

HMN FINANCIAL INC
Form 10-Q
November 04, 2015
UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2015

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 0-24100

HMN FINANCIAL, INC.

(Exact name of registrant as specified in its charter)

Delaware 41-1777397
(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

1016 Civic Center Drive N.W., Rochester, MN 55901
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: (507) 535-1200

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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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or 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 Smaller reporting company
(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock as of the latest practicable date.

Class	Outstanding at October 20, 2015
Common stock, \$0.01 par value	4,482,893

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Part I – FINANCIAL INFORMATION**Item 1: Financial Statements****HMN FINANCIAL, INC. AND SUBSIDIARIES****Consolidated Balance Sheets**

<i>(Dollars in thousands)</i>	September 30, 2015 (unaudited)	December 31, 2014
Assets		
Cash and cash equivalents	\$ 10,359	46,634
Securities available for sale:		
Mortgage-backed and related securities (amortized cost \$6,979 and \$2,755)	7,080	2,909
Other marketable securities (amortized cost \$138,254 and \$135,772)	138,258	134,925
	145,338	137,834
Loans held for sale	5,153	2,076
Loans receivable, net	432,174	365,113
Accrued interest receivable	2,162	1,713
Real estate, net	2,504	3,103
Federal Home Loan Bank stock, at cost	691	777
Mortgage servicing rights, net	1,446	1,507
Premises and equipment, net	7,426	6,982
Core deposit intangible	411	0
Prepaid expenses and other assets	1,040	1,157
Deferred tax asset, net	10,213	10,530
Total assets	\$ 618,917	577,426
Liabilities and Stockholders' Equity		
Deposits	\$ 531,586	496,750
Other borrowings	10,000	0
Accrued interest payable	252	93
Customer escrows	1,274	788
Accrued expenses and other liabilities	7,095	3,782
Total liabilities	550,207	501,413
Commitments and contingencies		
Stockholders' equity:		
Serial preferred stock (\$.01 par value): authorized 500,000 shares; issued and outstanding shares 0 and 10,000	0	10,000
Common stock (\$.01 par value): authorized 16,000,000; issued shares 9,128,662	91	91
Additional paid-in capital	50,314	50,207

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Retained earnings, subject to certain restrictions	79,446	77,805
Accumulated other comprehensive income (loss), net of tax	63	(418)
Unearned employee stock ownership plan shares	(2,465)	(2,610)
Treasury stock, at cost 4,645,769 and 4,658,323 shares	(58,739)	(59,062)
Total stockholders' equity	68,710	76,013
Total liabilities and stockholders' equity	\$ 618,917	577,426

See accompanying notes to consolidated financial statements.

HMN FINANCIAL, INC. AND SUBSIDIARIES**Consolidated Statements of Comprehensive Income**

(unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
<i>(Dollars in thousands, except per share data)</i>				
Interest income:				
Loans receivable	\$4,860	4,669	13,751	14,398
Securities available for sale:				
Mortgage-backed and related	35	38	87	131
Other marketable	468	378	1,455	889
Cash equivalents	26	45	48	157
Other	1	1	3	3
Total interest income	5,390	5,131	15,344	15,578
Interest expense:				
Deposits	231	297	705	937
Federal Home Loan Bank advances	0	0	1	0
Other borrowings	166	0	408	0
Total interest expense	397	297	1,114	937
Net interest income	4,993	4,834	14,230	14,641
Provision for loan losses	(56)	(989)	(239)	(4,777)
Net interest income after provision for loan losses	5,049	5,823	14,469	19,418
Non-interest income:				
Fees and service charges	863	903	2,489	2,627
Mortgage servicing fees	262	263	778	787
Gain on sales of loans	613	804	1,428	1,480
Gain on acquisition	289	0	289	0
Other	204	224	708	710
Total non-interest income	2,231	2,194	5,692	5,604
Non-interest expense:				
Compensation and benefits	3,299	3,193	10,285	9,944
Losses (gains) on real estate owned	168	(78)	121	(1,130)
Occupancy	936	896	2,741	2,654
Deposit insurance	125	74	269	328
Data processing	254	240	753	735
Other	1,187	1,100	3,031	3,055
Total non-interest expense	5,969	5,425	17,200	15,586
Income before income tax expense	1,311	2,592	2,961	9,436

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Income tax expense	491	1,054	1,095	3,736
Net income	\$820	1,538	1,866	5,700
Preferred stock dividends	0	(360)	(108)	(1,417)
Net income for common shareholders	820	1,178	1,758	4,283
Other comprehensive income (loss), net of tax	275	(70)	481	302
Comprehensive income attributable to common shareholders	\$1,095	1,108	2,239	4,585
Basic earnings per common share	\$0.20	0.29	0.43	1.06
Diluted earnings per common share	\$0.18	0.25	0.38	0.93

See accompanying notes to consolidated financial statements.

