are estimates that are subject to adjustments. However, while they are not expected to be materially different than those shown, any material adjustments to the estimates will be reflected, retroactively, as of the date of the transaction.

**6. TAXES ON INCOME**

## Edgar Filing: WSFS FINANCIAL CORP - Form 10-Q

We account for income taxes in accordance with FASB ASC 740, *Income Taxes* ( ASC 740 ) (Formerly SFAS No. 109, *Accounting for Income Taxes* and FASB Interpretation No. 48, *Accounting for Uncertainty In Income Taxes, an Interpretation of FASB Statement 109*). ASC 740 requires the recording of 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. We exercise 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.

---

## **Table of Contents**

As a result of the consolidation for accounting purposes of the SASCO reverse mortgage securitization trust during the third quarter of 2013, a deferred tax asset ( DTA ) of approximately \$6.7 million was recorded. However, because SASCO is not consolidated for income tax purposes, a full valuation allowance was also recorded on this DTA due to the uncertainty of its realization, as realization is dependent on future taxable income, which is anticipated upon consolidation for income tax purposes. We are taking steps to unwind the SASCO tax structure which will permit tax consolidation, at which point the uncertainty surrounding the realization of the DTA will be eliminated. Accordingly, if and when we complete this restructuring, we expect to remove the \$6.7 million valuation allowance which will result in an income tax benefit through earnings.

ASC 740 prescribes a minimum probability threshold that a tax position must meet before a financial statement benefit is recognized. We recognize, when applicable, interest and penalties related to unrecognized tax benefits in the provision for income taxes in the financial statements. Assessment of uncertain tax positions under ASC 740 requires careful consideration of the technical merits of a position based on our analysis of tax regulations and interpretations.

There were no unrecognized tax benefits as of December 31, 2012. We record interest and penalties on potential income tax deficiencies as income tax expense. Our federal and state tax returns for the 2009 through 2012 tax years are subject to examination as of September 30, 2013. During the current quarter, the audit of our 2010 federal tax return was completed by the Internal Revenue Service. We recorded a \$200,000 tax benefit as a result of settling this audit. No state income tax return examinations are currently in process.

## **7. SEGMENT INFORMATION**

In accordance with FASB ASC 280, *Segment Reporting* ( ASC 280 ) (Formerly SFAS No. 131, *Disclosures About Segments of an Enterprise and Related Information*) we discuss our business in three segments. There is one segment for each of WSFS Bank, Cash Connect, (the ATM division of WSFS Bank), and Trust and Wealth Management.

The WSFS Bank segment provides financial products to commercial and retail customers through its 51 offices located in Delaware (41), Pennsylvania (8) and Virginia (1) and Nevada (1). Retail and Commercial Banking, Commercial Real Estate Lending and other banking business units are operating departments of WSFS. These departments share the same regulator, the same market, many of the same customers and provide similar products and services through the general infrastructure of the Bank. Because of these and other reasons, these departments are not considered discrete segments and are appropriately aggregated within the WSFS Bank segment in accordance with ASC 280.

Cash Connect provides turnkey ATM services through strategic partnerships with several of the largest networks, manufacturers and service providers in the ATM industry. The balance sheet category Cash in non-owned ATMs includes cash from which fee income is earned through bailment arrangements with customers of Cash Connect.

The Wealth Management division provides a broad array of fiduciary, investment management, credit and deposit products to clients through four businesses. WSFS Investment Group, Inc. provides insurance and brokerage products primarily to our retail banking clients. Cypress Capital Management, LLC is a registered investment advisor with over \$609 million in assets under management. Cypress primary market segment is high net worth individuals, offering a balanced investment style focused on preservation of capital and current income. Christiana Trust, with \$8.1 billion in assets under administration, provides fiduciary and investment services to personal trust clients, and trustee, agency, custodial and commercial domicile services to corporate and institutional clients. WSFS Private Banking serves high net worth clients by delivering credit and deposit products and partnering with Cypress, Christiana and WSFS Investment Group to deliver investment management and fiduciary products and services.

**Table of Contents**

An operating segment is a component of an enterprise that engages in business activities from which it may earn revenues and incur expenses, whose operating results are regularly reviewed by the enterprise's chief operating decision makers to make decisions about resources to be allocated to the segment and assess its performance, and for which discrete financial information is available. We evaluate performance based on pretax ordinary income relative to resources used, and allocate resources based on these results. The accounting policies applicable to our segments are those that apply to our preparation of the accompanying Consolidated Financial Statements. Segment information for the three and nine months ended September 30, 2013 and 2012 follows:

**For the three months ended September 30, 2013**

| Statement of Operations            | WSFS Bank     | Cash Connect | Trust &<br>Wealth<br>Management<br>(In Thousands) | Total         |
|------------------------------------|---------------|--------------|---|---------------|
| <b>External customer revenues:</b> |               |              |   |               |
| Interest income                    | \$ 35,171     | \$           | \$ 1,945  | \$ 37,116     |
| Noninterest income                 | 12,449        | 6,360        | 3,933   | 22,742        |
| Total external customer revenues   | 47,620        | 6,360        | 5,878   | 59,858        |
| <b>Inter-segment revenues:</b>     |               |              |   |               |
| Interest income                    | 906           |              | 1,477   | 2,383         |
| Noninterest income                 | 1,689         | 222          | 28  | 1,939         |
| Total inter-segment revenues       | 2,595         | 222          | 1,505   | 4,322         |
| <b>Total revenue</b>               | <b>50,215</b> | <b>6,582</b> | <b>7,383</b>                                      | <b>64,180</b> |
| <b>External customer expenses:</b> |               |              |   |               |
| Interest expense                   | 3,587         |              | 123   | 3,710         |
| Noninterest expenses               | 26,510        | 3,470        | 2,829   | 32,809        |
| Provision for loan loss            | 2,263         |              | (294)   | 1,969         |
| Total external customer expenses   | 32,360        | 3,470        | 2,658   | 38,488        |
| <b>Inter-segment expenses</b>      |               |              |   |               |
| Interest expense                   | 1,477         | 400          | 506   | 2,383         |
| Noninterest expenses               | 250           | 561          | 1,128   | 1,939         |
| Total inter-segment expenses       | 1,727         | 961          | 1,634   | 4,322         |
| <b>Total expenses</b>              | <b>34,087</b> | <b>4,431</b> | <b>4,292</b>                                      | <b>42,810</b> |
| Income before taxes                | \$ 16,128     | \$ 2,151     | \$ 3,091  | \$ 21,370     |
| Provision for income taxes         |               |              |   | 7,210         |
| Consolidated net income            |               |              |   | \$ 14,160     |
| Capital expenditures               | \$ 460        | \$ 131       | \$  | \$ 591        |
| <b>As of September 30, 2013</b>    |               |              |   |               |
| <b>Statement of Condition</b>      |               |              |   |               |
| Cash and cash equivalents          | \$ 76,785     | \$ 422,544   | \$ 3,116  | \$ 502,445    |
| Other segment assets               | 3,756,277     | 1,995        | 181,939   | 3,940,211     |

Edgar Filing: WSFS FINANCIAL CORP - Form 10-Q

|                      |              |            |            |              |
|----------------------|--------------|------------|------------|--------------|
| Total segment assets | \$ 3,833,062 | \$ 424,539 | \$ 185,055 | \$ 4,442,656 |
|----------------------|--------------|------------|------------|--------------|

**Table of Contents**

For the three months ended September 30, 2012

| Statement of Operations            | WSFS Bank       | Cash Connect  | Trust & Wealth<br>Management<br>(In Thousands) | Total           |
|------------------------------------|-----------------|---------------|--|-----------------|
| <b>External customer revenues:</b> |                 |               |  |                 |
| Interest income                    | \$ 34,475       | \$            | \$ 2,039                                       | \$ 36,514       |
| Noninterest income                 | 11,686          | 4,707         | 3,355  | 19,748          |
| Total external customer revenues   | 46,161          | 4,707         | 5,394  | 56,262          |
| <b>Inter-segment revenues:</b>     |                 |               |  |                 |
| Interest income                    | 944             |               | 1,358  | 2,302           |
| Noninterest income                 | 2,122           | 148           | 24   | 2,294           |
| Total inter-segment revenues       | 3,066           | 148           | 1,382  | 4,596           |
| <b>Total revenue</b>               | <b>49,227</b>   | <b>4,855</b>  | <b>6,776</b>                                   | <b>60,858</b>   |
| <b>External customer expenses:</b> |                 |               |  |                 |
| Interest expense                   | 5,377           |               | 244  | 5,621           |
| Noninterest expenses               | 27,300          | 2,113         | 2,740  | 32,153          |
| Provision for loan loss            | 2,997           |               | 754  | 3,751           |
| Total external customer expenses   | 35,674          | 2,113         | 3,738  | 41,525          |
| <b>Inter-segment expenses</b>      |                 |               |  |                 |
| Interest expense                   | 1,358           | 338           | 606  | 2,302           |
| Noninterest expenses               | 172             | 586           | 1,536  | 2,294           |
| Total inter-segment expenses       | 1,530           | 924           | 2,142  | 4,596           |
| <b>Total expenses</b>              | <b>37,204</b>   | <b>3,037</b>  | <b>5,880</b>                                   | <b>46,121</b>   |
| Income (loss) before taxes         | \$ 12,023       | \$ 1,818      | \$ 896   | \$ 14,737       |
| Provision for income taxes         |                 |               |  | 4,758           |
| Consolidated net income            |                 |               |  | \$ 9,979        |
| <b>Capital expenditures</b>        | <b>\$ 1,289</b> | <b>\$ 311</b> | <b>\$ 3</b>                                    | <b>\$ 1,603</b> |
| <b>As of December 31, 2012</b>     |                 |               |  |                 |
| <b>Statement of Condition</b>      |                 |               |  |                 |
| Cash and cash equivalents          | \$ 68,419       | \$ 430,382    | \$ 2,086                                       | \$ 500,887      |
| Other segment assets               | 3,683,073       | 1,605         | 189,583  | 3,874,261       |
| Total segment assets               | \$ 3,751,492    | \$ 431,987    | \$ 191,669                                     | \$ 4,375,148    |

**Table of Contents**

For the nine months ended September 30, 2013

| Statement of Operations          | WSFS<br>Bank | Cash<br>Connect | Trust &<br>Wealth<br>Management<br>(In Thousands) | Total      |
|----------------------------------|--------------|-----------------|---|------------|
| External customer revenues:      |              |                 |   |            |
| Interest income                  | \$ 102,732   | \$              | \$ 5,857  | \$ 108,589 |
| Noninterest income               | 31,009       | 17,412          | 11,934  | 60,355     |
| Total external customer revenues | 133,741      | 17,412          | 17,791  | 168,944    |
| Inter-segment revenues:          |              |                 |   |            |
| Interest income                  | 2,723        |                 | 4,276   | 6,999      |
| Noninterest income               | 5,040        | 645             | 82  | 5,767      |
| Total inter-segment revenues     | 7,763        | 645             | 4,358   | 12,766     |
| Total revenue                    | 141,504      | 18,057          | 22,149  | 181,710    |
| External customer expenses:      |              |                 |   |            |
| Interest expense                 | 11,120       |                 | 427   | 11,547     |
| Noninterest expenses             | 79,671       | 9,629           | 9,031   | 98,331     |
| Provision for loan loss          | 6,044        |                 | (164)   | 5,880      |
| Total external customer expenses | 96,835       | 9,629           | 9,294   | 115,758    |
| Inter-segment expenses           |              |                 |   |            |
| Interest expense                 | 4,276        | 1,176           | 1,547   | 6,999      |
| Noninterest expenses             | 727          | 1,649           | 3,391   | 5,767      |
| Total inter-segment expenses     | 5,003        | 2,825           | 4,938   | 12,766     |
| Total expenses                   | 101,838      | 12,454          | 14,232  | 128,524    |
| Income (loss) before taxes       | \$ 39,666    | \$ 5,603        | \$ 7,917  | \$ 53,186  |
| Provision for income taxes       |              |                 |   | 18,378     |
| Consolidated net income          |              |                 |   | \$ 34,808  |
| Capital expenditures             | \$ 1,505     | \$ 591          | \$  | \$ 2,096   |



