

Ottawa Savings Bancorp, Inc.
Form 10-Q
November 14, 2013
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 000-51367

OTTAWA SAVINGS BANCORP, INC.

(Exact name of registrant as specified in its charter)

Edgar Filing: Ottawa Savings Bancorp, Inc. - Form 10-Q

United States

(State or other jurisdiction of incorporation or organization)

20-3074627

(I.R.S. Employer Identification Number)

925 LaSalle Street

Ottawa, Illinois

(Address of principal executive offices)

61350

(Zip Code)

(815) 433-2525

(Registrant's telephone number, including area code)

Not Applicable

(Former name, former address and former fiscal year,

if changed since last report)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or 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. (Check one):

Large Accelerated Filer
Filer

Accelerated

Non-Accelerated Filer (Do not check if a smaller reporting company)
Reporting Company

Smaller

Edgar Filing: Ottawa Savings Bancorp, Inc. - Form 10-Q

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 as of November 13, 2013
Common Stock, \$0.01 par value	2,117,979

OTTAWA SAVINGS BANCORP, INC.

FORM 10-Q

For the quarterly period ended September 30, 2013

INDEX

	Page
	<u>Number</u>
PART I – FINANCIAL INFORMATION	
Item 1	3
Item 2	23
Item 3	33
Item 4	33
PART II – OTHER INFORMATION	
Item 1	33
Item 1A	34
Item 2	34
Item 3	34
Item 4	34
Item 5	34
Item 6	34
SIGNATURES	35

Part I – Financial Information

ITEM 1 – FINANCIAL STATEMENTS

OTTAWA SAVINGS BANCORP, INC.**Consolidated Balance Sheets****September 30, 2013 and December 31, 2012**

(Unaudited)

	September 30, 2013	December 31, 2012
Assets		
Cash and due from banks	\$1,810,203	\$1,439,637
Interest bearing deposits	3,398,756	9,348,352
Total cash and cash equivalents	5,208,959	10,787,989
Federal funds sold	2,885,000	1,666,000
Securities held to maturity (fair value of \$13 at December 31, 2012)	-	12
Securities available for sale	34,952,460	28,863,603
Non-marketable equity securities	1,233,536	1,334,436
Loans, net of allowance for loan losses of \$3,214,275 and \$3,381,441 at September 30, 2013 and December 31, 2012, respectively	113,133,554	121,994,851
Loans held for sale	-	171,095
Premises and equipment, net	6,498,148	6,629,794
Accrued interest receivable	670,709	696,638
Foreclosed real estate	907,320	1,297,214
Deferred tax assets	2,463,044	2,243,663
Cash value of life insurance	2,097,322	1,587,436
Prepaid FDIC premiums	-	163,999
Income tax refunds receivable	-	166,590
Other assets	1,806,574	1,442,841
Total assets	\$171,856,626	\$179,046,161
Liabilities and Stockholders' Equity		
Liabilities		
Deposits:		
Non-interest bearing	\$5,015,782	\$4,313,635
Interest bearing	142,644,024	150,761,010
Total deposits	147,659,806	155,074,645
Accrued interest payable	2,780	806
Other liabilities	2,728,591	2,686,620
Total liabilities	150,391,177	157,762,071

Edgar Filing: Ottawa Savings Bancorp, Inc. - Form 10-Q

Commitments and contingencies		
Redeemable common stock held by ESOP plan	290,144	237,712
Stockholders' Equity		
Common stock, \$.01 par value, 12,000,000 shares authorized; 2,224,911 shares issued	22,249	22,249
Additional paid-in-capital	8,704,577	8,705,547
Retained earnings	14,325,324	13,689,967
Unallocated ESOP shares	(317,975)	(356,132)
Unearned management recognition plan shares	(24,359)	(33,977)
Accumulated other comprehensive (loss) income	(32,249)	468,554
	22,677,567	22,496,208
Less:		
Treasury stock, at cost; 106,932 shares	(1,212,118)	(1,212,118)
Maximum cash obligation related to ESOP shares	(290,144)	(237,712)
Total stockholders' equity	21,175,305	21,046,378
Total liabilities and stockholders' equity	\$171,856,626	\$179,046,161

See accompanying notes to these unaudited consolidated financial statements.