HMN FINANCIAL, INC. AND SUBSIDIARIES

Consolidated Statement of Stockholders' Equity

For the Nine-Month Period Ended September 30, 2015

(unaudited)

	Serial Preferred Stock	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Unearned Employee Stock Ownership Plan Shares	Treasury Stock	Total Stock- Holders' Equity
<i>(Dollars in thousands)</i>								
Balance, December 31, 2014	\$ 10,000	91	50,207	77,805	(418)	(2,610)	(59,062)	76,013
Net income				1,866				1,866
Other comprehensive income					481			481
Redemption of preferred stock	(10,000)							(10,000)
Restricted stock awards			(332)				332	0
Restricted stock awards forfeiture			9				(9)	0
Amortization of restricted stock awards			387					387
Dividends on preferred stock				(225)				(225)
Earned employee stock ownership plan shares			43			145		188
Balance, September 30, 2015	\$ 0	91	50,314	79,446	63	(2,465)	(58,739)	68,710

See accompanying notes to consolidated financial statements.

HMN FINANCIAL, INC. AND SUBSIDIARIES**Consolidated Statements of Cash Flows**

(unaudited)

	Nine Months Ended	
	September 30,	
	2015	2014
<i>(Dollars in thousands)</i>		
Cash flows from operating activities:		
Net income	\$1,866	5,700
Adjustments to reconcile net income to cash provided by operating activities:		
Provision for loan losses	(239)	(4,777)
Depreciation	516	416
Amortization of (discounts) premiums, net	(10)	7
Amortization of deferred loan fees	(194)	(175)
Amortization of core deposit intangible	9	0
Amortization of purchased loan market adjustments	(112)	0
Amortization of mortgage servicing rights and servicing costs	427	385
Capitalized mortgage servicing rights	(366)	(219)
Loss (gain) on sales of real estate	121	(1,130)
Gain on sales of loans	(1,428)	(1,480)
Proceeds from sale of loans held for sale	55,995	42,724
Disbursements on loans held for sale	(50,952)	(29,032)
Amortization of restricted stock awards	387	176
Amortization of unearned ESOP shares	145	145
Earned employee stock ownership shares priced above original cost	43	37
Stock option compensation	0	1
(Increase) decrease in accrued interest receivable	(254)	167
Increase (decrease) in accrued interest payable	148	(46)
Decrease in other assets	195	170
Increase in other liabilities	3,252	3,508
Other, net	33	388
	9,582	16,965
Net cash provided by operating activities		
Cash flows from investing activities:		
Principal collected on securities available for sale	1,257	1,726
Proceeds collected on maturities of securities available for sale	118,570	55,000
Purchases of securities available for sale	(109,070)	(89,000)
Purchase of Federal Home Loan Bank Stock	(119)	0
Redemption of Federal Home Loan Bank Stock	205	7
Proceeds from sales of real estate and premises	772	4,382
Net (increase) decrease in loans receivable	(49,252)	11,898
Gain on acquisition	(289)	0
Acquisition of Kasson State Bank (net of cash acquired)	4,816	0

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Purchases of premises and equipment	(570)	(538)
Net cash used by investing activities	(33,680)	(16,525)
Cash flows from financing activities:		
Decrease in deposits	(12,438)	(49,024)
Redemption of preferred stock	(10,000)	(10,000)
Dividends to preferred stockholders	(225)	(5,604)
Proceeds from borrowings	41,000	0
Repayment of borrowings	(31,000)	0
Increase in customer escrows	486	679
Net cash used by financing activities	(12,177)	(63,949)
Decrease in cash and cash equivalents	(36,275)	(63,509)
Cash and cash equivalents, beginning of period	46,634	120,686
Cash and cash equivalents, end of period	\$10,359	57,177
Supplemental cash flow disclosures:		
Cash paid for interest	\$954	983
Cash paid for income taxes	191	0
Supplemental noncash flow disclosures:		
Transfer of loans to real estate	110	142
Loans transferred to loans held for sale	6,701	11,954

See accompanying notes to consolidated financial statements.

HMN FINANCIAL, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(unaudited)

September 30, 2015 and 2014

(1) HMN Financial, Inc.

HMN Financial, Inc. (HMN or the Company) is a stock savings bank holding company that owns 100 percent of Home Federal Savings Bank (the Bank). The Bank has a community banking philosophy and operates retail banking and loan production facilities in Minnesota, Iowa, and Wisconsin. The Bank has two wholly owned subsidiaries, Osterud Insurance Agency, Inc. (OIA), which offers financial planning products and services, and HFSB Property Holdings, LLC (HPH), which acts as an intermediary for the Bank in holding and operating certain foreclosed properties.