**Table of Contents**

For the nine months ended September 30, 2012

| Statement of Operations            | WSFS Bank      | Cash<br>Connect | Trust &<br>Wealth<br>Management | Total          |
|------------------------------------|----------------|-----------------|---------------------------------|----------------|
|                                    | (In Thousands) |                 |                                 |                |
| <b>External customer revenues:</b> |                |                 |                                 |                |
| Interest income                    | \$ 107,199     | \$              | \$ 6,301                        | \$ 113,500     |
| Noninterest income                 | 42,238         | 13,254          | 10,006                          | 65,498         |
| Total external customer revenues   | 149,437        | 13,254          | 16,307                          | 178,998        |
| <b>Inter-segment revenues:</b>     |                |                 |                                 |                |
| Interest income                    | 3,099          |                 | 4,344                           | 7,443          |
| Noninterest income                 | 6,368          | 568             | 79                              | 7,015          |
| Total inter-segment revenues       | 9,467          | 568             | 4,423                           | 14,458         |
| <b>Total revenue</b>               | <b>158,904</b> | <b>13,822</b>   | <b>20,730</b>                   | <b>193,456</b> |
| <b>External customer expenses:</b> |                |                 |                                 |                |
| Interest expense                   | 17,330         |                 | 669                             | 17,999         |
| Noninterest expenses               | 81,267         | 6,628           | 8,264                           | 96,159         |
| Provision for loan loss            | 26,786         |                 | 1,593                           | 28,379         |
| Total external customer expenses   | 125,383        | 6,628           | 10,526                          | 142,537        |
| <b>Inter-segment expenses</b>      |                |                 |                                 |                |
| Interest expense                   | 4,344          | 1,008           | 2,091                           | 7,443          |
| Noninterest expenses               | 647            | 1,711           | 4,657                           | 7,015          |
| Total inter-segment expenses       | 4,991          | 2,719           | 6,748                           | 14,458         |
| <b>Total expenses</b>              | <b>130,374</b> | <b>9,347</b>    | <b>17,274</b>                   | <b>156,995</b> |
| Income (loss) before taxes         | \$ 28,530      | \$ 4,475        | \$ 3,456                        | \$ 36,461      |
| Provision for income taxes         |                |                 |                                 | 12,708         |
| Consolidated net income            |                |                 |                                 | \$ 23,753      |
| Capital expenditures               | \$ 5,406       | \$ 321          | \$ 20                           | \$ 5,747       |

**8. FAIR VALUE DISCLOSURES OF FINANCIAL ASSETS AND LIABILITIES****FAIR VALUE OF FINANCIAL ASSETS AND LIABILITIES**

ASC 820-10, *Fair Value Measurements and Disclosure*, defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. ASC 820-10 establishes a fair value hierarchy that prioritizes the use of inputs used in valuation methodologies into the following three levels:

Level 1: Inputs to the valuation methodology are quoted prices, unadjusted, for identical assets or liabilities in active markets. A quoted price in an active market provides the most reliable evidence of fair value and shall be used to measure fair value whenever available.

## Edgar Filing: WSFS FINANCIAL CORP - Form 10-Q

Level 2: Inputs to the valuation methodology include quoted prices for similar assets or liabilities in active markets; inputs to the valuation methodology include quoted prices for identical or similar assets or liabilities in markets that are not active; or inputs to the valuation methodology that are derived principally from or can be corroborated by observable market data by correlation or other means.

Level 3: Inputs to the valuation methodology are unobservable and significant to the fair value measurement. Level 3 assets and liabilities include financial instruments whose value is determined using discounted cash flow methodologies, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

**Table of Contents**

A description of the valuation methodologies used for instruments measured at fair value, as well as the general classification of such instruments pursuant to the valuation hierarchy, is set forth below.

The table below presents the balances of assets measured at fair value as of September 30, 2013 (there were no material liabilities measured at fair value):

| Description  | Quoted<br>Prices<br>in<br>Active<br>Markets for<br>Identical<br>Asset<br>(Level<br>1) | Significant<br>Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) | Total<br>Fair<br>Value |
|--|---|---|--|------------------------|
|  | (in Thousands)  |   |  |                        |
| <b>Assets Measured at Fair Value on a Recurring Basis</b>          |   |   |  |                        |
| Available-for-sale securities:                                     |   |   |  |                        |
| Collateralized mortgage obligations                                | \$  | \$ 108,470  | \$   | \$ 108,470             |
| FNMA   |   | 368,249   |  | 368,249                |
| FHLMC  |   | 106,123   |  | 106,123                |
| GNMA   |   | 98,954  |  | 98,954                 |
| U.S. Government and agencies                                       |   | 41,798  |  | 41,798                 |
| State and political subdivisions                                   |   | 83,332  |  | 83,332                 |
| <b>Total assets measured at fair value on a recurring basis</b>    | <b>\$</b>   | <b>\$ 806,926</b>   | <b>\$</b>  | <b>\$ 806,926</b>      |
| <b>Liabilities Measured at Fair Value on a nonrecurring Basis</b>  |   |   |  |                        |
| Bonds payable  | \$  | \$ 26,340   | \$   | \$ 26,340              |
| <b>Assets Measured at Fair Value on a Nonrecurring Basis</b>       |   |   |  |                        |
| Other real estate owned  | \$  | \$  | \$ 7,163   | \$ 7,163               |
| Reverse mortgage loans   |   |   | 40,095   | 40,095                 |
| Impaired loans (collateral dependent)                              |   |   | 43,379   | 43,379                 |
| <b>Total assets measured at fair value on a nonrecurring basis</b> | <b>\$</b>   | <b>\$</b>   | <b>\$ 90,637</b>                                   | <b>\$ 90,637</b>       |

**Table of Contents**

The table below presents the balances of assets measured at fair value as of December 31, 2012 (there are no material liabilities measured at fair value):

| Description  | Quoted<br>Prices<br>in<br>Active<br>Markets for<br>Identical<br>Asset<br>(Level<br>1) | Significant<br>Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) | Total<br>Fair<br>Value |
|--|---|---|--|------------------------|
| (in Thousands)   |   |   |  |                        |
| <b>Assets Measured at Fair Value on a Recurring Basis</b>          |   |   |  |                        |
| Available-for-sale securities:                                     |   |   |  |                        |
| Collateralized mortgage obligations                                | \$  | \$ 252,300  | \$ 7,096   | \$ 259,396             |
| FNMA   |   | 406,255   |  | 406,255                |
| FHLMC  |   | 59,650  |  | 59,650                 |
| GNMA   |   | 132,455   |  | 132,455                |
| U.S. Government and agencies                                       |   | 46,990  |  | 46,990                 |
| State and political subdivisions                                   |   | 3,209   |  | 3,209                  |
| Reverse mortgage loans   |   |   | (457)  | (457)                  |
| Trading Securities   |   |   | 12,590   | 12,590                 |
| <b>Total assets measured at fair value on a recurring basis</b>    | <b>\$</b>   | <b>\$ 900,859</b>   | <b>\$ 19,229</b>                                   | <b>\$ 920,088</b>      |
| <b>Assets Measured at Fair Value on a Nonrecurring Basis</b>       |   |   |  |                        |
| Other real estate owned  | \$  | \$  | \$ 4,622   | \$ 4,622               |
| Impaired loans   |   |   | 52,904   | 52,904                 |
| <b>Total assets measured at fair value on a nonrecurring basis</b> | <b>\$</b>   | <b>\$</b>   | <b>\$ 57,526</b>                                   | <b>\$ 57,526</b>       |

Fair value is based upon quoted market prices, where available. If such quoted market prices are not available, fair value is based upon internally developed models or obtained from third parties that primarily use, as inputs, observable market-based parameters. Valuation adjustments may be made to ensure that financial instruments are recorded at fair value. These adjustments may include unobservable parameters. Our valuation methodologies may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. While we believe our valuation methodologies are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date.

*Available-for-sale securities.* As of September 30, 2013, securities classified as available-for-sale were reported at fair value using both Level 2 and Level 3 inputs. Included in the Level 2 total were approximately \$41.8 million in Federal Agency debentures, \$681.8 million in Federal Agency MBS, and \$83.3 million in municipal bonds. Agency and MBS securities were predominately AAA-rated. We believe that this Level 2 designation is appropriate for these securities under FASB ASC 820-10 as, with almost all fixed income securities, none are exchange traded, and all are priced by correlation to observable market data. For these securities we obtain fair value measurements from an independent pricing service. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, U.S. government and agency yield curves, live trading levels, trade execution data, market consensus prepayment speeds, credit information, and the security's terms and conditions, among other factors. Included in the Level 3 total at December 31, 2012, was a small equity tranche of a reverse mortgage security purchased on July 15, 2011. This security was Level 3 because there was no active market for this security and no observable inputs that reflected quoted prices for identical assets in active markets (Level 1) or inputs other than quoted prices that were observable for the asset through corroboration with observable market data (Level 2). In order to establish the fair value for a Level 3 asset a mark-to-model was developed using the income approach described in FASB ASC 820-10-35-32 and was similar to the methodology used to value our trading securities described below. As of September 30, 2013, we consolidated the assets and liabilities of the securitization trust which resulted in these securities are being eliminated in consolidation. For additional information regarding these transactions, see Note 5, Reverse Mortgages and Related Assets and the discussion of reverse mortgages in this section.

**Table of Contents**

*Trading securities.* The amount included in the trading securities category at December 31, 2012 represented the fair value of a BBB-rated tranche of a reverse mortgage security. There was never an active market for these securities. As such, we classified these trading securities as Level 3 under FASB ASC 820-10. As prescribed by FASB ASC 820-10 management used various observable and unobservable inputs to develop a range of likely fair value prices where this security would be exchanged in an orderly transaction between market participants at the measurement date. The unobservable inputs reflected management's assumptions about the assumptions that market participants would use in pricing this asset. Included in these inputs were the median of a selection of other BBB-rated securities as well as quoted market prices from higher rated tranches of this asset class. The unobservable inputs consisted of prepayments, house price appreciation and interest rates. Management completed a sensitivity analysis at December 31, 2012 which showed any increase or decrease in these inputs would not have had a significant impact on the fair value of these assets. As a result, the value assigned to this security was determined primarily through a discounted cash flow analysis. All of these assumptions required a significant degree of management judgment. As of September 30, 2013, we consolidated the assets and liabilities of the securitization trust which resulted in these securities being completely eliminated in consolidation. For additional information regarding these transactions, see Note 5, Reverse Mortgages and Related Assets and the discussion of reverse mortgages in this section.

*Reverse Mortgages.* Reverse mortgage loans are valued using a present value cash flow model that incorporates the projected cash flows of the notes (including payouts and collections) and then discounts these cash flows using a rate that is commensurate with the risk adjusted rate. The inputs to the model reflect our expectations of what other market participants would use in pricing these assets in a current transaction. Due to the significant amount of management judgment and the unobservable input calculations, these reverse mortgages have been classified as Level 3. For additional information regarding these transactions, see Note 5, Reverse Mortgages and Related Assets and the discussion of reverse mortgages in this section.

*The changes in Level 3 assets measured at fair value on a recurring basis are summarized as follows:*

| (In Thousands)   | Trading<br>Securities | Reverse<br>Mortgages | Available-<br>for-sale<br>Securities | Total     |
|--|-----------------------|----------------------|--------------------------------------|-----------|
| <b>Balance at December 31, 2011</b>                    | \$ 12,432             | \$ (646)             | \$ 3,936                             | \$ 15,722 |
| Total net income for the period included in net income | 33                    | 12                   |                                      | 45        |
| Purchases, sales, issuances, and settlements, net      |                       | 177                  |                                      | 177       |
| Mark-to-market adjustment                              | 125                   |                      | 3,160                                | 3,285     |
| <b>Balance at December 31, 2012</b>                    | \$ 12,590             | \$ (457)             | \$ 7,096                             | \$ 19,229 |
| Mark-to-market adjustment                              | (125)                 |                      |                                      | (125)     |
| Reverse mortgage securitization trust consolidation    | (12,465)              | 457                  | (7,096)                              | (19,104)  |
| <b>Balance at September 30, 2013</b>                   | \$                    | \$                   | \$                                   | \$        |

*Other real estate owned.* Other real estate owned consists of loan collateral which has been repossessed through foreclosure or other measures. Initially, foreclosed assets are recorded as held for sale at the lower of the loan balance or fair value of the collateral less estimated selling costs. Subsequent to foreclosure, valuations are updated periodically and the assets may be marked down further, reflecting a new cost basis. The fair value of our real estate owned was estimated using Level 3 inputs based on appraisals obtained from third parties.

*Impaired loans.* We evaluate and value impaired loans at the time the loan is identified as impaired, and the fair values of such loans are estimated using Level 3 inputs in the fair value hierarchy. Each loan's collateral has a unique appraisal and management's discount of the value is based on the factors unique to each impaired loan. The significant unobservable input in determining the fair value is management's subjective discount on appraisals of the collateral securing the loan, which range from 10% - 50%. Collateral may consist of real estate and/or business assets including equipment, inventory and/or accounts receivable and the value of these assets is determined based on the appraisals by qualified licensed appraisers hired by us. Appraised and reported values may be discounted based on management's historical knowledge, changes in market conditions from the time of valuation, estimated costs to sell, and/or management's expertise and knowledge of the client and the client's business.

Impaired loans, which are measured for impairment using the fair value of the collateral for collateral dependent loans, had a net amount of \$43.4 million and \$52.9 million at September 30, 2013 and December 31, 2012, respectively. The valuation allowance on impaired loans was \$6.0 million as of September 30, 2013 and \$5.0 million as of December 31, 2012.



---

**Table of Contents**

**FAIR VALUE OF FINANCIAL INSTRUMENTS**

The reported fair values of financial instruments are based on a variety of factors. In certain cases, fair values represent quoted market prices for identical or comparable instruments. In other cases, fair values have been estimated based on assumptions regarding the amount and timing of estimated future cash flows that are discounted to reflect current market rates and varying degrees of risk. Accordingly, the fair values may not represent actual values of the financial instruments that could have been realized as of period-end or that will be realized in the future.