OTTAWA SAVINGS BANCORP, INC.**Consolidated Statements of Operations****Three and Nine Months Ended September 30, 2013 and 2012**

(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Interest and dividend income:				
Interest and fees on loans	\$1,494,762	\$1,707,929	\$4,760,905	\$5,290,545
Securities:				
Residential mortgage-backed and related securities	114,339	146,188	334,534	498,755
U.S. agency securities	-	4,875	-	38,297
State and municipal securities	69,255	59,010	196,725	151,082
Dividends on non-marketable equity securities	831	1,233	2,544	3,094
Interest-bearing deposits	1,233	508	4,302	3,081
Total interest and dividend income	1,680,420	1,919,743	5,299,010	5,984,854
Interest expense:				
Deposits	343,977	530,132	1,152,505	1,669,763
Borrowings	-	-	-	1
Total interest expense	343,977	530,132	1,152,505	1,669,764
Net interest income	1,336,443	1,389,611	4,146,505	4,315,090
Provision for loan losses	225,000	330,000	775,000	1,332,000
Net interest income after provision for loan losses	1,111,443	1,059,611	3,371,505	2,983,090
Other income:				
Gain on sale of securities	-	-	-	13,948
Gain on sale of loans	18,216	18,674	64,961	77,046
Gain on sale of OREO	-	27,014	-	96,736
Origination of mortgage servicing rights, net of amortization	3,005	(5,791)	7,659	(3,040)
Customer service fees	80,645	73,125	224,059	212,421
(Loss) income on bank owned life insurance	(2,441)	7,827	9,886	23,230
Other	16,039	21,979	174,596	51,815
Total other income	115,464	142,828	481,161	472,156
Other expenses:				
Salaries and employee benefits	388,535	399,340	1,144,192	1,102,630
Directors fees	25,200	21,000	75,600	63,000
Occupancy	115,589	111,193	336,002	328,260
Deposit insurance premium	56,999	61,283	171,663	181,722
Legal and professional services	80,435	53,333	222,803	165,062
Data processing	68,497	81,143	218,968	242,407
Valuation adjustments and expenses on foreclosed real estate	71,956	60,913	246,988	106,957
Loss on sale of OREO	18,327	-	4,177	-
Loss on sale of repossessed assets	-	-	385	14,472

Edgar Filing: Ottawa Savings Bancorp, Inc. - Form 10-Q

Loss on consumer loans	-	-	-	41,514
Other	130,977	120,728	429,348	378,131
Total other expenses	956,515	908,933	2,850,126	2,624,155
Income before income tax expense	270,392	293,506	1,002,540	831,091
Income tax expense	101,557	114,836	367,183	257,543
Net income	\$168,835	\$178,670	\$635,357	\$573,548
Basic earnings per share	\$0.08	\$0.09	\$0.31	\$0.28
Diluted earnings per share	\$0.08	\$0.09	\$0.31	\$0.27

See accompanying notes to these unaudited consolidated financial statements.

OTTAWA SAVINGS BANCORP, INC.**Consolidated Statements of Comprehensive Income****Three and Nine Months Ended September 30, 2013 and 2012**

(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Net income	\$168,835	\$178,670	\$635,357	\$573,548
Other comprehensive (loss) income, before tax:				
Securities available for sale:				
Unrealized holding (losses) gains arising during the period	(90,135)	196,624	(758,794)	194,189
Reclassification adjustment for (gains) included in net income	-	-	-	(13,948)
Other comprehensive (loss) income, before tax	(90,135)	196,624	(758,794)	180,241
Income tax (benefit) expense related to items of other comprehensive (loss) income	(30,647)	66,852	(257,991)	61,282
Other comprehensive (loss) income, net of tax	(59,488)	129,772	(500,803)	118,959
Comprehensive income	\$109,347	\$308,442	\$134,554	\$692,507

See accompanying notes to these unaudited consolidated financial statements.