The consolidated financial statements included herein are for HMN, the Bank, OIA and HPH. All significant intercompany accounts and transactions have been eliminated in consolidation.

(2) Basis of Preparation

The accompanying unaudited consolidated financial statements were prepared in accordance with instructions for Form 10-Q and, therefore, do not include all disclosures necessary for a complete presentation of the consolidated balance sheets, consolidated statements of comprehensive income, consolidated statement of stockholders' equity and consolidated statements of cash flows in conformity with U.S. generally accepted accounting principles. However, all normal recurring adjustments which are, in the opinion of management, necessary for the fair presentation of the interim financial statements have been included. The results of operations for the nine-month period ended September 30, 2015 are not necessarily indicative of the results which may be expected for the entire year.

(3) Derivative Instruments and Hedging Activities

The Company had commitments outstanding to extend credit to future borrowers that had not closed prior to the end of the quarter. The Company intends to sell these commitments, which are referred to as its mortgage pipeline. As commitments to originate or purchase loans enter the mortgage pipeline, the Company generally enters into commitments to sell the mortgage pipeline into the secondary market on a firm commitment or best efforts basis. The commitments to originate, purchase or sell loans on a firm commitment basis are derivatives and are recorded at market value. As a result of marking to market the mortgage pipeline and the related firm commitments to sell at

September 30, 2015, the Company recorded an increase in other assets of \$76,000, an increase in other liabilities of \$9,000 and a gain included in the gain on sales of loans of \$67,000.

The current commitments to sell loans held for sale are derivatives that do not qualify for hedge accounting. As a result, these derivatives are marked to market and the related loans held for sale are recorded at the lower-of-cost-or-market. As of and for the nine months ended September 30, 2015, the Company recorded an increase in other liabilities of \$75,000 and a loss included in the gain on sales of loans of \$75,000.

(4) Fair Value Measurements

ASC 820, *Fair Value Measurements*, establishes a framework for measuring the fair value of assets and liabilities using a hierarchy system consisting of three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. These levels are:

Level 1 - Valuation is based upon quoted prices for identical instruments traded in active markets that the Company has the ability to access.

Level 2 - Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which significant assumptions are observable in the market.

Level 3 - Valuation is generated from model-based techniques that use significant assumptions not observable in the market and are used only to the extent that observable inputs are not available. These unobservable assumptions reflect our own estimates of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include use of option pricing models, discounted cash flow models and similar techniques.

The following table summarizes the assets and liabilities of the Company for which fair values are determined on a recurring basis as of September 30, 2015 and December 31, 2014.

Carrying value at September 30,
2015

<i>(Dollars in thousands)</i>	Total	Level 1	Level 2	Level 3
Securities available for sale	\$ 145,338	0	145,338	0
Mortgage loan commitments	93	0	93	0
Total	\$ 145,431	0	145,431	0

Carrying value at December 31,
2014

<i>(Dollars in thousands)</i>	Total	Level 1	Level 2	Level 3
Securities available for sale	\$ 137,834	0	137,834	0
Mortgage loan commitments	16	0	16	0
Total	\$ 137,850	0	137,850	0

There were no transfers between Levels 1, 2, or 3 during the three or nine-month periods ended September 30, 2015.

The Company may also be required, from time to time, to measure certain other financial assets at fair value on a nonrecurring basis in accordance with generally accepted accounting principles. These adjustments to fair value usually result from the application of the lower-of-cost-or-market accounting or write-downs of individual assets. For assets measured at fair value on a nonrecurring basis in the third quarter of 2015 that were still held at September 30, 2015, the following table provides the level of valuation assumptions used to determine each adjustment and the carrying value of the related individual assets or portfolios at September 30, 2015 and December 31, 2014.

Carrying value at September 30,
2015

<i>(Dollars in thousands)</i>	Total	Level 1	Level 2	Level 3	Three months ended	Nine months ended
					September 30, 2015	September 30, 2015

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					Total gains (losses)	Total gains (losses)
Loans held for sale	\$5,153	0	5,153	0	83	75
Mortgage servicing rights	1,446	0	1,446	0	0	0
Loans ⁽¹⁾	9,848	0	9,848	0	39	(203)
Real estate, net ⁽²⁾	2,504	0	2,504	0	(200)	(200)
Total	\$18,951	0	18,951	0	(78)	(328)

Carrying value at December 31,
2014

					Year ended
(Dollars in thousands)	Total	Level 1	Level 2	Level 3	December 31, 2014 Total gains (losses)
Loans held for sale	\$2,076	0	2,076	0	(1)
Mortgage servicing rights	1,507	0	1,507	0	0
Loans ⁽¹⁾	11,882	0	11,882	0	532
Real estate, net ⁽²⁾	3,103	0	3,103	0	(134)
Total	\$18,568	0	18,568	0	397

(1) Represents the carrying value and related specific reserves on loans for which adjustments are based on the appraised value of the collateral. The carrying value of loans fully charged-off is zero.