The following methods and assumptions were used to estimate the fair value of each class of financial instruments for which it is practicable to estimate that value:

*Cash and Short-Term Investments:* For cash and short-term investments, including due from banks, federal funds sold, securities purchased under agreements to resell and interest-bearing deposits with other banks, the carrying amount is a reasonable estimate of fair value.

*Investments and Mortgage-Backed Securities:* Since quoted market prices are not available, fair value is estimated using quoted prices for similar securities, which we obtain from a third party vendor. We utilize one of the largest providers of securities pricing to the industry and management periodically assesses the inputs used by this vendor to price the various types of securities owned by us to validate the vendor's methodology. The fair value of our investment in reverse mortgages is based on the net present value of estimated cash flows, which have been updated to reflect recent external appraisals of the underlying collateral. For additional discussion of our mortgage-backed securities-trading or our internally developed models, see Fair Value of Financial Assets in Note 7 to the Consolidated Financial Statements.

*Loans held-for-sale:* Loans held-for-sale are carried at the lower of cost or market of the aggregate, or in some cases, individual loans.

*Loans:* Fair values are estimated for portfolios of loans with similar financial characteristics. Loans are segregated by type: commercial, commercial mortgages, construction, residential mortgages and consumer. For loans that reprice frequently, the book value approximates fair value. The fair values of other types of loans are estimated by discounting expected cash flows using the current rates at which similar loans would be made to borrowers with comparable credit ratings and for similar remaining maturities. The fair value of nonperforming loans is based on recent external appraisals of the underlying collateral. Estimated cash flows, discounted using a rate commensurate with current rates and the risk associated with the estimated cash flows, are utilized if appraisals are not available. This technique does not contemplate an exit price.

*Reverse Mortgages.* Reverse mortgage loans are valued using a present value cash flow model that incorporates the projected cash flows of the notes (including payouts and collections) and then discounts these cash flows using a rate that is commensurate with the risk adjusted rate. The inputs to the model reflect our expectations of what other market participants would use in pricing these assets in a current transaction. Due to the significant amount of management judgment and the unobservable inputs in the calculations, these reverse mortgages have been classified as Level 3. For additional information regarding these transactions, see Note 5, Reverse Mortgages and Related Assets and the discussion of reverse mortgages in this section.

*Bank-Owned Life Insurance:* The estimated fair value approximates the book value for this investment.

*Demand Deposits, Savings Deposits and Time Deposits:* The fair value of demand deposits and savings deposits is determined by projecting future cash flows using an estimated economic life based on account characteristics. The resulting cash flow is discounted using rates available on alternative funding sources. The fair value of time deposits is estimated using the rate and maturity characteristics of the deposits to estimate their cash flow. The cash flow is discounted at rates for similar term wholesale funding.

*Borrowed Funds:* Rates currently available to us for debt with similar terms and remaining maturities are used to estimate fair value of existing debt.

*Stock in the Federal Home Loan Bank of Pittsburgh:* The fair value of FHLB stock is assumed to be essentially equal to its cost basis, since the stock is non-marketable but redeemable at its par value.

*Bonds Payable:* The fair value of bonds payable approximates the carrying value as the interest rates are based on market interest rates.

*Off-Balance Sheet Instruments:* The fair value of off-balance sheet instruments, including commitments to extend credit and standby letters of credit, approximates the recorded net deferred fee amounts, which are not significant. Because commitments to extend credit and letters of credit are generally not assignable by either us or the borrower, they only have value to us and the borrower.





**Table of Contents**

The book value and estimated fair value of our financial instruments are as follows:

| (In Thousands)                                | Fair Value Measurement | September 30, 2013 |            | December 31, 2012 |            |
|---|------------------------|--------------------|------------|-------------------|------------|
|   |                        | Book Value         | Fair Value | Book Value        | Fair Value |
| <b>Financial assets:</b>                      |                        |                    |            |                   |            |
| Cash and cash equivalents                     | Level 1                | \$ 502,445         | \$ 502,445 | \$ 500,887        | \$ 500,887 |
| Investment securities                         | See previous table     | 806,926            | 806,926    | 920,088           | 920,088    |
| Loans held for sale                           | Level 3                | 12,608             | 12,608     | 12,758            | 12,758     |
| Loans, net                                    | Level 3                | 2,829,992          | 2,818,832  | 2,723,916         | 2,746,001  |
| Reverse mortgage loans                        | Level 3                | 40,095             | 40,095     | (457)             | (457)      |
| Stock in Federal Home Loan Bank of Pittsburgh | Level 2                | 33,876             | 33,876     | 31,165            | 31,165     |
| Accrued interest receivable                   | Level 2                | 9,833              | 9,833      | 9,652             | 9,652      |
| <b>Financial liabilities:</b>                 |                        |                    |            |                   |            |
| Deposits                                      | Level 2                | 3,121,198          | 2,912,952  | 3,274,963         | 3,174,907  |
| Borrowed funds                                | Level 2                | 874,615            | 874,534    | 637,266           | 638,375    |
| Bonds Payable                                 | Level 2                | 26,340             | 26,340     |                   |            |
| Standby letters of credit                     | Level 3                | 135                | 135        | 224               | 224        |
| Accrued interest payable                      | Level 2                | 3,254              | 3,254      | 1,099             | 1,099      |

**9. INDEMNIFICATIONS AND GUARANTEES**

**Secondary Market Loan Sales.** Given the current interest rate environment and current customer preference for long-term fixed rate mortgages, coupled with our desire not to hold these assets in our portfolio, we generally sell newly originated fixed rate conventional, 15 to 30 year loans in the secondary market to GSEs such as FHLMC or to wholesale lenders. Loans held-for-sale are carried at the lower cost or market value of the aggregate, or in some cases, individual loans. Gains and losses on sales of loans are recognized at the time of the sale. We sometimes retain the servicing rights on residential mortgage loans sold which results in monthly service fee income. Otherwise, we sell loans with servicing released on a nonrecourse basis. Rate-locked loan commitments we intend to sell in the secondary market are accounted for as derivatives under the guidance promulgated in FASB ASC Topic 815, *Derivatives and Hedging*.

We generally do not sell loans with recourse except to the extent arising from standard loan sale contract provisions covering violations of representations and warranties and, under certain circumstances first payment defaults by borrowers. These are customary repurchase provisions in the secondary market for conforming mortgage loan sales. These indemnifications may require our repurchase of the loans. Repurchases and losses are rare, and no provision is made for the losses at the time of sale. There were no such repurchases for the three and nine months ended September 30, 2013.

**Swap Guarantees.** We entered into agreements with three unrelated financial institutions whereby those financial institutions entered into interest rate derivative contracts (interest rate swap transactions) with customers referred to them by us. By the terms of the agreements, those financial institutions have recourse to us for any exposure created under each swap transaction in the event the customer defaults on the swap agreement and the agreement is in a paying position to the third-party financial institution. This is a customary arrangement that allows smaller financial institutions like us to provide access to interest rate swap transactions for our customers without creating the swap ourselves. These swap guarantees are accounted for as credit derivatives under FASB ASC Topic 815, *Derivatives and Hedging*.

At September 30, 2013 there were 104 variable-rate swap transactions between third party financial institutions and our customers, compared to 95 at December 31, 2012. The initial notional amount aggregated approximately \$416.8 million at September 30, 2013 compared to \$381.7 million at December 31, 2012. At September 30, 2013 maturities ranged from approximately six months to 11 years. The aggregate market value of these swaps to customers was a liability of \$24.2 million at September 30, 2013 and \$35.5 million at December 31, 2012.

**Table of Contents****10. ASSOCIATE (EMPLOYEE) BENEFIT PLANS****Postretirement Benefits**

We share certain costs of providing health and life insurance benefits to retired Associates (and their eligible dependents). Substantially all Associates may become eligible for these benefits if they reach normal retirement age while working for us.

We account for our obligations under the provisions of FASB ASC 715, *Compensation - Retirement Benefits* ( ASC 715 ). ASC 715 requires the costs of these benefits be recognized over an Associate's active working career. Disclosures are in accordance with ASC 715.

The following disclosures of the net periodic benefit cost components of postretirement benefits were measured at January 1, 2013 and 2012:

| (In Thousands)                        | Three months ended    |                       | Nine months ended     |                       |
|---------------------------------------|-----------------------|-----------------------|-----------------------|-----------------------|
|                                       | September 30,<br>2013 | September 30,<br>2012 | September 30,<br>2013 | September 30,<br>2012 |
| Service cost                          | \$ 86                 | \$ 72                 | \$ 258                | \$ 216                |
| Interest cost                         | 44                    | 44                    | 132                   | 131                   |
| Amortization of transition obligation |                       | 15                    |                       | 45                    |
| Net loss recognition                  | 20                    | 17                    | 60                    | 51                    |
| Net periodic benefit cost             | \$ 150                | \$ 148                | \$ 450                | \$ 443                |

**Table of Contents****11. CHANGE IN ACCUMULATED OTHER COMPREHENSIVE INCOME**

Accumulated other comprehensive income includes unrealized gains and losses on available-for-sale investments, unrealized gains and losses on interest-only strips, and unrecognized prior service costs on BOLI. Changes to other accumulated other comprehensive income are presented net of tax effect as a component of equity. Reclassification out of accumulated other comprehensive is recorded on the statement of operations either as a gain or loss.

Changes to accumulated other comprehensive income by component are shown net of taxes in the following tables for the period indicated:

| (in thousands)   | Net unrealized<br>gains on<br>investment<br><br>securities<br>available-for-sale | Net unrealized<br>losses on defined<br>benefit<br>pension<br>plan | Total       |
|--|--|---|-------------|
| <b>Balance, June 30, 2013</b>  | \$ (12,309)  | \$ (472)  | \$ (12,781) |
| Other comprehensive loss before reclassifications                    | (3,106)  |   | (3,106)     |
| Less: Amounts reclassified from accumulated other comprehensive loss | (190)  |   | (190)       |
| Net current-period other comprehensive loss                          | (3,296)  |   | (3,296)     |
| <b>Balance, September 30, 2013</b>                                   | \$ (15,605)  | \$ (472)  | \$ (16,077) |
| <b>Balance, June 30, 2012</b>  | \$ 9,767   | \$ (472)  | \$ 9,295    |
| Other comprehensive income before reclassifications                  | 9,558  |   | 9,558       |
| Less: Amounts reclassified from accumulated other comprehensive loss | (1,520)  |   | (1,520)     |
| Net current-period other comprehensive loss                          | 8,038  |   | 8,038       |
| <b>Balance, September 30, 2012</b>                                   | \$ 17,805  | \$ (472)  | \$ 17,333   |

**Table of Contents**

| (in thousands)   | Net unrealized<br>gains on<br>investment<br><br>securities<br>available-for-sale | Net unrealized<br>losses on defined<br>benefit<br>pension<br>plan | Total              |
|--|--|---|--------------------|
| <b>Balance, December 31, 2012</b>                                    | \$ 13,415  | \$ (472)  | \$ 12,943          |
| Other comprehensive loss before reclassifications                    | (27,249)   |   | (27,249)           |
| Less: Amounts reclassified from accumulated other comprehensive loss | (1,771)  |   | (1,771)            |
| Net current-period other comprehensive loss                          | (29,020)   |   | (29,020)           |
| <b>Balance, September 30, 2013</b>                                   | <b>\$ (15,605)</b>   | <b>\$ (472)</b>   | <b>\$ (16,077)</b> |
| <b>Balance, December 31, 2011</b>                                    | \$ 11,674  | \$ (472)  | \$ 11,202          |
| Other comprehensive income before reclassifications                  | 17,165   |   | 17,165             |
| Less: Amounts reclassified from accumulated other comprehensive loss | (11,034)   |   | (11,034)           |
| Net current-period other comprehensive income                        | 6,131  |   | 6,131              |
| <b>Balance, September 30, 2012</b>                                   | <b>\$ 17,805</b>   | <b>\$ (472)</b>   | <b>\$ 17,333</b>   |

The statement of operations impacted by components of other comprehensive income are presented in the table below.

| (in thousands)                            | Three Months Ended<br>September 30, |                  | Affected line item in    |
|---|-------------------------------------|------------------|--------------------------|
|   | 2013                                | 2012             | Statements of Operations |
| <b>Securities available-for-sale:</b>     |                                     |                  |                          |
| Realized gains on securities transactions | \$ 306                              | \$ 2,451         | Securities gains, net    |
| Income taxes                              | (116)                               | (931)            | Income tax provision     |
| <b>Net of tax</b>                         | <b>\$ 190</b>                       | <b>\$ 1,520</b>  |                          |
|   |                                     |                  |                          |
| (in thousands)                            | Nine Months Ended<br>September 30,  |                  | Affected line item in    |
|   | 2013                                | 2012             | Statements of Operations |
| <b>Securities available-for-sale:</b>     |                                     |                  |                          |
| Realized gains on securities transactions | \$ 2,856                            | \$ 17,797        | Securities gains, net    |
| Income taxes                              | (1,085)                             | (6,763)          | Income tax provision     |
| <b>Net of tax</b>                         | <b>\$ 1,771</b>                     | <b>\$ 11,034</b> |                          |

**Table of Contents****12. GOODWILL AND INTANGIBLES**

Our goodwill and other intangible assets are accounted for in accordance with the accounting guidance in FASB ASC Topic 350 *Intangibles Goodwill and Other*.