OTTAWA SAVINGS BANCORP, INC.**Consolidated Statements of Cash Flows****Nine Months Ended September 30, 2013 and 2012**

(Unaudited)

	2013	2012
Cash Flows from Operating Activities		
Net income	\$635,357	\$573,548
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	140,218	150,575
Provision for loan losses	775,000	1,332,000
Provision for deferred income taxes	38,608	244,225
Net amortization of premiums and discounts on securities	459,644	373,010
Gain on sale of securities	-	(13,948)
Origination of mortgage loans held for sale	(5,042,468)	(6,137,409)
Proceeds from sale of mortgage loans held for sale	5,278,524	5,818,255
Gain on sale of loans, net	(64,961)	(77,046)
Origination of mortgage servicing rights, net of amortization	(7,659)	3,040
Proceeds from sale of non-mortgage loans held for sale	268,634	-
Loss (gain) on sale of foreclosed real estate	4,177	(96,736)
Write down of foreclosed real estate	109,284	13,000
Loss on sale of repossessed assets	385	14,472
Loss on consumer loans	-	41,514
ESOP compensation expense	26,458	20,787
MRP compensation expense	9,617	3,806
Compensation expense on RRP options granted	10,730	7,211
Increase in cash surrender value of life insurance	(9,886)	(23,230)
Change in assets and liabilities:		
Decrease in prepaid FDIC insurance premiums	163,999	173,648
Decrease in accrued interest receivable	25,929	25,930
Increase in other assets	(316,316)	(132,230)
Decrease in income tax refunds receivable	166,590	738,658
Increase (decrease) in accrued interest payable and other liabilities	43,944	(29,427)
Net cash provided by operating activities	2,715,808	3,023,653
Cash Flows from Investing Activities		
Securities available for sale:		
Purchases	(12,808,383)	(8,369,727)
Sales, maturities and paydowns	5,501,090	10,574,675
Securities held to maturity:		
Sales, maturities and paydowns	12	2
Purchase of bank-owned life insurance	(500,000)	-
Net decrease (increase) in loans	7,220,501	(1,432,228)
Net (increase) decrease in federal funds sold	(1,219,000)	60,000

Edgar Filing: Ottawa Savings Bancorp, Inc. - Form 10-Q

Proceeds from sale of foreclosed real estate	829,095	716,691
Proceeds from sale of repossessed assets	4,357	26,616
Purchase of premises and equipment	(8,572)	(23,236)
Sale of non-marketable equity securities	100,900	1,200,516
Net cash (used in) provided by investing activities	(880,000)	2,753,309
Cash Flows from Financing Activities		
Net decrease in deposits	(7,414,838)	(1,410,414)
Net cash used in financing activities	(7,414,838)	(1,410,414)
Net (decrease) increase in cash and cash equivalents	(5,579,030)	4,366,548
Cash and cash equivalents:		
Beginning	10,787,989	2,945,465
Ending	\$5,208,959	\$7,312,013

(Continued)

See accompanying notes to these unaudited consolidated financial statements.

OTTAWA SAVINGS BANCORP, INC.**Consolidated Statements of Cash Flows****Nine Months Ended September 30, 2013 and 2012**

(Unaudited)

	2013	2012
Supplemental Disclosures of Cash Flow Information		
Cash payments for:		
Interest paid to depositors	\$1,150,531	\$1,663,581
Interest paid on borrowings	-	1
Income taxes paid, net of (refunds) received	295,217	(794,787)
Supplemental Schedule of Noncash Investing and Financing Activities		
Real estate acquired through or in lieu of foreclosure	552,662	1,592,746
Other assets acquired in settlement of loans	44,500	20,600
Sale of foreclosed real estate through loan origination	-	397,736
Transfer of non-mortgage loans to held for sale	268,634	-
Deferred gains on the sale of OREO properties	-	17,618
Increase in ESOP put option liability	52,432	72,666

See accompanying notes to these unaudited consolidated financial statements.

OTTAWA SAVINGS BANCORP, INC.

Notes to Unaudited Consolidated Financial Statements

(continued)

NOTE 1 – NATURE OF BUSINESS

Ottawa Savings Bancorp, Inc. (the “Company”) was incorporated under the laws of the United States on July 11, 2005, for the purpose of serving as the holding company of Ottawa Savings Bank (the “Bank”), as part of the Bank’s conversion from a mutual to a stock form of organization. The Company is a publicly traded banking company with assets of \$171.9 million at September 30, 2013 and is headquartered in Ottawa, Illinois.

In 2005, the Board of Directors of the Bank unanimously adopted a plan of conversion providing for the conversion of the Bank from an Illinois chartered mutual savings bank to a federally chartered stock savings bank and the purchase of all of the common stock of the Bank by the Company. The depositors of the Bank approved the plan at a meeting held in 2005.