(2) Represents the fair value and related losses of foreclosed real estate and other collateral owned that were measured at fair value subsequent to their initial classification as foreclosed assets.

(5) Fair Value of Financial Instruments

Generally accepted accounting principles require interim reporting period disclosure about the fair value of financial instruments, including assets, liabilities and off-balance sheet items for which it is practicable to estimate fair value. The fair value hierarchy level for each asset and liability, as defined in note 4, have been included in the following table for September 30, 2015. The fair value estimates are made based upon relevant market information, if available, and upon the characteristics of the financial instruments themselves. Because no market exists for a significant portion of the Company's financial instruments, fair value estimates are based upon judgments regarding future expected loss experience, current economic conditions, risk characteristics of various financial instruments and other factors. The estimated fair value of the Company's financial instruments as of September 30, 2015 and December 31, 2014 are shown below.

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<i>(Dollars in thousands)</i>	September 30, 2015					Contract amount	December 31, 2014					
	Carrying amount	Estimated fair value	Fair value hierarchy				Carrying amount	Estimated fair value	Fair value hierarchy			
			Level 1	Level 2	Level 3				Level 1	Level 2	Level 3	
Financial assets:												
Cash and cash equivalents	\$10,359	10,359	10,359				46,634	46,634	46,634			
Securities available for sale	145,338	145,338		145,338			137,834	137,834		137,834		
Loans held for sale	5,153	5,153		5,153			2,076	2,076		2,076		
Loans receivable, net	432,174	430,694		430,694			365,113	364,509		364,509		
Federal Home Loan Bank stock	691	691		691			777	777		777		
Accrued interest receivable	2,162	2,162		2,162			1,713	1,713		1,713		
Financial liabilities:												
Deposits	531,586	531,310		531,310			496,750	496,494		496,494		
Other borrowings	10,000	10,025		10,025			0	0				
Accrued interest payable	252	252		252			93	93		93		
Off-balance sheet financial instruments:												
Commitments to extend credit	93	93				234,591	16	16				14
Commitments to sell loans	(114)	(114)				11,061	(30)	(30)				3,2

Cash and Cash Equivalents

The carrying amount of cash and cash equivalents approximates their fair value.

Securities Available for Sale

The fair values of securities were based upon quoted market prices for identical or similar instruments in active markets.

Loans Held for Sale

The fair values of loans held for sale were based upon quoted market prices for loans with similar interest rates and terms to maturity.

Loans Receivable, net

The fair value of the loan portfolio was calculated by discounting the scheduled cash flows through the estimated maturity using anticipated prepayment speeds and using discount rates that reflect the credit and interest rate risk inherent in each loan portfolio.

Federal Home Loan Bank Stock

The carrying amount of FHLB stock approximates its fair value.

Accrued Interest Receivable

The carrying amount of accrued interest receivable approximates its fair value since it is short-term in nature and does not present unanticipated credit concerns.

Deposits

The fair value of demand deposits, savings accounts and certain money market account deposits is the amount payable on demand at the reporting date. The fair value of fixed maturity certificates of deposit is estimated using the rates currently offered for deposits of similar remaining maturities. If the fair value of the fixed maturity certificates of deposit is calculated at less than the carrying amount, the carrying value of these deposits is reported as the fair value.

The fair value estimate for deposits does not include the benefit that results from the low cost funding provided by the Company's existing deposits and long-term customer relationships compared to the cost of obtaining different sources of funding. This benefit is commonly referred to as the core deposit intangible.

Other Borrowings

The fair values of other borrowings with fixed maturities are estimated based on discounted cash flow analysis using as discount rates the interest rates charged by the Federal Home Loan Bank for borrowings of similar remaining maturities.

Accrued Interest Payable

The carrying amount of accrued interest payable approximates its fair value since it is short-term in nature.

Commitments to Extend Credit

The fair values of commitments to extend credit are estimated using the fees normally charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present creditworthiness of the counter parties.

Commitments to Sell Loans

The fair values of commitments to sell loans are estimated using the quoted market prices for loans with similar interest rates and terms to maturity.