At December 31, 2012, we completed the Step One test of the analysis to determine potential goodwill impairment of the WSFS Bank and Trust and Wealth Management reporting units. The valuation incorporated a market-based analysis and indicated the fair values of our WSFS Bank and Trust and Wealth Management reporting units were above their carrying amounts. Therefore, in accordance with FASB ASC 350-20-35-6, the Step Two analysis was not required at that time. During the nine months ended September 30, 2013 we determined there were no events or other indicators of impairment as it relates to goodwill or other intangibles.

FASB ASC 350, also requires that an acquired intangible asset be separately recognized if the benefit of the intangible asset is obtained through contractual or other legal rights, or if the asset can be sold, transferred, licensed, rented or exchanged, regardless of the acquirer's intent to do so.

During the third quarter of 2013, we completed the purchase of Array and Arrow. As a result of this transaction, we have recognized intangible assets of \$2.4 million and goodwill of \$4.2 million. The intangibles are mainly the result of the fair value of customer relationships and covenants not-to-compete. The fair values listed above are estimates and are subject to adjustment. However, while they are not expected to be materially different than those shown, any material adjustments to the estimates will be reflected, retroactively, as of the date of the transaction.

The following table summarizes other intangible assets:

|                                      | Gross<br>Intangible<br>Assets | Accumulated<br>Amortization<br>(In Thousands) | Net<br>Intangible<br>Assets |
|--------------------------------------|-------------------------------|---|-----------------------------|
| <b>September 30, 2013</b>            |                               |   |                             |
| Core deposits                        | \$ 4,370                      | \$ (2,458)                                    | \$ 1,912                    |
| Other                                | 7,104                         | (1,870)                                       | 5,234                       |
| <b>Total other intangible assets</b> | <b>\$ 11,474</b>              | <b>\$ (4,328)</b>                             | <b>\$ 7,146</b>             |
| <b>December 31, 2012</b>             |                               |   |                             |
| Core deposits                        | \$ 4,370                      | \$ (2,020)                                    | \$ 2,350                    |
| Other                                | 4,464                         | (1,640)                                       | 2,824                       |
| <b>Total other intangible assets</b> | <b>\$ 8,834</b>               | <b>\$ (3,660)</b>                             | <b>\$ 5,174</b>             |

Core deposits are amortized over their expected lives using the present value of the benefit of the core deposits and straight-line methods of amortization. During the nine months ended September 30, 2013, we recognized amortization expense on other intangible assets of \$612,000.

The following presents the estimated amortization expense of intangibles:

| (In Thousands)    | Amortization<br>of Intangibles |
|-------------------|--------------------------------|
| Remaining in 2013 | \$ 370                         |
| 2014              | 1,171                          |
| 2015              | 1,139                          |
| 2016              | 882                            |
| 2017              | 735                            |
| Thereafter        | 2,849                          |

|       |    |       |
|-------|----|-------|
| Total | \$ | 7,146 |
|-------|----|-------|

**Table of Contents****13. BUSINESS COMBINATIONS***Array Financial Group, Inc. and Arrow Land Transfer Company Acquisition*

On July 31, 2013, WSFS Bank successfully completed the purchase of Array Financial Group, Inc. (Array), a Delaware Valley mortgage banking company, specializing in a variety of residential mortgage and refinancing solutions, and Arrow Land Transfer Company (Arrow), an abstract and title company that is a related entity to Array. All Array and Arrow employees are now WSFS Associates.

These companies were acquired through an asset purchase transaction for the purchase price of \$8.1 million (including a \$1.4 million payment for the working capital of the two companies), \$4.0 million of which will be earned through a five-year earn out based on achieved earnings contribution targets, the fair value is \$2.8 million at September 30, 2013. Operating results of Array and Arrow are included in the consolidated financial statements since the date of acquisition.

The transaction was accounted for as a business combination using the acquisition method of accounting and, accordingly, assets acquired, liabilities assumed and consideration paid were recorded at their estimated fair values as of the acquisition date. The excess of consideration paid over the fair value of net assets acquired was recorded as goodwill, which will not be amortizable for book purposes, however will be deductible for tax purposes. We allocated the total balance of goodwill to our WSFS Bank segment. We also recognized \$2.4 million in intangible assets which will be amortized over 7 years utilizing the straight-line method.

In connection with the acquisition, the following table summarizes the combined fair value of the assets and liabilities acquired:

|   |                 |
|---|-----------------|
| <b>Consideration Paid:</b>                                    |                 |
| Cash paid at closing  | \$ 5,374        |
| Fair value of contingent consideration                        | 2,750           |
| Value of consideration  | 8,124           |
| <b>Assets acquired:</b>                                       |                 |
| <i>(In Thousands)</i>   |                 |
| Cash  | 1,185           |
| Accounts receivable   | 220             |
| Fixed assets  | 148             |
| Loans-Held-For-Sale   | 10,096          |
| Intangible assets   | 2,353           |
| Total assets  | 14,002          |
| <b>Liabilities assumed:</b>                                   |                 |
| Warehouse line of credit                                      | 10,067          |
| Accounts payable  | 60              |
| Total Liabilities   | 10,127          |
| <b>Net assets acquired</b>                                    | <b>3,875</b>    |
| <b>Goodwill resulting from acquisition of Array and Arrow</b> | <b>\$ 4,249</b> |

The fair values listed above are estimates and are subject to adjustment. However, while they are not expected to be materially different than those shown, any material adjustments to the estimates will be reflected retroactively, as of the date of the transaction.

**Table of Contents**

**14. LEGAL PROCEEDINGS**

In July 2011, we were served with a complaint, filed in U.S. Bankruptcy Court for the Eastern District of Pennsylvania, by a bankruptcy trustee relating to a former WSFS Bank customer. The complaint challenges the Bank's actions relating to the repayment of an outstanding loan and also seeks to avoid and recover the pre-bankruptcy repayment of that loan, approximately \$5.0 million. The matter has been captioned Goldstein v. Wilmington Savings Fund Society, FSB (In re: Universal Marketing, Inc.), Chapter 7, Case No. 09-15404 (ELF), Adv. Pro. No. 11-00512. We believe we acted appropriately and we are vigorously defending ourselves against the complaint.

In July 2013, a complaint was filed against WSFS Bank and certain executives alleging that the Bank acted improperly in issuing, amending and/or collecting approximately \$18.0 million in outstanding loans. The matter has been captioned Bennett v. Wilmington Savings Fund Society, FSB, Case No. 2013-08738, in the Court of Common Pleas, Montgomery County, Pennsylvania. This complaint was filed in the context of suits filed by WSFS Bank to obtain repayment and other damages relating to these same loans. We have entered into a settlement agreement to resolve these actions.

Based upon available information we believe the estimate of the aggregate range of reasonably possible losses for all of these legal proceedings was from approximately \$250,000 to approximately \$5.0 million at September 30, 2013.

Except as noted above, there are no other significant pending legal proceedings involving us other than those arising out of routine operations. We do not anticipate that the ultimate liability, if any, arising out of such other proceedings will have a material effect on the Consolidated Financial Statements.



**Table of Contents****ITEM 2. MANAGEMENT DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS  
GENERAL**

We are a thrift holding company headquartered in Wilmington, Delaware. Substantially all of our assets are held by our subsidiary, Wilmington Savings Fund Society, FSB, or WSFS Bank, one of the ten oldest banks continuously operating under the same name in the United States. As a federal savings bank, which was formerly chartered as a state mutual savings bank, we enjoy broad fiduciary powers. A fixture in the community, WSFS Bank has been in operation for more than 181 years. In addition to its focus on stellar customer service, WSFS Bank has continued to fuel growth and remain a leader in our community. We are a relationship-focused, locally-managed, community banking institution that has grown to become the largest thrift holding company in the State of Delaware, one of the top commercial lenders in the state and the third largest bank in terms of Delaware deposits. We state our mission simply: We Stand for Service. Our strategy of Engaged Associates delivering Stellar Service growing Customer Advocates and value for our Owners focuses on exceeding customer expectations, delivering stellar service and building customer advocacy through highly-trained, relationship-oriented, friendly, knowledgeable and empowered Associates.

Our core banking business is commercial lending funded by customer-generated deposits. We have built a \$2.4 billion commercial loan portfolio by recruiting the best seasoned commercial lenders in our markets and offering a high level of service and flexibility typically associated with a community bank. We fund this business primarily with deposits generated through commercial relationships and retail deposits. We service our customers primarily from our 51 offices located in Delaware (41), Pennsylvania (8), Virginia (1) and Nevada (1) and through our website at [www.wsfsbank.com](http://www.wsfsbank.com). We also offer a broad variety of consumer loan products, retail securities and insurance brokerage through our retail branches.

In July 2013 we added two new divisions to WSFS Bank with the purchase Array Financial Group, Inc., a mortgage banking company, and a related entity, Arrow Land Transfer Company, an abstract and title company.

Our Cash Connect division is a premier provider of ATM Vault Cash and related services in the United States. Cash Connect manages more than \$488 million in vault cash in nearly 15,000 ATMs nationwide and also provides online reporting and ATM cash management, predictive cash ordering, armored carrier management, ATM processing and equipment sales. Cash Connect also operates over 450 ATMs for WSFS Bank, which has, by far, the largest branded ATM network in Delaware.

As a leading provider of ATM Vault Cash to the U.S. ATM industry, Cash Connect is exposed to substantial operational risk, including theft of cash from ATMs, armored vehicles, or armored carrier terminals, as well as general risk of accounting errors or fraud. This risk is managed through a series of financial controls, automated tracking and settlement systems, contracts, and other risk mitigation strategies, including both loss prevention and loss recovery strategies. Throughout its 12-year history, Cash Connect periodically has been exposed to theft through theft from armored courier companies and consistently has been able to recover losses through its risk management strategies.

The Wealth Management division provides a broad array of fiduciary, investment management, credit and deposit products to clients through four businesses. WSFS Investment Group, Inc. provides insurance and brokerage products primarily to our retail banking clients. Cypress Capital Management, LLC is a registered investment advisor with over \$600 million in assets under management. Cypress primary market segment is high net worth individuals, offering a balanced investment style focused on preservation of capital and current income. Christiana Trust, with \$8.1 billion in assets under administration, provides fiduciary and investment services to personal trust clients, and trustee, agency, custodial and commercial domicile services to corporate and institutional clients. WSFS Private Banking serves high net worth clients by delivering credit and deposit products and partnering with Cypress, Christiana and WSFS Investment Group to deliver investment management and fiduciary products and services.

We have two consolidated subsidiaries, WSFS Bank and Montchanin Capital Management, Inc. or Montchanin. We also have one unconsolidated affiliate, WSFS Capital Trust III, or the Trust. WSFS Bank has two wholly-owned subsidiaries, WSFS Investment Group, Inc. and Monarch Entity Services LLC, or Monarch. Montchanin has one wholly-owned subsidiary, Cypress. In addition to the subsidiaries listed above, we also have one consolidated variable interest entity ( VIE ), SASCO 2002-RM1 ( SASCO ), which is a reverse mortgage securitization trust.