In adopting the plan, the Board of Directors of the Bank determined that the conversion was advisable and in the best interests of its depositors and the Bank. The conversion was completed in 2005 when the Company issued 1,223,701 shares of common stock to Ottawa Savings Bancorp MHC (a mutual holding company), and 1,001,210 shares of common stock to the public. As of September 30, 2013, Ottawa Savings Bancorp MHC holds 1,223,701 shares of common stock, representing 57.8% of the Company’s common shares outstanding.

The Bank’s business is to attract deposits from the general public and use those funds to originate and purchase one-to-four family, multi-family and non-residential real estate, construction, commercial and consumer loans, which the Bank primarily holds for investment. The Bank has continually diversified its products to meet the needs of the community.

NOTE 2 – BASIS OF PRESENTATION

The consolidated financial statements presented in this quarterly report include the accounts of the Company and the Bank. The consolidated financial statements of the Company have been prepared in accordance with U.S. generally accepted accounting principles (“GAAP”) for interim financial information and predominant practices followed by the

financial services industry, and are unaudited. In the opinion of the Company's management, all adjustments, consisting of normal recurring adjustments, which the Company considers necessary to fairly state the Company's financial position and the results of operations and cash flows have been recorded. The interim financial statements should be read in conjunction with the audited financial statements and accompanying notes of the Company for the year ended December 31, 2012. Certain amounts in the accompanying financial statements and footnotes for 2012 have been reclassified with no effect on net income or stockholders' equity to be consistent with the 2013 classifications. The results of the Company's operations for any interim period are not necessarily indicative of the results of the Company's operations for any other interim period or for a full fiscal year.

NOTE 3 – USE OF ESTIMATES

The preparation of the financial statements in conformity with GAAP requires management to make estimates and assumptions that affect amounts reported in the consolidated financial statements. Changes in these estimates and assumptions are considered reasonably possible and may have a material impact on the consolidated financial statements and, thus, actual results could differ from the amounts reported and disclosed herein.

At September 30, 2013, there were no material changes in the Company's significant accounting policies from those disclosed in the Form 10-K filed with the Securities and Exchange Commission on March 28, 2013. Reference should be made to Note 4 below for explanation of a change the Company made to the calculation it uses to determine historical loss rates that are used in the allowance for loan losses calculation.

NOTE 4 – CRITICAL ACCOUNTING POLICIES

We consider accounting policies involving significant judgments and assumptions by management that have, or could have, a material impact on the carrying value of certain assets or on income to be critical accounting policies. We consider the allowance for loan losses and deferred income taxes to be our critical accounting policies.

OTTAWA SAVINGS BANCORP, INC.

Notes to Unaudited Consolidated Financial Statements

(continued)

Allowance for Loan Losses. The allowance for loan losses is an amount necessary to absorb known or inherent losses that are both probable and reasonably estimable and is established through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance. The allowance for loan losses is evaluated on a regular basis by management and is based upon management's periodic review of the collectability of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect each borrower's ability to repay, estimated value of any underlying collateral and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

Due to changing economic conditions which resulted in reduced charge-offs through June 30, 2013, management evaluated and changed the historical loss period used in the allowance for loan losses calculation during the quarter ended June 30, 2013. Through March 31, 2013, management used the most recent eight quarters of loss history to calculate historical loss rates. The weighting applied to the quarters was graduated, with heavier weightings applied to the most recent quarters of loss history. Beginning with the quarter ended June 30, 2013, management expanded the loss period and began using the most recent twelve quarters of loss history to calculate historical loss rates. The weighting applied to the quarters is still graduated, with heavier weightings applied to the most recent quarters of loss history; however, the weighting applied has a lesser graduation than the previous methodology. The new weighting applies 40% to each of the most recent four quarters and 30% to each of the next eight quarters. Management evaluated the impact of the change in methodology by calculating the allowance for loan losses using both the old methodology and the new methodology at June 30, 2013, and determined that the change in methodology did not have a material impact on the allowance for loan losses as of June 30, 2013.

A loan is considered impaired when, based on current information and events, it is probable that we will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan by loan basis using either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price, or the fair value of the collateral if the loan is collateral dependent.

Deferred Income Taxes. Deferred income tax assets and liabilities are computed for differences between the financial statement and tax basis of assets and liabilities that will result in taxable or deductible amounts in the future based on enacted tax laws and rates applicable to the periods in which the differences are expected to affect taxable income. Deferred tax assets are also recognized for operating loss and tax credit carry-forwards. Accounting guidance requires that companies assess whether a valuation allowance should be established against their deferred tax assets based on the consideration of all available evidence using a “more likely than not” standard.