(6) Other Comprehensive Income (Loss)

Other comprehensive income (loss) is defined as the change in equity during a period from transactions and other events from nonowner sources. Comprehensive income (loss) is the total of net income and other comprehensive income (loss), which for the Company is comprised of unrealized gains and losses on securities available for sale. The components of other comprehensive income (loss) and the related tax effects for the quarter and nine-months ended September 30, 2015 and 2014 were as follows:

<i>(Dollars in thousands)</i>	For the three months ended September 30,					
	2015		2014			
Securities available for sale:	Before Tax	Net	Before Tax	Net	Net	
	tax	of	tax	effect	of	
		tax			tax	
Net unrealized gains (losses) arising during the period	\$458	183	275	(234)	(164)	(70)
Other comprehensive income (loss)	\$458	183	275	(234)	(164)	(70)

<i>(Dollars in thousands)</i>	For the nine months ended September 30,	
	2015	2014

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Securities available for sale:	Before Tax tax	Net of tax	Before Tax tax	Net of tax	Before Tax tax	Net of tax
Net unrealized gains arising during the period	\$798	317	481	317	15	302
Other comprehensive income	\$798	317	481	317	15	302

(7) Securities Available For Sale

The following table shows the gross unrealized losses and fair value for the securities available for sale portfolio, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at September 30, 2015 and December 31, 2014.

	September 30, 2015			Twelve months or more			Total	
	# of Investments	Fair Value	Unrealized Losses	# of Investments	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
<i>(Dollars in thousands)</i>								
Mortgage backed securities:								
Federal National Mortgage Association (FNMA)	6	\$51	(1)	0	\$0	0	51	(1)
Collateralized mortgage obligations:								
FNMA	2	522	(2)	0	0	0	522	(2)
Other marketable securities:								
U.S. Government agency obligations	1	5,005	(2)	0	0	0	5,005	(2)
Municipal obligations	14	2,168	(6)	0	0	0	2,168	(6)
Corporate debt	1	337	(4)	0	0	0	337	(4)
Corporate preferred stock	0	0	0	1	350	(350)	350	(350)
Corporate equity	1	52	(6)	0	0	0	52	(6)
Total temporarily impaired securities	25	\$8,135	(21)	1	\$350	(350)	\$8,485	(371)

	December 31, 2014			Twelve months or more			Total	
	# of Investments	Fair Value	Unrealized Losses	# of Investments	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
<i>(Dollars in thousands)</i>								
Other marketable securities:								
U.S. Government agency obligations	22	\$104,453	(551)	1	\$4,970	(50)	\$109,423	(601)
Corporate preferred stock	0	0	0	1	420	(280)	420	(280)
Total temporarily impaired securities	22	\$104,453	(551)	2	\$5,390	(330)	\$109,843	(881)

We review our investment portfolio on a quarterly basis 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 market liquidity for the investment, 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 recover the temporary loss.

The unrealized losses reported for corporate preferred stock over twelve months at September 30, 2015 related to a single trust preferred security that was issued by the holding company of a small community bank. Typical of most trust preferred issuances, the issuer has the ability to defer interest payments for up to five years with interest payable on the deferred balance. In September 2014, the issuer paid all previously deferred interest that was due and all payments were current as of September 30, 2014. In January 2015, the issuer began to defer its scheduled interest payments as allowed by the terms of the security agreement. The issuer's subsidiary bank has incurred operating losses due to increased provisions for loan losses but still met the regulatory requirements to be considered "well capitalized" based on its most recent regulatory filing. Based on a review of the issuer, it was determined that the trust preferred security was not other-than-temporarily impaired at September 30, 2015. The Company does not intend to sell the trust preferred security and has the intent and ability to hold it for a period of time sufficient to recover the temporary loss. Management believes that the Company will receive all principal and interest payments contractually due on the security and that the decrease in the market value is primarily due to a lack of liquidity in the market for trust preferred securities and the deferral of interest by the issuer. Management will continue to monitor the credit risk of the issuer and may be required to recognize other-than-temporary impairment charges on this security in future periods.