**Table of Contents****FORWARD-LOOKING STATEMENTS**

This Quarterly Report on Form 10-Q contains estimates, predictions, opinions, projections and other forward-looking statements as that phrase is defined in the Private Securities Litigation Reform Act of 1995. Such statements include, without limitation, references to our financial goals, management's plans and objectives for future operations, financial and business trends, business prospects, and management's outlook or expectations for earnings, revenues, expenses, capital levels, liquidity levels, asset quality or other future financial or business performance, strategies or expectations. Such forward-looking statements are based on various assumptions (some of which may be beyond our control) and are subject to risks and uncertainties (which change over time) and other factors which could cause actual results to differ materially from those currently anticipated. Such risks and uncertainties include, but are not limited to, those related to the economic environment, particularly in the market areas in which we operate, including an increase in unemployment levels; our level of nonperforming assets; the volatility of the financial and securities markets, including changes with respect to the market value of financial assets; changes in market interest rates which may increase funding costs and reduce earning asset yields thus reducing margin; increases in benchmark rates would also increase debt service requirements for customers whose terms include a variable interest rate, which may negatively impact the ability of borrowers to pay as contractually obligated; changes in government regulation affecting financial institutions, including the Dodd-Frank Wall Street Reform and Consumer Protection Act and the rules and regulations being issued in accordance with this statute and potential expenses and elevated capital levels associated therewith; possible additional loan losses and impairment of the collectability of loans; possible changes in trade, monetary and fiscal policies, laws and regulations and other activities of governments, agencies, and similar organizations, may have an adverse effect on business; possible rules and regulations issued by the Consumer Financial Protection Bureau or other regulators which might adversely impact our business model or products and services; possible stresses in the real estate markets, including possible continued deterioration in property values that affect the collateral value underlying our real estate loans; our ability to expand into new markets, develop competitive new products and services in a timely manner, and to maintain profit margins in the face of competitive pressures; possible changes in consumer and business spending and saving habits could affect our ability to increase assets and to attract deposits; our ability to effectively manage credit risk, interest rate risk, market risk, operational risk, legal risk, liquidity risk, reputational risk, and regulatory and compliance risk; the effects of increased competition from both banks and non-banks; the effects of geopolitical instability and risks such as terrorist attacks; the effects of weather and natural disasters such as floods, droughts, wind, tornados and hurricanes, and the effects of man-made disasters; possible changes in the speed of loan prepayments by our customers and loan origination or sales volumes; possible acceleration of prepayments of mortgage-backed securities ( MBS ) due to low interest rates, and the related acceleration of premium amortization on prepayments on MBS due to low interest rates; and the costs associated with resolving any problem loans, litigation and other risks and uncertainties. Such risks and uncertainties are discussed herein, including under the heading Risk Factors, and in our Form 10-K for the year ended December 31, 2012 and other documents filed by us with the Securities and Exchange Commission ( SEC ) from time to time. Forward looking statements are as of the date they are made, and we do 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 us.

**CRITICAL ACCOUNTING POLICIES**

The discussion and analysis of the financial condition and results of operations are based on the Consolidated Financial Statements, which are prepared in conformity with GAAP. The preparation of these Consolidated Financial Statements requires us to make estimates and assumptions affecting the reported amounts of assets, liabilities, revenue and expenses. We regularly evaluate these estimates and assumptions including those related to the allowance for loan losses, deferred taxes, fair value measurements, goodwill and other intangible assets. We base our estimates on historical experience and various other factors and assumptions that are believed to be reasonable under the circumstances. These form the basis for making judgments on the carrying value of assets and liabilities that are not readily apparent from other sources. Although our current estimates contemplate current economic conditions and how we expect them to change in the future, for the remainder of 2013, it is reasonably possible that actual conditions may be worse than anticipated in those estimates, which could materially affect our results of operations and financial condition. Actual results may differ from these estimates under different assumptions or conditions.

The following are critical accounting policies that involve more significant judgments and estimates. See further discussion of these critical accounting policies in our Annual Report on Form 10-K for the year ended December 31, 2012.

**Allowance for Loan Losses**

We maintain an allowance for loan losses and charge losses to this allowance for loan losses when realized. We consider the determination of our allowance for loan losses to be critical because it requires significant judgment reflecting our best estimate of impairment related to specifically evaluated impaired loans as well as the inherent risk of loss for those in the remaining loan portfolio. Our evaluation is based upon a continuing review of the portfolio, with consideration given to evaluations resulting from examinations performed by regulatory authorities.

---

**Table of Contents****Deferred Taxes**

We account for income taxes in accordance with Financial Accounting Standards Board ( FASB ) Accounting Standards Codification ( ASC ) 740, *Income Taxes* ( ASC 740 ), which requires the recording of 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. We consider our accounting policies on deferred taxes to be critical because we regularly assess the need for valuation allowances on deferred income tax assets that may result from, among other things, limitations imposed by Internal Revenue Code and uncertainties, including the timing of settlement and realization of these differences. See Note 6, Taxes on Income to our Consolidated Financial Statements, for additional information on deferred taxes and related valuation allowance.

**Fair Value Measurements**

We adopted FASB ASC 820-10 *Fair Value Measurements and Disclosures* ( ASC 820 ), which defines fair value, establishes a framework for measuring fair value under GAAP, and expands disclosures about fair value measurements. We consider our accounting policies related to fair value measurements to be critical because they are important to the portrayal of our financial condition and results, and they require our subjective and complex judgment as a result of the need to make estimates about the effects of matters that are inherently uncertain. See Note 8, Fair Value Disclosures of Financial Assets to our Consolidated Financial Statements.

**Goodwill and Other Intangible Assets**

Intangible assets resulting from acquisitions under the purchase method of accounting consist of goodwill and other intangible assets. Goodwill is not amortized and is subject to at least annual assessments for impairment by applying a fair value based test. We review goodwill annually and again at any quarter-end if a triggering event occurs during the quarter that may affect goodwill. This review evaluates potential impairment by determining if our fair value has fallen below carrying value.

Other intangible assets consist mainly of core deposits, covenants not to compete and customer relationships obtained through acquisitions and are amortized over their estimated lives using the present value of the benefit of the core deposits and straight-line methods of amortization. Core deposit intangibles are evaluated for impairment when events or changes in circumstances indicate that the carrying amount may not be recoverable.

**FINANCIAL CONDITION, CAPITAL RESOURCES AND LIQUIDITY****Financial Condition**

Our total assets increased \$67.5 million or 2% to \$4.4 billion during the nine months ended September 30, 2013. Included in this increase was a \$106.1 million, or 4%, increase in net loans, and a \$40.5 million increase in reverse mortgages resulting from the consolidation of a reverse mortgage securitization trust during the nine months ended September 30, 2013. See Note 5, Reverse Mortgage Loans and Related Assets and Liabilities to our Consolidated Financial Statements for more information. Partially offsetting these increases was a \$113.6 million decrease in investment securities.

Total liabilities increased \$114.6 million during the nine months ended September 30, 2013 to \$4.1 billion. This increase was primarily the result of increased Federal Home Loan Bank advances of \$224.1 million, or 60%. In addition, bonds payable increased by \$26.3 million due to the consolidation of the reverse mortgage securitization trust during the third quarter of 2013. Partially offsetting these increases was a \$153.8 million decrease in total deposits, mainly due to the expected decline in time and temporary trust deposits during the period, and a \$9.2 million decrease in other borrowed funds.

**Capital Resources**

Stockholders' equity decreased \$47.1 million between December 31, 2012 and September 30, 2013. This decrease was mainly due to the \$52.6 million redemption of preferred stock (formerly TARP), a \$29.0 million decrease in the value of our available-for-sale securities portfolio and the payment of dividends on our common stock and preferred stock of \$4.9 million during the nine months ended September 30, 2013. Partially offsetting this decrease was net income of \$34.8 million during the nine months ended September 30, 2013. Tangible common equity (a non-GAAP financial measure) increased \$5.7 million from \$335.3 million at December 31, 2012 to \$341.0 million at September 30, 2013.

## Edgar Filing: WSFS FINANCIAL CORP - Form 10-Q

Tangible common book value per share of common stock (a non-GAAP financial measure) was \$38.55 at September 30, 2013, an increase of \$0.34, or less than 1%, from \$38.21 reported at December 31, 2012. Book value per share of common stock was \$42.27 at September 30, 2013, a decrease of \$5.72 from \$47.99 reported at December 31, 2012.

**Table of Contents**

Below is a table comparing WSFS Bank's consolidated capital position to the minimum regulatory requirements as of September 30, 2013:

| (Dollars in thousands)                   | Consolidated Bank Capital |             | For Capital Adequacy Purposes |             | To be Well-Capitalized Under Prompt Corrective Action Provisions |             |
|--|---------------------------|-------------|-------------------------------|-------------|--|-------------|
|  | Amount                    | % of Assets | Amount                        | % of Assets | Amount   | % of Assets |
| Total Capital (to Risk-Weighted Assets)  | \$ 486,298                | 14.30 %     | \$ 272,149                    | 8.00 %      | \$ 340,187   | 10.00 %     |
| Core Capital (to Adjusted Total Assets)  | 443,839                   | 10.17       | 174,525                       | 4.00        | 218,156  | 5.00        |
| Tangible Capital (to Tangible Assets)    | 443,839                   | 10.17       | 65,447                        | 1.50        | N/A  | N/A         |
| Tier 1 Capital (to Risk-Weighted Assets) | 443,839                   | 13.05       | 136,075                       | 4.00        | 204,112  | 6.00        |

Under guidelines issued by banking regulators, savings institutions such as WSFS Bank must maintain tangible capital equal to 1.5% of adjusted total assets, core capital equal to 4.0% of adjusted total assets, Tier 1 capital equal to 4.0% of risk weighted assets and total or risk-based capital (a combination of core and supplementary capital) equal to 8.0% of risk-weighted assets. Failure to meet minimum capital requirements can initiate certain mandatory actions and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on our bank's financial statements.

At September 30, 2013, WSFS Bank was in compliance with regulatory capital requirements and was considered a well-capitalized institution. WSFS Bank's core capital ratio of 10.17%, Tier 1 capital ratio of 13.05% and total risk based capital ratio of 14.30%, all remain substantially in excess of well-capitalized regulatory benchmarks, the highest regulatory capital rating. In addition, and not included in Bank capital, the holding company held \$17.9 million in cash to support potential dividends, acquisitions, strategic growth plans.

**Liquidity**

We manage our liquidity and funding needs through our Treasury function and our Asset/Liability Committee. We have a policy that separately addresses liquidity, and management monitors our adherence to policy limits. Also, liquidity risk management is a primary area of examination by the banking regulators.

We have ready access to several sources to fund growth and meet its liquidity needs. Among these are: net income, retail deposit programs, loan repayments, borrowing from the FHLB, repurchase agreements, access to the Federal Discount Window, and access to the brokered deposit market as well as other wholesale funding avenues. In addition, we have a large portfolio of high-quality, liquid investments, primarily short-duration MBS and government sponsored enterprises (GSE) notes that provide a near-continuous source of cash flow to meet current cash needs, or can be sold to meet larger discrete needs for cash. We believe these sources are sufficient to maintain required and prudent levels of liquidity.

During the nine months ended September 30, 2013, cash and cash equivalents increased \$1.6 million to \$502.4 million. This increase was primarily a result of the following: \$64.4 million from the repayments of MBS available-for-sale; \$47.4 million increase in cash provided by operations; and \$4.0 million increase in cash due to the increase in securities sold under agreement to repurchase. Offsetting these increases in cash were: \$224.1 million from the net repayments of FHLB Advances; \$149.1 million decrease in demand, savings and time deposits; \$121.4 million increase in net loans; and \$52.6 million from repurchase of preferred stock.

**NONPERFORMING ASSETS**

The following table shows our nonperforming assets and past due loans at the dates indicated. Nonperforming assets include nonaccruing loans, nonperforming real estate, assets acquired through foreclosure and restructured mortgage and home equity consumer debt. Nonaccruing loans are those on which the accrual of interest has ceased. Loans are placed on nonaccrual status immediately if, in the opinion of management, collection is doubtful, or when principal or interest is past due 90 days or more and the value of the collateral is insufficient to cover principal and interest. Interest accrued but not collected at the date a loan is placed on nonaccrual status is reversed and charged against interest income. In addition, the amortization of net deferred loan fees is suspended when a loan is placed on nonaccrual status. Subsequent cash receipts are applied either to the outstanding principal balance or recorded as interest income, depending on management's assessment of the ultimate collectability of principal and interest. Past due loans are loans contractually past due 90 days or more as to principal or interest payments but which remain on accrual status because they are considered well secured and in the process of collection.



**Table of Contents**

|   | September 30,<br>2013 | December 31,<br>2012 |
|---|-----------------------|----------------------|
| (In Thousands)                                    |                       |                      |
| <b>Nonaccruing loans:</b>                         |                       |                      |
| Commercial  | \$ 5,650              | \$ 4,861             |
| Owner-occupied commercial                         | 12,568                | 14,001               |
| Consumer  | 2,549                 | 4,728                |
| Commercial mortgage                               | 8,690                 | 12,634               |
| Residential mortgage                              | 8,439                 | 9,989                |
| Construction                                      | 274                   | 1,547                |
| <br>  |                       |                      |
| Total nonaccruing loans                           | 38,170                | 47,760               |
| Assets acquired through foreclosure               | 7,163                 | 4,622                |
| Troubled debt restructuring (accruing)            | 11,161                | 10,093               |
| <br>  |                       |                      |
| Total nonperforming assets                        | \$ 56,494             | \$ 62,475            |
| <br>  |                       |                      |
| <b>Past due loans (1):</b>                        |                       |                      |
| Residential mortgages                             | 658                   | 786                  |
| <br>  |                       |                      |
| Total past due loans                              | \$ 658                | \$ 786               |
| <br>  |                       |                      |
| <b>Ratios:</b>                                    |                       |                      |
| Allowance for loan losses to total loans (2)      | 1.44 %                | 1.58 %               |
| Nonperforming assets to total assets              | 1.27                  | 1.43                 |
| Nonaccruing loans to total loans (2)              | 1.33                  | 1.73                 |
| Loan loss allowance to nonaccruing loans          | 108.54                | 91.96                |
| Loan loss allowance to total nonperforming assets | 73.34                 | 70.30                |

(1) Past due loans are accruing loans which are contractually past due 90 days or more as to principal or interest. These loans are well secured and in the process of collection.