Per accounting guidance, the Company reviewed its deferred tax assets at September 30, 2013 and determined that no valuation allowance was necessary. Despite a continued challenging economic environment, the Company has a history of strong earnings, is well-capitalized, and has positive expectations regarding future taxable income.

The deferred tax asset will be analyzed quarterly to determine if a valuation allowance is warranted. There can be no guarantee that a valuation allowance will not be necessary in future periods. In making such judgments, significant weight is given to evidence that can be objectively verified. In making decisions regarding any valuation allowance, the Company considers both positive and negative evidence and analyzes changes in near-term market conditions as well as other factors which may impact future operating results.

OTTAWA SAVINGS BANCORP, INC.**Notes to Unaudited Consolidated Financial Statements****(continued)****NOTE 5 – EARNINGS PER SHARE**

Basic earnings per share is based on net income divided by the weighted average number of shares outstanding during the period, including allocated and committed-to-be-released Employee Stock Ownership Plan (“ESOP”) shares and vested Management Recognition Plan (“MRP”) shares. Diluted earnings per share show the dilutive effect, if any, of additional common shares issuable under stock options and awards.

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2013	2012	2013	2012
Net income available to common stockholders	\$168,835	\$178,670	\$635,357	\$573,548
Basic potential common shares:				
Weighted average shares outstanding	2,117,979	2,117,979	2,117,979	2,117,979
Weighted average unallocated ESOP shares	(32,636)	(37,724)	(33,895)	(38,988)
Weighted average unvested MRP shares	(6,719)	(8,899)	(6,719)	(8,899)
Basic weighted average shares outstanding	2,078,624	2,071,356	2,077,365	2,070,092
Dilutive potential common shares:				
Weighted average unrecognized compensation on MRP shares	5,028	5,738	5,009	18,753
Weighted average RRP options outstanding *	-	-	-	-
Dilutive weighted average shares outstanding	2,083,652	2,077,094	2,082,374	2,088,845
Basic earnings per share	\$0.08	\$0.09	\$0.31	\$0.28
Diluted earnings per share	\$0.08	\$0.09	\$0.31	\$0.27

* The effect of share options was not included in the calculation of diluted earnings per share because to do so would have been anti-dilutive.

NOTE 6 – EMPLOYEE STOCK OWNERSHIP PLAN

On July 11, 2005, the Company adopted an ESOP for the benefit of substantially all employees. Upon adoption of the ESOP, the ESOP borrowed \$763,140 from the Company and used those funds to acquire 76,314 shares of the Company's stock in the initial public offering at a price of \$10.00 per share.

Shares purchased by the ESOP with the loan proceeds are held in a suspense account and are allocated to ESOP participants on a pro rata basis as principal and interest payments are made by the ESOP to the Company. The loan is secured by shares purchased with the loan proceeds and will be repaid by the ESOP with funds from the Company's discretionary contributions to the ESOP and earnings on the ESOP assets. Annual principal and interest payments of approximately \$77,000 are to be made by the ESOP.

As shares are released from collateral, the Company will report compensation expense equal to the current market price of the shares, and the shares will become outstanding for earnings-per-share ("EPS") computations. Dividends on allocated ESOP shares reduce retained earnings, and dividends on unallocated ESOP shares reduce accrued interest.

A terminated participant or the beneficiary of a deceased participant who received a distribution of employer stock from the ESOP has the right to require the Company to purchase such shares at their fair market value any time within 60 days of the distribution date. If this right is not exercised, an additional 60 day exercise period is available in the year following the year in which the distribution is made and begins after a new valuation of the stock has been determined and communicated to the participant or beneficiary. At September 30, 2013, 36,268 shares at a fair value of \$8.00 have been classified as mezzanine capital.