A summary of securities available for sale at September 30, 2015 and December 31, 2014 is as follows:

<i>(Dollars in thousands)</i>	Amortized cost	Gross unrealized gains	Gross unrealized losses	Fair value
<u>September 30, 2015:</u>				
Mortgage-backed securities:				
Federal Home Loan Mortgage Corporation (FHLMC)	\$ 1,382	45	0	1,427
FNMA	2,598	41	(1) 2,638
Government National Mortgage Association (GNMA)	40	0	0	40
Collateralized mortgage obligations:				
FHLMC	1,285	9	0	1,294
FNMA	1,625	9	(2) 1,632
GNMA	49	0	0	49
	6,979	104	(3) 7,080
Other marketable securities:				

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U.S. Government agency obligations	133,151	355	(2)	133,504
Municipal obligations	4,004	17	(6)	4,015
Corporate debt	341	0	(4)	337
Corporate preferred stock	700	0	(350)	350
Corporate equity	58	0	(6)	52
	138,254	372	(368)	138,258
	\$ 145,233	476	(371)	145,338

<i>(Dollars in thousands)</i>	Amortized cost	Gross unrealized gains	Gross unrealized losses	Fair value
<u>December 31, 2014:</u>				
Mortgage-backed securities:				
FHLMC	\$ 1,418	90	0	1,508
FNMA	1,337	64	0	1,401
	2,755	154	0	2,909
Other marketable securities:				
U.S. Government agency obligations	135,014	31	(601)	134,444
Corporate preferred stock	700	0	(280)	420
Corporate equity	58	3	0	61
	135,772	34	(881)	134,925
	\$ 138,527	188	(881)	137,834

The following table indicates amortized cost and estimated fair value of securities available for sale at September 30, 2015 based upon contractual maturity adjusted for scheduled repayments of principal and projected prepayments of principal based upon current economic conditions and interest rates.

<i>(Dollars in thousands)</i>	Amortized Cost	Fair Value
Due less than one year	\$ 8,180	8,228
Due after one year through five years	132,979	133,376
Due after five years through ten years	3,038	3,051
Due after ten years	978	631
No stated maturity	58	52
Total	\$ 145,233	145,338

The allocation of mortgage-backed securities in the table above is based upon the anticipated future cash flow of the securities using estimated mortgage prepayment speeds. The allocation of other marketable securities that have call features is based on the anticipated cash flows to the call date if it is anticipated that the security will be called, or to the maturity date if it is not anticipated to be called.

(8) Loans Receivable, Net

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A summary of loans receivable at September 30, 2015 and December 31, 2014 is as follows:

<i>(Dollars in thousands)</i>	September 30, 2015	December 31, 2014
1-4 family	\$ 82,227	69,841
Commercial real estate:		
Residential developments	29,074	19,960
Other	207,045	171,708
Consumer	236,119	191,668
	62,855	54,925
Commercial business:		
Construction industry	7,210	7,121
Other	52,616	50,001
	59,826	57,122
Total loans	441,027	373,556
Less:		
Unamortized discounts	14	14
Net deferred loan costs	53	97
Allowance for loan losses	8,786	8,332
Total loans receivable, net	\$ 432,174	365,113

(9) Allowance for Loan Losses and Credit Quality Information

The allowance for loan losses for the three and nine months ended September 30, 2015 and 2014 is summarized as follows:

<i>(Dollars in thousands)</i>	1-4 Family	Commercial Real Estate	Consumer	Commercial Business	Total
<u>For the three months ended September 30, 2015:</u>					
Balance, June 30, 2015	\$1,011	5,278	1,162	951	8,402
Provision for losses	117	(462)	25	264	(56)
Charge-offs	(19)	0	(39)	(1)	(59)
Recoveries	1	435	7	56	499
Balance, September 30, 2015	\$1,110	5,251	1,155	1,270	8,786
<u>For the nine months ended September 30, 2015:</u>					
Balance, December 31, 2014	\$1,096	5,024	1,009	1,203	8,332
Provision for losses	30	(415)	191	(45)	(239)
Charge-offs	(19)	0	(66)	(6)	(91)
Recoveries	3	642	21	118	784
Balance, September 30, 2015	\$1,110	5,251	1,155	1,270	8,786
Allocated to:					
Specific reserves	\$270	370	307	127	1,074
General reserves	826	4,654	702	1,076	7,258
Balance, December 31, 2014	\$1,096	5,024	1,009	1,203	8,332
Allocated to:					
Specific reserves	\$220	259	353	79	911
General reserves	890	4,992	802	1,191	7,875
Balance, September 30, 2015	\$1,110	5,251	1,155	1,270	8,786
<u>Loans receivable at December 31, 2014:</u>					
Individually reviewed for impairment	\$1,867	9,728	806	555	12,956
Collectively reviewed for impairment	67,974	181,940	54,119	56,567	360,600
Ending balance	\$69,841	191,668	54,925	57,122	373,556
<u>Loans receivable at September 30, 2015:</u>					
Individually reviewed for impairment	\$1,862	7,589	917	402	10,770
Collectively reviewed for impairment	80,365	228,530	61,938	59,424	430,257
Ending balance	\$82,227	236,119	62,855	59,826	441,027