(2) Total loans exclude loans held for sale.

Nonperforming assets decreased \$6.0 million between December 31, 2012 and September 30, 2013. As a result, non-performing assets as a percentage of total assets decreased from 1.43% at December 31, 2012 to 1.27% at September 30, 2013. Nonperforming loans improved from 1.73% of total loans at December 31, 2012 to 1.33% at September 30, 2013 as new migration continued to be outpaced by charge-offs, pay downs and assets being moved to Other Real Estate Owned (OREO). OREO increased by net \$2.5 million to \$7.2 million from \$4.6 million at December 31, 2012.

As of September 30, 2013 we had \$106.9 million of loans which, although performing at that date, required increased supervision and review. They may, depending on the economic environment and other factors, become nonperforming assets in future periods. The amount of such loans at December 31, 2012 was \$120.0 million. The majority of these loans are secured by commercial real estate, with others being secured by residential real estate, inventory and receivables.

**Table of Contents**

The following table summarizes the changes in nonperforming assets during the period indicated:

|                                    | <b>For the<br/>nine<br/>months<br/>ended<br/>September 30, 2013</b> | <b>For the year<br/>ended<br/>December 31, 2012</b> |
|------------------------------------|---|---|
|                                    | (In Thousands)  |   |
| Beginning balance                  | \$ 62,475   | \$ 91,675   |
| Additions                          | 21,594  | 73,170  |
| Collections                        | (16,290)  | (46,514)  |
| Collections from loan dispositions |   | (14,305)  |
| Transfers to accrual               | (1,055)   | (552)   |
| Charge-offs / write-downs, net     | (10,230)  | (40,999)  |
| Ending balance                     | \$ 56,494   | \$ 62,475   |

The timely identification of problem loans is a key element in our strategy to manage our loan portfolio. Timely identification enables us to take appropriate action and, accordingly, minimize losses. An asset review system established to monitor the asset quality of our loans and investments in real estate portfolios facilitates the identification of problem assets. In general, this system utilizes guidelines established by federal regulation.

**INTEREST RATE SENSITIVITY**

The matching of maturities or repricing periods of interest rate-sensitive assets and liabilities to promote a favorable interest rate spread and mitigate exposure to fluctuations in interest rates is our primary tool for achieving our asset/liability management strategies. We regularly review our interest rate sensitivity and adjust the sensitivity within acceptable tolerance ranges established by the Board of Directors. At September 30, 2013, interest-earning liabilities exceeded interest-bearing assets that mature or reprice within one year (interest-sensitive gap) by \$69.8 million. Our interest-sensitive liabilities as a percentage of interest-sensitive assets within the one-year window decreased from 98.09% at December 31, 2012 to 97.06% at September 30, 2013. Likewise, the one-year interest-sensitive gap as a percentage of total assets changed to -1.57% at September 30, 2013 from -1.02% at December 31, 2012. The low level of sensitivity reflects our continuing efforts to effectively manage interest rate risk.

Market risk is the risk of loss from adverse changes in market prices and rates. Our market risk arises primarily from interest rate risk inherent in our lending, investing, and funding activities. To that end, we actively monitor and manage our interest rate risk exposure. One measure, required to be performed by federal regulation, measures the impact of an immediate change in interest rates in 100 basis point increments on the economic value of equity ratio. The economic value of equity ratio is defined as the economic value of the estimated cash flows from assets and liabilities as a percentage of economic value of cash flows from total assets. The table below shows the estimated impact of immediate changes in interest rates on our net interest margin and economic value of equity ratio at the specified levels at September 30, 2013 and December 31, 2012:



**Table of Contents**

| % Change in<br>Interest Rate<br>(Basis Points) | September 30, 2013                              |                                    | December 31, 2012                         |                                    |
|--|---|------------------------------------|---|------------------------------------|
|  | % Change in<br>Net<br>Interest<br>Margin<br>(1) | Economic<br>Value of<br>Equity (2) | % Change in<br>Net Interest<br>Margin (1) | Economic<br>Value of<br>Equity (2) |
| +300   | 3%  | 12.71%                             | 4%  | 12.49%                             |
| +200   | 0%  | 12.80%                             | 1%  | 12.62%                             |
| +100   | -2%   | 12.66%                             | -3%                                       | 12.54%                             |
| -  | 0%  | 12.54%                             | 0%  | 12.31%                             |
| -100   | -1%   | 11.97%                             | 1%  | 11.56%                             |
| -200 (3)                                       | NMF   | NMF                                | NMF                                       | NMF                                |
| -300 (3)                                       | NMF   | NMF                                | NMF                                       | NMF                                |

- (1) The percentage difference between net interest margin in a stable interest rate environment and net interest margin as projected under the various rate change environments.
- (2) The economic value of equity ratio of the Company in a stable interest rate environment and the economic value of equity ratio as projected under the various rate change environments.
- (3) Sensitivity indicated by a decrease of 200 or 300 basis points is not deemed meaningful at September 30, 2013 given the low absolute level of interest rates at that time.

We also engage in other business activities that are sensitive to changes in interest rates. For example, mortgage banking revenues and expenses can fluctuate with changing interest rates. These fluctuations are difficult to model and estimate.

**COMPARISON OF THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2013****Results of Operations**

We recorded net income of \$14.2 million for the quarter ended September 30, 2013, a 42% increase over \$10.0 million for the quarter ended September 30, 2012. Income allocable to common stockholders (after preferred stock dividends) was \$13.8 million, or \$1.54 per diluted share of common stock, for the quarter ended September 30, 2013 (a 45% increase in diluted earnings per share, or EPS). During the third quarter of 2013 we realized \$3.8 million in gains related to the consolidation of the 2002 reverse mortgage securitization which more than offset a decrease of \$2.6 million in securities gains. Investment management and fiduciary revenue, credit/debit card and ATM fees (largely related to our ATM division), and traditional banking business all increased during the third quarter of 2013 reflecting fundamental momentum in these businesses. Noninterest expenses for the third quarter of 2013 totaled \$32.8 million compared to \$32.2 million for the third quarter of 2012. The increase of \$656,000, or 2%, was mainly due to increased salaries, benefits, and other compensation due to the improved performance, and a change in billing methodology by Cash Connect division, offset by a decrease in loan workout and OREO costs and regulatory expenses. Net interest margin increased \$2.5 million due to several initiatives undertaken by us in late 2012 and into 2013.

Net income for the nine months of 2013 was \$34.8 million as compared to \$23.8 million for the nine months of 2012. Net income allocable to common stockholders was \$33.2 million, or \$3.72 per diluted share of common stock, compared to net income allocable to common stockholders of \$21.7 million, or \$2.47 per diluted share of common stock, for the nine months ended September 30, 2012, a 51% increase. Consistent with the quarterly results, the nine months of 2013 were impacted by improvements in investment management and fiduciary revenue and credit/debit card and ATM income and decreases in loan workout and OREO costs and regulatory expenses which also helped partially offset the \$15.0 million decrease in security gains.

**Table of Contents****Net Interest Income**

The following tables provide information concerning the balances, yields and rates on interest-earning assets and interest-bearing liabilities during the periods indicated.

|   | Three Months Ended September 30, 2013 |          |                    |                    |          |                    |
|---|---------------------------------------|----------|--------------------|--------------------|----------|--------------------|
|   | 2013                                  |          |                    | 2012               |          |                    |
|   | Average<br>Balance                    | Interest | Yield/<br>Rate (1) | Average<br>Balance | Interest | Yield/<br>Rate (1) |
| (Dollars In Thousands)                                  |                                       |          |                    |                    |          |                    |
| <b>Assets:</b>  |                                       |          |                    |                    |          |                    |
| Interest-earning assets:                                |                                       |          |                    |                    |          |                    |
| Loans (2) (3):  |                                       |          |                    |                    |          |                    |
| Commercial real estate loans                            | \$ 818,361                            | \$ 9,877 | 4.83 %             | \$ 718,046         | \$ 8,803 | 4.90 %             |
| Residential real estate loans (7)                       | 249,476                               | 2,455    | 3.94               | 276,681            | 2,980    | 4.31               |
| Commercial loans  | 1,525,053                             | 17,023   | 4.40               | 1,435,514          | 16,848   | 4.61               |
| Consumer loans  | 287,555                               | 3,353    | 4.63               | 283,704            | 3,372    | 4.73               |
| Total loans   | 2,880,445                             | 32,708   | 4.56               | 2,713,945          | 32,003   | 4.73               |
| Mortgage-backed securities (4) (6)                      | 711,659                               | 3,527    | 1.98               | 829,930            | 4,344    | 2.09               |
| Reverse mortgages and Investment securities (4) (5) (6) | 112,237                               | 794      | 3.66               | 53,392             | 158      | 1.27               |
| Other interest-earning assets                           | 38,054                                | 87       | 0.91               | 31,187             | 9        | 0.11               |
| Total interest-earning assets                           | 3,742,395                             | 37,116   | 4.01               | 3,628,454          | 36,514   | 4.03               |
| Allowance for loan losses                               | (42,315)                              |          |                    | (46,808)           |          |                    |
| Cash and due from banks                                 | 80,586                                |          |                    | 70,366             |          |                    |
| Cash in non-owned ATMs                                  | 424,125                               |          |                    | 362,332            |          |                    |
| Bank-owned life insurance                               | 63,030                                |          |                    | 63,315             |          |                    |
| Other noninterest-earning assets                        | 131,780                               |          |                    | 118,330            |          |                    |
| Total assets  | \$ 4,399,601                          |          |                    | \$ 4,195,989       |          |                    |
| <b>Liabilities and Stockholders Equity:</b>             |                                       |          |                    |                    |          |                    |
| Interest-bearing liabilities:                           |                                       |          |                    |                    |          |                    |
| Interest-bearing deposits:                              |                                       |          |                    |                    |          |                    |
| Interest-bearing demand                                 | \$ 563,409                            | \$ 121   | 0.09 %             | \$ 404,185         | \$ 53    | 0.05 %             |
| Money market  | 764,973                               | 238      | 0.12               | 759,944            | 431      | 0.23               |
| Savings   | 388,132                               | 50       | 0.05               | 390,275            | 83       | 0.08               |
| Customer time deposits                                  | 512,689                               | 1,123    | 0.87               | 716,676            | 2,365    | 1.31               |
| Total interest-bearing customer deposits                | 2,229,203                             | 1,532    | 0.27               | 2,271,080          | 2,932    | 0.51               |
| Brokered certificates of deposit                        | 174,690                               | 141      | 0.32               | 283,345            | 305      | 0.43               |
| Total interest-bearing deposits                         | 2,403,893                             | 1,673    | 0.28               | 2,554,425          | 3,237    | 0.50               |
| FHLB of Pittsburgh advances                             | 651,993                               | 482      | 0.29               | 389,745            | 1,403    | 1.41               |
| Trust preferred borrowings                              | 67,011                                | 339      | 1.98               | 67,011             | 369      | 2.15               |
| Senior Debt   | 55,000                                | 943      | 6.86               | 20,924             | 353      | 6.60               |
| Other borrowed funds (8)                                | 133,077                               | 273      | 0.82               | 129,293            | 259      | 0.80               |
| Total interest-bearing liabilities                      | 3,310,974                             | 3,710    | 0.45               | 3,161,398          | 5,621    | 0.71               |
| Noninterest-bearing demand deposits                     | 669,807                               |          |                    | 590,133            |          |                    |
| Other noninterest-bearing liabilities                   | 32,756                                |          |                    | 33,757             |          |                    |

Edgar Filing: WSFS FINANCIAL CORP - Form 10-Q

|   |                     |                     |
|---|---------------------|---------------------|
| Stockholders' equity  | <b>386,064</b>      | 410,701             |
| <b>Total liabilities and stockholders' equity</b>                   | <b>\$ 4,399,601</b> | <b>\$ 4,195,989</b> |
| Excess of interest-earning assets over interest-bearing liabilities | <b>\$ 431,421</b>   | \$ 467,056          |
| <b>Net interest and dividend income</b>                             | <b>\$ 33,406</b>    | <b>\$ 30,893</b>    |
| Interest rate spread  | <b>3.56 %</b>       | 3.32 %              |
| <b>Net interest margin</b>  | <b>3.61 %</b>       | <b>3.41 %</b>       |

- (1) Weighted average yields have been computed on a tax-equivalent basis using a 35% effective tax rate.
- (2) Nonperforming loans are included in average balance computations.
- (3) Balances are reflected net of unearned income.
- (4) Includes securities available-for-sale.
- (5) Includes reverse mortgages.
- (6) Average Balances and related yield are calculated using the fair value of available-for-sale securities.
- (7) Includes residential mortgage loans HFS
- (8) Includes bonds payable related to the reverse mortgage securitization trust consolidation