The following table reflects the status of the shares held by the ESOP:

	September 30,	December 31,
	2013	2012
Shares allocated	44,517	40,701
Shares withdrawn from the plan	(8,249)	(6,250)
Unallocated shares	31,797	35,613
Total ESOP shares	68,065	70,064
Fair value of unallocated shares	\$ 254,376	\$ 245,730

OTTAWA SAVINGS BANCORP, INC.**Notes to Unaudited Consolidated Financial Statements****(continued)****NOTE 7 – INVESTMENT SECURITIES**

The amortized cost and fair values of securities, with gross unrealized gains and losses, follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
September 30, 2013:				
Available for Sale				
State and municipal securities	\$8,687,665	\$ 92,745	\$ 319,641	\$8,460,769
Residential mortgage-backed securities	26,313,658	358,672	180,639	26,491,691
	\$35,001,323	\$ 451,417	\$ 500,280	\$34,952,460
December 31, 2012:				
Held to Maturity				
Residential mortgage-backed securities	\$ 12	\$ 1	\$ -	\$ 13
Available for Sale				
State and municipal securities	6,789,496	343,292	12,266	7,120,522
Residential mortgage-backed securities	21,364,176	478,917	100,012	21,743,081
	\$28,153,672	\$ 822,209	\$ 112,278	\$28,863,603

The amortized cost and fair value at September 30, 2013, by contractual maturity, are shown below. Maturities may differ from contractual maturities in residential mortgage-backed securities because the mortgages underlying the securities may be called or prepaid without penalties. Therefore, stated maturities of residential mortgage-backed securities are not disclosed.

	Securities Available for Sale	
	Amortized Cost	Fair Value
Due after three months through one year	\$-	\$-
Due after one year through five years	-	-

Edgar Filing: Ottawa Savings Bancorp, Inc. - Form 10-Q

Due after five years through ten years	3,336,855	3,309,690
Due after ten years	5,350,810	5,151,079
Residential mortgage-backed securities	26,313,658	26,491,691
	\$35,001,323	\$34,952,460

The following table reflects securities with gross unrealized losses for less than 12 months and for 12 months or more at September 30, 2013 and December 31, 2012:

	Less than 12 Months		12 Months or More		Total	
	Fair	Unrealized	Fair	Unrealized	Fair	Unrealized
	Value	Losses	Value	Losses	Value	Losses
September 30, 2013						
Securities Available for Sale						
State and municipal securities	\$4,883,362	\$ 319,641	\$-	\$ -	\$4,883,362	\$ 319,641
Residential mortgage-backed securities	9,716,208	149,394	1,746,935	31,245	11,463,143	180,639
	\$14,599,570	\$ 469,035	\$1,746,935	\$ 31,245	\$16,346,505	\$ 500,280
December 31, 2012						
Securities Available for Sale						
State and municipal securities	\$1,160,173	\$ 12,266	\$-	\$ -	\$1,160,173	\$ 12,266
Residential mortgage-backed securities	4,318,926	73,606	2,587,548	26,406	6,906,474	100,012
	\$5,479,099	\$ 85,872	\$2,587,548	\$ 26,406	\$8,066,647	\$ 112,278

OTTAWA SAVINGS BANCORP, INC.

Notes to Unaudited Consolidated Financial Statements

(continued)

Management evaluates securities for other-than-temporary impairment at least on a quarterly basis, and more frequently when economic or market concerns warrant such evaluation. Consideration is given to (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, and (3) the intent and ability to retain and whether it is not more likely than not the Company will be required to sell its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value. In analyzing an issuer's financial condition, management considers whether the securities are issued by the federal government or its agencies, whether downgrades by bond rating agencies have occurred, and industry analysts' reports.

At September 30, 2013, 26 securities had unrealized losses with an aggregate depreciation of 2.97% from the Company's amortized cost basis. The Company does not consider these investments to be other than temporarily impaired at September 30, 2013 due to the following:

Decline in value is attributable to
interest rates.

The value did not decline due to credit quality.

The Company does not intend to sell these securities.

The Company has adequate liquidity such that it will not more likely than not have to sell these securities before recovery of the amortized cost basis, which may be at maturity.

There were no proceeds from the sales of securities for the three months ended September 30, 2013 and 2012, resulting in no realized gains or losses for the three months ended September 30, 2013 and 2012.

There were no proceeds from the sales of securities for the nine months ended September 30, 2013 and proceeds of \$3.0 million for the nine months ended September 30, 2012. There were no realized gains for the nine months ended September 30, 2013 and gross realized gains of \$58,614 for the nine months ended September 30, 2012. There were no realized losses for the nine months ended September 30, 2013 and gross realized losses of \$44,666 for the nine months ended September 30, 2012. The tax provision applicable to these net realized gains amounted to none and \$4,742, respectively.