<i>(Dollars in thousands)</i>	1-4 Family	Commercial Real Estate	Consumer	Commercial Business	Total
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For the three months ended September 30, 2014:

Balance, June 30, 2014	\$2,085	3,823	1,164	1,624	8,696
Provision for losses	(489)	14	(16)	(498)	(989)
Charge-offs	0	0	(15)	(55)	(70)
Recoveries	0	229	10	47	286
Balance, September 30, 2014	\$1,596	4,066	1,143	1,118	7,923

For the nine months ended September 30, 2014:

Balance, December 31, 2013	\$1,628	6,458	1,106	2,209	11,401
Provision for losses	60	(3,588)	83	(1,332)	(4,777)
Charge-offs	(92)	(936)	(75)	(56)	(1,159)
Recoveries	0	2,132	29	297	2,458
Balance, September 30, 2014	\$1,596	4,066	1,143	1,118	7,923

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The following table summarizes the amount of classified and unclassified loans at September 30, 2015 and December 31, 2014:

<i>(Dollars in thousands)</i>	September 30, 2015					Unclassified	
	Classified Special Mention	Substandard	Doubtful	Loss	Total	Total	Total Loans
1-4 family	\$191	2,556	55	0	2,802	79,425	82,227
Commercial real estate:							
Residential developments	0	6,842	0	0	6,842	22,232	29,074
Other	3,158	12,744	0	0	15,902	191,143	207,045
Consumer	0	568	89	260	917	61,938	62,855
Commercial business:							
Construction industry	48	185	0	0	233	6,977	7,210
Other	4,653	1,567	14	0	6,234	46,382	52,616
	\$8,050	24,462	158	260	32,930	408,097	441,027

<i>(Dollars in thousands)</i>	December 31, 2014					Unclassified	
	Classified Special Mention	Substandard	Doubtful	Loss	Total	Total	Total Loans
1-4 family	\$0	2,493	207	0	2,700	67,141	69,841
Commercial real estate:							
Residential developments	323	9,960	0	0	10,283	9,677	19,960
Other	7,376	8,792	0	0	16,168	155,540	171,708
Consumer	0	489	55	261	805	54,120	54,925
Commercial business:							
Construction industry	0	439	0	0	439	6,682	7,121
Other	4,255	1,156	0	0	5,411	44,590	50,001
	\$11,954	23,329	262	261	35,806	337,750	373,556

Classified loans represent special mention, substandard (performing and non-performing), and non-performing loans categorized as doubtful and loss. Loans classified as special mention are loans that have potential weaknesses that, if left uncorrected, may result in deterioration of the repayment prospects for the asset or in the Bank's credit position at some future date. Loans classified as substandard are loans that are generally inadequately protected by the current net worth and paying capacity of the obligor, or by the collateral pledged, if any. Loans classified as substandard have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. Substandard loans are characterized by the distinct possibility that the Bank will sustain some loss if the deficiencies are not corrected. Loans classified as doubtful have the weaknesses of those classified as substandard, with additional characteristics that make collection in full on the basis of currently existing facts, conditions and values questionable, and there is a high possibility of loss. A loan classified as loss is considered uncollectible and of such little value that continuance as an asset on the balance sheet is not warranted. Loans classified as substandard or doubtful require the Bank to perform an analysis of the individual loan and charge off any loans, or portion thereof, that are deemed uncollectible.

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The aging of past due loans at September 30, 2015 and December 31, 2014 is summarized as follows:

<i>(Dollars in thousands)</i>	30-59 Days Past Due	60-89 Days Past Due	90 Days or More Past Due	Total Past Due	Current Loans	Total Loans	Loans 90 Days or More Past Due and Still Accruing
<i>September 30, 2015</i>							
1-4 family	\$915	318	714	1,947	80,280	82,227	0
Commercial real estate:							
Residential developments	0	0	0	0	29,074	29,074	0
Other	0	0	0	0	207,045	207,045	0
Consumer	306	290	147	743	62,112	62,855	0
Commercial business:							
Construction industry	0	0	0	0	7,210	7,210	0
Other	263	20	15	298	52,318	52,616	0
	\$1,484	628	876	2,988	438,039	441,027	0
<i>December 31, 2014</i>							
1-4 family	\$413	673	841	1,927	67,914	69,841	0
Commercial real estate:							
Residential developments	0	0	0	0	19,960	19,960	0
Other	0	0	0	0	171,708	171,708	0
Consumer	550	176	131	857	54,068	54,925	0
Commercial business:							
Construction industry	0	0	0	0	7,121	7,121	0
	136	0	0	136	49,865	50,001	0