**Table of Contents**

|  | Nine Months Ended September 30, |                |                    |                     |                |                    |
|--|---------------------------------|----------------|--------------------|---------------------|----------------|--------------------|
|  | 2013                            |                |                    | 2012                |                |                    |
|  | Average<br>Balance              | Interest       | Yield/<br>Rate (1) | Average<br>Balance  | Interest       | Yield/<br>Rate (1) |
| (Dollars In Thousands)   |                                 |                |                    |                     |                |                    |
| <b>Assets:</b>   |                                 |                |                    |                     |                |                    |
| Interest-earning assets:   |                                 |                |                    |                     |                |                    |
| Loans (2) (3):   |                                 |                |                    |                     |                |                    |
| Commercial real estate loans   | \$ 791,222                      | \$ 28,143      | 4.74 %             | \$ 729,599          | \$ 26,717      | 4.88 %             |
| Residential real estate loans (8)  | 254,154                         | 7,631          | 4.00               | 276,400             | 9,211          | 4.44               |
| Commercial loans   | 1,506,616                       | 50,467         | 4.45               | 1,459,698           | 51,891         | 4.73               |
| Consumer loans   | 285,772                         | 10,027         | 4.69               | 285,701             | 10,244         | 4.79               |
| Loans held for sale (7)  |                                 |                |                    | 7,113               | 122            | 2.29               |
| <b>Total loans</b>   | <b>2,837,764</b>                | <b>96,268</b>  | <b>4.52</b>        | <b>2,758,511</b>    | <b>98,185</b>  | <b>4.76</b>        |
| Mortgage-backed securities (4) (6)   | 744,812                         | 10,726         | 1.92               | 817,253             | 14,953         | 2.44               |
| Reverse mortgages and investment securities (4) (5) (6)                    | 84,001                          | 1,461          | 2.91               | 50,152              | 335            | 0.99               |
| Other interest-earning assets  | 34,924                          | 134            | 0.51               | 33,208              | 27             | 0.11               |
| <b>Total interest-earning assets</b>                                       | <b>3,701,501</b>                | <b>108,589</b> | <b>3.94</b>        | <b>3,659,124</b>    | <b>113,500</b> | <b>4.16</b>        |
| Allowance for loan losses  | (43,417)                        |                |                    | (49,140)            |                |                    |
| Cash and due from banks  | 78,444                          |                |                    | 90,969              |                |                    |
| Cash in non-owned ATMs   | 421,573                         |                |                    | 363,497             |                |                    |
| Bank-owned life insurance  | 62,978                          |                |                    | 63,465              |                |                    |
| Other noninterest-earning assets   | 122,792                         |                |                    | 123,228             |                |                    |
| <b>Total assets</b>  | <b>\$ 4,343,871</b>             |                |                    | <b>\$ 4,251,143</b> |                |                    |
| <b>Liabilities and Stockholders Equity:</b>                                |                                 |                |                    |                     |                |                    |
| Interest-bearing liabilities:  |                                 |                |                    |                     |                |                    |
| Interest-bearing deposits:   |                                 |                |                    |                     |                |                    |
| Interest-bearing demand  | \$ 544,125                      | \$ 369         | 0.09 %             | \$ 395,081          | \$ 157         | 0.05 %             |
| Money market   | 775,121                         | 832            | 0.14               | 754,942             | 1,357          | 0.24               |
| Savings  | 393,544                         | 161            | 0.05               | 388,894             | 361            | 0.12               |
| Customer time deposits   | 547,126                         | 3,692          | 0.90               | 739,073             | 7,886          | 1.43               |
| <b>Total interest-bearing customer deposits</b>                            | <b>2,259,916</b>                | <b>5,054</b>   | <b>0.30</b>        | <b>2,277,990</b>    | <b>9,761</b>   | <b>0.57</b>        |
| Brokered certificates of deposit   | 178,522                         | 459            | 0.34               | 283,169             | 891            | 0.42               |
| <b>Total interest-bearing deposits</b>                                     | <b>2,438,438</b>                | <b>5,513</b>   | <b>0.30</b>        | <b>2,561,159</b>    | <b>10,652</b>  | <b>0.56</b>        |
| FHLB of Pittsburgh advances  | 561,357                         | 1,376          | 0.32               | 466,266             | 4,985          | 1.40               |
| Trust preferred borrowings   | 67,011                          | 1,005          | 1.98               | 67,011              | 1,114          | 2.18               |
| Senior Debt  | 55,000                          | 2,830          | 6.86               | 7,026               | 353            | 6.60               |
| Other borrowed funds (9)   | 141,719                         | 823            | 0.77               | 136,282             | 895            | 0.88               |
| <b>Total interest-bearing liabilities</b>                                  | <b>3,263,525</b>                | <b>11,547</b>  | <b>0.47</b>        | <b>3,237,744</b>    | <b>17,999</b>  | <b>0.74</b>        |
| Noninterest-bearing demand deposits  | 638,289                         |                |                    | 574,708             |                |                    |
| Other noninterest-bearing liabilities                                      | 30,763                          |                |                    | 33,922              |                |                    |
| Stockholders equity  | 411,294                         |                |                    | 404,769             |                |                    |
| <b>Total liabilities and stockholders equity</b>                           | <b>\$ 4,343,871</b>             |                |                    | <b>\$ 4,251,143</b> |                |                    |
| <b>Excess of interest-earning assets over interest-bearing liabilities</b> | <b>\$ 437,976</b>               |                |                    | <b>\$ 421,380</b>   |                |                    |

Edgar Filing: WSFS FINANCIAL CORP - Form 10-Q

|                      |                  |           |
|----------------------|------------------|-----------|
| Net interest income  | <b>\$ 97,042</b> | \$ 95,501 |
| Interest rate spread | <b>3.47 %</b>    | 3.42 %    |
| Net interest margin  | <b>3.52 %</b>    | 3.49 %    |

- (1) Weighted average yields have been computed on a tax-equivalent basis using a 35% effective tax rate.
- (2) Nonperforming loans are included in average balance computations.
- (3) Balances are reflected net of unearned income.
- (4) Includes securities available-for-sale.
- (5) Includes reverse mortgages.
- (6) Average Balances and related yield are calculated using fair value of available-for-sale securities.
- (7) Represents loans held for sale in conjunction with asset disposition strategies.
- (8) Includes residential mortgage loans HFS.
- (9) Includes bonds payable related to the reverse mortgage securitization trust consolidation.

## **Table of Contents**

The net interest margin for the third quarter of 2013 was 3.61%, a 20 basis point increase compared to 3.41% for the third quarter of 2012. The increase in net interest margin from the third quarter of 2012 included one-time net adjustments totaling \$446,000, largely related to prepayment and other fees on two loan relationships that were paid off at the end of the quarter. In addition, the net interest margin increased as a result of securities portfolio yield improvement, prudent deposit and loan pricing and improved balance sheet mix. This included several initiatives undertaken in late 2012 and into 2013, including mortgage-banking securities deleveraging strategy; the prepayment of higher rate Federal Home Loan Bank ( FHLB ) borrowing; and the intentional reduction in higher-cost CDs.

The interest margin for the nine months ended September 30, 2013 was 3.52% compared to the 3.49% for the same period in 2012. Similar to the quarterly discussion above, the margin increased due to one-time net adjustments, securities portfolio yield improvement, prudent deposit and loan pricing and favorable balance sheet mix based on several initiatives we had taken. Partially offsetting these increases were higher interest expenses due to the issuance of \$55 million of Senior Notes in August 2012 to provide liquidity and capital flexibility at the holding company level, a decrease in our residential loans due to our strategy of reselling these loans, and a decline in our MBS portfolio.

### **Provision for Loan Losses**

Our provision for loan losses is based on the inherent risk of our loans and considers various factors including collateral values, trends in asset quality, level of delinquent loans and concentrations. In addition, regional economic conditions are also taken into consideration. The provision for loan losses was \$2.0 million and \$5.9 million, respectively, for the three and nine months ended September 30, 2013, compared to \$3.8 and \$28.4 for the same period in 2012.

Our allowance for loan losses of \$41.4 million at September 30, 2013 decreased \$2.5 million from \$43.9 million at December 31, 2012. In addition, the ratio of allowance to loan losses to total gross loans was 1.44% at September 30, 2013, compared to 1.58% at December 31, 2012. These decreases reflect that overall credit quality continued to improve over 2012 results:

Net charge-offs were \$8.4 million for the nine months ended September 30, 2013 compared to \$44.2 million for the nine months ended September 30, 2012.

Total problem loans (all criticized, classified, and non-performing loans) improved to 40.5% of Tier 1 Capital plus allowance for loan losses, compared to 52.5% at December 31, 2012 and 59.7% at September 30, 2012.

Nonperforming loans decreased to \$38.2 million as of September 30, 2013 compared to \$62.5 million as of December 31, 2012.

Total loan delinquency increased to 1.84% as of September 30, 2013, compared to 1.62% as of December 31, 2012 as a result of one \$19.0 million relationship with a highly seasonal business. This relationship is evaluated monthly for accrual status.

**Table of Contents**

|   | <b>For the Nine Months<br/>Ended September 30,</b> |             |
|---|--|-------------|
|   | <b>2013</b>  | <b>2012</b> |
| (Dollars in Thousands)  |  |             |
| Beginning balance   | <b>\$ 43,922</b>                                   | \$ 53,080   |
| Provision for loan losses   | <b>5,880</b>                                       | 28,379      |
| Charge-offs:  |  |             |
| Residential real estate   | <b>985</b>   | 3,343       |
| Commercial real estate  | <b>1,824</b>                                       | 5,600       |
| Construction  | <b>1,344</b>                                       | 10,680      |
| Commercial  | <b>2,311</b>                                       | 11,920      |
| Owner-occupied commercial   | <b>68</b>  | 3,012       |
| Overdrafts  | <b>734</b>   | 813         |
| Consumer  | <b>3,419</b>                                       | 4,680       |
| <b>Total charge-offs</b>  | <b>10,685</b>                                      | 40,048      |
| Recoveries:   |  |             |
| Residential real estate   | <b>51</b>  | 171         |
| Commercial real estate  | <b>442</b>   | 382         |
| Construction  | <b>106</b>   | 1,642       |
| Commercial  | <b>900</b>   | 1,482       |
| Owner-occupied commercial   | <b>100</b>   | 13          |
| Overdrafts  | <b>315</b>   | 297         |
| Consumer  | <b>400</b>   | 200         |
| <b>Total recoveries</b>   | <b>2,314</b>                                       | 4,187       |
| <b>Net charge-offs</b>  | <b>8,371</b>                                       | 35,861      |
| Ending balance  | <b>\$ 41,431</b>                                   | \$ 45,598   |
| <b>Net charge-offs to average gross loans outstanding, net of unearned income (1)</b> | <b>0.39 %</b>                                      | 1.75 %      |

(1) Ratios for the nine months ended September 30, 2013 and 2012 annualized.

**Noninterest Income**

Noninterest income increased \$3.0 million during the third quarter of 2013 from the same period a year ago. Excluding securities gains in both periods, the reverse mortgage consolidation gain in 2013, the unanticipated BOLI income in 2012 and the impact from a Cash Connect billing change, noninterest income increased by \$1.4 million, or 8% from the same period in 2012. This increase was primarily the result of growth in credit/debit card and fees (largely related to the ATM division), which increased \$636,000, or 11%, and investment management and fiduciary revenue, which increased \$578,000, or 18%, reflecting continued fundamental momentum in these businesses. The increase in noninterest income also reflected continued growth and success in the traditional banking franchise.

For the nine months ended September 30, 2013 noninterest income decreased \$5.1 million to \$60.4 million compared to the same period in 2012. Excluding the same items described in the paragraph above, noninterest income increased by \$7.0 million. This increase was primarily the result of growth in investment management and fiduciary revenue of \$1.9 million and a \$1.2 million increase in credit/debit card and ATM fees (largely related to our ATM division) reflecting growth in all business lines. In addition, a billing methodology change related to our Cash Connect division increased noninterest income by \$3.1 million in 2013 (which also increased noninterest expenses by a similar amount).

**Table of Contents****Noninterest Expense**

Noninterest expense for the third quarter of 2013 increased \$656,000, or 2% from the same period in 2012. Excluding the impact of a change in the method of billing by Cash Connect (\$900,000, net), noninterest expenses decreased by \$335,000 below the same period in the prior year. This decrease was mainly due to a \$1.6 million reduction in loan workout and OREO costs, which were partially offset by a \$706,000 increase in salaries, benefits and other compensation.

For the nine months ended September 30, 2013, noninterest expense increased \$2.2 million, or 2% compared to the same period in 2012. Excluding the \$2.8 million impact from the billing change at Cash Connect, noninterest expense decreased by \$667,000. This was mainly due to a \$3.5 million decrease in loan workout and OREO costs and a \$1.2 million decrease in regulatory costs. These decreases were partially offset by a \$2.5 million increase in salaries, benefits and other compensation costs related to our growth and increased incentives related to our improved performance.

**Income Taxes**

We and our subsidiaries file a consolidated federal income tax return and separate state income tax returns. Income taxes are accounted for in accordance with ASC 740, which requires the recording of deferred income taxes for tax consequences of temporary differences. We recorded an income tax expense of \$7.2 million and \$18.4 million during the three and nine months ended September 30, 2013, respectively, compared to an income tax expense of \$4.8 million and \$12.7 million for the same periods in 2012.

The third quarter of 2013 included the recognition of \$200,000 of tax benefits related to the completion of an IRS audit of our 2010 tax return. The third quarter of 2012 included the recognition of tax benefits related to \$1.0 million of tax-free income from life insurance proceeds received from our BOLI investment. Our effective tax rate was 33.7% and 34.6% for the three and nine months ended September 30, 2013, respectively, compared to 32.3% and 34.9% during the same periods in 2012. Excluding the IRS audit impact and tax-free BOLI proceeds, our effective tax rates were 34.7% and 34.9% for the three and nine months ended September 30, 2013, respectively, compared to 34.7% and 35.8% during the same periods in 2012.

The effective tax rate reflects the recognition of certain tax benefits in the financial statements including those benefits from tax-exempt interest income, federal low-income housing tax credits, and BOLI income. These tax benefits are offset by the tax effect of stock-based compensation expense related to incentive stock options and a provision for state income tax expense.

We frequently analyze our projections of taxable income and make adjustments to our provision for income taxes accordingly.

**RECONCILIATION OF NON-GAAP MEASUREMENT TO GAAP**

The following table provides a reconciliation of tangible common book value per share of common stock to book value per share of common stock, the most directly comparable GAAP financial measure. We believe this measure is important to management and investors to better understand and assess changes from period to period in stockholders' equity exclusive of changes in intangible assets.

|  | September 30,<br>2013 | December 31,<br>2012 |
|--|-----------------------|----------------------|
|  | (In Thousands)        |                      |
| <b><u>Tangible Common Book Value per Share of Common Stock</u></b> |                       |                      |
| End of period balance sheet data:                                  |                       |                      |
| <b>Stockholders' equity</b>  | <b>\$ 373,951</b>     | \$ 421,054           |
| Goodwill and other intangible assets                               | <b>(32,939)</b>       | (33,320)             |
| Preferred equity, net of discount                                  |                       | (52,474)             |
| <b>Tangible common equity (numerator)</b>                          | <b>\$ 341,012</b>     | \$ 335,260           |
| <b>Shares of common stock outstanding (denominator)</b>            | <b>8,844</b>          | 8,773                |
| <b>Book value per share of common stock</b>                        | <b>\$ 42.28</b>       | \$ 47.99             |



Edgar Filing: WSFS FINANCIAL CORP - Form 10-Q

|  |                 |                 |
|--|-----------------|-----------------|
| Goodwill and other intangible assets                 | (3.72)          | (3.80)          |
| Preferred equity, net of discount                    |                 | (5.98)          |
| <b>Tangible book value per share of common stock</b> | <b>\$ 38.56</b> | <b>\$ 38.21</b> |

---

**Table of Contents****RECENT ACCOUNTING PRONOUNCEMENTS**

In December 2011, the FASB issued Accounting Standards Update or ASU No. 2011-11, *Disclosures About Offsetting Assets and Liabilities*. This project began as an attempt to converge the offsetting requirements under U.S. GAAP and International Financial Reporting Standards (IFRS). However, as the FASB and International Accounting Standards Board were not able to reach a converged solution with regards to offsetting requirements, they each developed convergent disclosure requirements to assist in reconciling differences in the offsetting requirements under U.S. GAAP and IFRS. The new disclosure requirements mandate that entities disclose both gross and net information about instruments and transactions eligible for offset in the statement of financial position as well as instruments and transactions subject to an agreement similar to a master netting arrangement. ASU No. 2011-11 also requires disclosure of collateral received and posted in connection with master netting agreements or similar arrangements. In January 2013, the FASB issued ASU No. 2013-01, *Clarifying the Scope of Disclosures about Offsetting Assets and Liabilities*. The provisions of ASU No. 2013-01 limit the scope of the new balance sheet offsetting disclosures to the following financial instruments, to the extent they are offset in the financial statements or subject to an enforceable master netting arrangement or similar agreement, irrespective of whether they are offset in the statement of financial position: (1) derivative financial instruments; (2) repurchase agreements and reverse repurchase agreements; and (3) securities borrowing and securities lending transactions. We adopted the provisions of ASU No. 2011-11 and ASU No. 2013-01 effective January 1, 2013. The provisions of ASU No. 2011-11 and ASU No. 2013-01 only impacted the disclosure requirements related to the offsetting of assets and liabilities and information about instruments and transactions eligible for offset in the statement of financial position, the adoption of this amendment did not have a material effect on our Consolidated Financial Statements.

In July 2012, the FASB issued ASU No. 2012-02, *Intangibles—Goodwill and Other (Topic 350): Testing Indefinite-Lived Intangible Assets for Impairment* which allows an entity testing an indefinite-lived intangible asset for impairment the option of performing a qualitative assessment before calculating the fair value of the asset. This update also addresses circumstances that a company should consider in interim periods, but does not remove the requirement for testing of indefinite-lived intangible assets for impairment annually and between annual tests if there is a change in events and circumstances. The provisions of ASU No. 2012-02 became effective for the interim reporting period ended March 31, 2013 and did not have a material effect on our Consolidated Financial Statements.

In February 2013, the FASB issued ASU No. 2013-02, *Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income*, to improve the transparency of reporting these reclassifications. ASU No. 2013-02 does not amend any existing requirements for reporting net income or other comprehensive income in the financial statements. ASU No. 2013-02 requires an entity to disaggregate the total change of each component of other comprehensive income (e.g., unrealized gains or losses on available-for-sale investment securities) and separately present reclassification adjustments and current period other comprehensive income. The provisions of ASU No. 2013-02 also requires that entities present either in a single note or parenthetically on the face of the financial statements, the effect of significant amounts reclassified from each component of accumulated other comprehensive income based on its source (e.g., unrealized gains or losses on available-for-sale investment securities) and the income statement line item affected by the reclassification (e.g., realized gains (losses) on sales of investment securities). If a component is not required to be reclassified to net income in its entirety (e.g., amortization of defined benefit plan items), entities would instead cross reference to the related note to the financial statements for additional information (e.g., pension note). We adopted the provisions of ASU No. 2013-02 prospectively for reporting periods ending after December 15, 2012. The adoption of this amendment did not have a material effect on our Consolidated Financial Statements.

In July 2013, the FASB issued ASU No. 2013-10, *Inclusion of the Fed Funds Effective Swap Rate (or Overnight Index Swap Rate) as a Benchmark Interest Rate for Hedge Accounting Purposes*. These amendments allow the Fed Funds Effective Swap Rate (OIS) to be used as a U.S. benchmark interest rate for hedge accounting purposes, in addition to the current benchmark rates of UST (the rate on direct Treasury obligations of the U.S. government) and LIBOR (the London Interbank Offered Rate on swaps). The amendments were effective on a prospective basis for new or redesignated hedging relationships on July 17, 2013. The adoption of this amendment did not have material effect on our Consolidated Financial Statements.

In July 2013, the FASB issued ASU No. 2013-11, *Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists*, to clarify the balance sheet presentation of an unrecognized tax benefit when a net operating loss carryforward, a similar tax loss, or a tax credit carryforward exists. The ASU requires an unrecognized tax benefit, or a portion of an unrecognized tax benefit, to be presented in the financial statements as a reduction to a deferred tax asset for a net operating loss carryforward, a similar tax loss, or a tax credit carryforward, except as follows. To the extent a net operating loss carryforward, a similar tax loss, or a tax credit carryforward is not available at the reporting date under the tax law of the applicable jurisdiction to settle any additional income taxes that would result from the disallowance of a tax position or the tax law of the applicable jurisdiction does not require the entity to use, and the entity does not intend to use, the deferred tax asset for such purpose, the unrecognized tax benefit should be presented in the financial statements as a liability and should not be combined with deferred tax assets. The ASU is effective for fiscal years, and interim periods within those years, beginning after December 15, 2013. The adoption is not expected to have a material effect on our Consolidated Financial Statements.



---

**Table of Contents**

**RECENT LEGISLATION**

In July 2013, the Board of Governors of the Federal Reserve System, FDIC and the OCC approved final rules (the Final Capital Rules ) implementing revised capital rules to reflect the requirements of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the Dodd-Frank Act ) and the Basel III international capital standards. Among other things, the Final Capital Rules establish a new capital ratio of common equity Tier 1 capital of 4.5% and a common equity Tier 1 capital conservation buffer of 2.5% of risk-weighted assets; increase the minimum ratio of Tier 1 capital ratio from 4% to 6% and include a minimum leverage ratio of 4%; place an emphasis on common equity Tier 1 capital and implement the Dodd-Frank Act phase-out of certain instruments from Tier 1 capital; and change the risk weights assigned to certain instruments. Failure to meet these standards would result in limitations on capital distributions as well as executive bonuses. The Final Capital Rules will be applicable to us on January 1, 2015 with conservation buffers phasing in over the subsequent 5 years.

While it is still too early to fully analyze the impact of all aspects of the new regulatory guidance, we currently have strong capital levels and are significantly above well capitalized levels under the current guidelines.

On July 31, 2013, a Federal District Court judge ruled that the Federal Reserve inflated debit interchange fees when implementing the Durbin amendment of the Dodd-Frank Act in 2011. The judge ruled that the Federal Reserve erred in using criteria outside of the scope Congress intended to determine the fee cap, which the Federal Reserve set at 21 cents per transaction. The judge also ruled that the network options for both signature and PIN transactions were not set appropriately in accordance with the Dodd-Frank Act. The judge has stayed this decision to give the Federal Reserve time to adopt interim standards and has scheduled a conference with the parties on August 14, 2013. If not overturned on appeal, this ruling could significantly affect debit fees for the banking industry and for us. However, these developments are preliminary and the impact on us is not determinable at this time.

The many provisions of the Dodd-Frank Act are so extensive that implementation by regulators is still ongoing. Several of the key regulations included in the original law have been delayed since the law s passing, making an assessment of the Dodd Frank Act s full effect on us not possible at this time.

**Item 3. Quantitative and Qualitative Disclosures About Market Risk**

Incorporated herein by reference from Item 2, of this Quarterly Report on Form 10-Q.

**Item 4. Controls and Procedures**

- (a) **Evaluation of disclosure controls and procedures.** Based on their evaluation of our disclosure controls and procedures (as defined in Rules 13a-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act )), our principal executive officer and the principal financial officer have concluded that as of the end of the period covered by this Quarterly Report on Form 10-Q such disclosure controls and procedures are effective to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC s rules and forms.
- (b) **Changes in internal control over financial reporting.** During the quarter ended September 30, 2013, there was no change in our internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

**Part II. OTHER INFORMATION**

**Item 1. Legal Proceedings**

Incorporated herein by reference to Note 12 Legal Proceedings to the Consolidated Financial Statements

**Item 1A. Risk Factors**

Our management does not believe there have been any material changes to the risk factors previously disclosed under Item 1A. of the Company's Form 10-K for the year ended December 31, 2012, previously filed with the SEC.

**Table of Contents****Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

The following tables represent information with respect to repurchases preferred stock made by us during the three months ended September 30, 2013.

| <b>Preferred</b> | Total Number of<br>Shares Purchased | Average<br>Price<br>Paid Per Share | Total<br>Number of<br>Shares<br>Purchased<br>as Part of Publicity<br>Announced<br>Plans<br>or Programs | Maximum Number<br>of Shares that<br>May<br>Yet Be<br>Purchased<br>Under the<br>Plans or<br>Programs |
|------------------|-------------------------------------|------------------------------------|--|---|
| 2013             |                                     |                                    |  |   |
| July             |                                     | \$                                 |  |   |
| August           | 32,625                              | 1,000.00                           |  |   |
| September        |                                     |                                    |  |   |
| Total (1)        | 32,625                              | \$ 1,000.00                        |  |   |

- (1) The shares repurchased were not part of a publicly announced repurchase plan or program. These shares were owned by preferred stockholders.

**Item 3. Defaults upon Senior Securities**

Not applicable

**Item 4. Mine Safety Disclosures**

Not applicable

**Item 5. Other Information**

Not applicable

**Item 6. Exhibits**

- (a) Exhibit 31.1 Certification of CEO pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- (b) Exhibit 31.2 Certification of CFO pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- (c) Exhibit 32 Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- (d) Exhibit 101.INS XBRL Instance Document
- (e) Exhibit 101.SCH XBRL Schema Document
- (f) Exhibit 101.CAL XBRL Calculation Linkbase Document
- (g) Exhibit 101.LAB XBRL Labels Linkbase Document
- (h) Exhibit 101.PRE XBRL Presentation Linkbase Document
- (i) Exhibit 101.DEF XBRL Definition Linkbase Document



**Table of Contents**

**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

**WSFS FINANCIAL CORPORATION**

Date: November 12, 2013

/s/ Mark A. Turner  
Mark A. Turner  
President and Chief Executive Officer  
(Principal Executive Officer)

Date: November 12, 2013

/s/ Stephen A. Fowle  
Stephen A. Fowle  
Executive Vice President and  
Chief Financial Officer  
(Principal Financial and Accounting Officer)