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Other

\$1,099 849 972 2,920 370,636 373,556 0

Impaired loans include loans that are non-performing (non-accruing) and loans that have been modified in a troubled debt restructuring (TDR). The following table summarizes impaired loans and related allowances as of September 30, 2015 and December 31, 2014:

<i>(Dollars in thousands)</i>	September 30, 2015			December 31, 2014		
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Recorded Investment	Unpaid Principal Balance	Related Allowance
Loans with no related allowance recorded:						
1-4 family	\$995	995	0	755	755	0
Commercial real estate:						
Residential developments	5,215	7,558	0	7,416	10,040	0
Other	500	645	0	48	216	0
Consumer	410	411	0	463	464	0
Commercial business:						
Construction industry	0	102	0	80	198	0
Other	14	14	0	0	0	0
Loans with an allowance recorded:						
1-4 family	867	867	220	1,112	1,112	270
Commercial real estate:						
Residential developments	1,684	1,684	233	1,522	1,522	240
Other	190	190	26	742	743	130
Consumer	507	524	353	343	360	307
Commercial business:						
Construction industry	0	0	0	0	0	0
Other	388	939	79	475	1,026	127
Total:						
1-4 family	1,862	1,862	220	1,867	1,867	270

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Commercial real estate:

Residential developments	6,899	9,242	233	8,938	11,562	240
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Other	690	835	26	790	959	130
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Consumer	917	935	353	806	824	307
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Commercial business:

Construction industry	0	102	0	80	198	0
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Other	402	953	79	475	1,026	127
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	\$10,770	13,929	911	12,956	16,436	1,074
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The following tables summarize average recorded investment and interest income recognized on impaired loans during the three and nine months ended September 30, 2015 and 2014.

<i>(Dollars in thousands)</i>	For the three months ended September 30, 2015		For the nine months ended September 30, 2015	
	Average Recorded Investment	Interest Recognized	Average Recorded Investment	Interest Recognized
Loans with no related allowance recorded:				
1-4 family	\$989	1	866	32
Commercial real estate:				
Residential developments	5,884	97	6,480	287
Other	501	8	388	22
Consumer	363	1	365	5
Commercial business:				
Construction industry	3	0	36	0
Other	20	0	10	1
Loans with an allowance recorded:				
1-4 family	968	3	1,069	10
Commercial real estate:				
Residential developments	1,705	6	1,540	24
Other	192	0	330	0
Consumer	531	2	434	16
Commercial business:				
Construction industry	0	0	0	0
Other	397	4	432	13

Total:

1-4 family	1,957	4	1,935	42
Commercial real estate:				
Residential developments	7,589	103	8,020	311
Other	693	8	718	22
Consumer	894	3	799	21
Commercial business:				
Construction industry	3	0	36	0
Other	417	4	442	14
	\$11,553	122	11,950	410

<i>(Dollars in thousands)</i>	For the three months ended September 30, 2014		For the nine months ended September 30, 2014	
	Average Recorded Investment	Interest Recognized	Average Recorded Investment	Interest Recognized
Loans with no related allowance recorded:				
1-4 family	\$234	3	352	6
Commercial real estate:				
Residential developments	7,691	102	7,688	112
Other	51	5	51	5
Consumer	456	8	468	10
Commercial business:				
Construction industry	86	0	89	0
Other	0	0	0	0
Loans with an allowance recorded:				
1-4 family	1,606	6	1,651	13
Commercial real estate:				
Residential developments	1,153	0	3,521	0
Other	866	9	874	24
Consumer	489	3	479	9
Commercial business:				
Construction industry	0	0	0	0
Other	981	8	990	23
Total:				
1-4 family	1,840	9	2,003	19

Commercial real estate:

Residential developments	8,844	102	11,209	112
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Other	917	14	925	29
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Consumer	945	11	947	19
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Commercial business:

Construction industry	86	0	89	0
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Other	981	8	990	23
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	\$13,613	144	16,163	202
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At September 30, 2015 and December 31, 2014, non-accruing loans totaled \$9.1 million and \$10.9 million, respectively, for which the related allowance for loan losses was \$0.6 million and \$0.8 million, respectively. All of the interest income that was recognized for non-accruing loans was recognized using the cash basis method of income recognition. Non-accruing loans for which no specific allowance has been recorded, because management determined that the value of the collateral was sufficient to repay the loan, totaled \$6.7 million and \$8.0 million at September 30, 2015 and December 31, 2014, respectively. Non-accrual loans also include certain loans that have had terms modified in a TDR.

The non-accrual loans at September 30, 2015 and December 31, 2014 are summarized as follows:

<i>(Dollars in thousands)</i>	September	December
	30, 2015	31, 2014