NOTE 8 – LOANS AND ALLOWANCE FOR CREDIT LOSSES

The components of loans, net of deferred loan costs (fees), are as follows:

	September 30,	December 31,
	2013	2012
Mortgage loans:		
One-to-four family residential loans	\$78,606,568	\$83,018,756
Multi-family residential loans	2,794,137	4,849,766
Total mortgage loans	81,400,705	87,868,522
Other loans:		
Non-residential real estate loans	18,542,330	20,506,860
Commercial loans	6,797,594	8,648,191
Consumer direct	513,581	542,652
Purchased auto	9,093,619	7,810,067
Total other loans	34,947,124	37,507,770
Gross loans	116,347,829	125,376,292
Less: Allowance for loan losses	(3,214,275)	(3,381,441)
Loans, net	\$113,133,554	\$121,994,851

Purchases of loans receivable, segregated by class of loans, for the periods indicated were as follows:

	Three Months Ended		Nine Months Ended	
	September 30,	September 30,	September 30,	September 30,
	2013	2012	2013	2012
Purchased auto	\$510,729	\$504,550	\$3,536,965	\$5,351,138

OTTAWA SAVINGS BANCORP, INC.**Notes to Unaudited Consolidated Financial Statements****(continued)**

Net (charge-offs) / recoveries, segregated by class of loans, for the periods indicated were as follows:

	Three Months Ended		Nine Months Ended	
	September 30, 2013	2012	September 30, 2013	2012
One-to-four family	\$(523,236)	\$(763,244)	\$(705,543)	\$(2,000,218)
Multi-family	(286,906)	-	(286,906)	(133,429)
Non-residential	(54,591)	(183,257)	52,596	(271,021)
Commercial	-	-	-	(7,259)
Consumer direct	(647)	(379)	(647)	(350)
Purchased auto	4,433	(8,656)	(1,666)	(8,546)
Net (charge-offs)/recoveries	\$(860,947)	\$(955,536)	\$(942,166)	\$(2,420,823)

OTTAWA SAVINGS BANCORP, INC.**Notes to Unaudited Consolidated Financial Statements****(continued)**

The following table presents the activity in the allowance for loan losses by portfolio segment for the three months ended September 30, 2013 and 2012:

September 30, 2013	One-to-Four Family	Multi-family	Non-residential	Commercial	Consumer Direct	Purchased Auto	Total
Balance at beginning of period	\$ 2,908,642	\$ 55,991	\$ 713,094	\$ 83,560	\$ 3,674	\$ 85,261	\$ 3,850,222
Provision charged to income	(30,762)	377,410	(60,564)	(52,086)	(1,294)	(7,704)	225,000
Loans charged off	(528,313)	(286,906)	(54,680)	-	(647)	-	(870,546)
Recoveries of loans previously charged off	5,077	-	89	-	-	4,433	9,599
Balance at end of period	\$ 2,354,644	\$ 146,495	\$ 597,939	\$ 31,474	\$ 1,733	\$ 81,990	\$ 3,214,275

September 30, 2012	One-to-Four Family	Multi-family	Non-residential	Commercial	Consumer Direct	Purchased Auto	Total
Balance at beginning of period	\$ 2,753,034	\$ 201,375	\$ 1,226,121	\$ 45,355	\$ 7,746	\$ 50,494	\$ 4,284,125
Provision charged to income	483,059	(9,062)	(175,009)	(11,797)	(5,588)	48,397	330,000
Loans charged off	(763,244)	-	(183,257)	-	(531)	(11,042)	(958,074)
Recoveries of loans previously charged off	-	-	-	-	152	2,386	2,538
Balance at end of period	\$ 2,472,849	\$ 192,313	\$ 867,855	\$ 33,558	\$ 1,779	\$ 90,235	\$ 3,658,589

The following table presents the activity in the allowance for loan losses by portfolio segment for the nine months ended September 30, 2013 and 2012:

September 30, 2013	One-to-Four Family	Multi-family	Non-residential	Commercial	Consumer Direct	Purchased Auto	Total
Balance at beginning of year	\$ 2,057,336	\$ 161,901	\$ 1,012,119	\$ 75,130	\$ 1,465	\$ 73,490	\$ 3,381,441
Provision charged to income	1,002,851	271,500	(466,776)	(43,656)	915	10,166	775,000
Loans charged off	(715,620)	(286,906)	(83,587)	-	(647)	(9,596)	(1,096,356)
Recoveries of loans previously charged off	10,077	-	136,183	-	-	7,930	154,190
Balance at end of period	\$ 2,354,644	\$ 146,495	\$ 597,939	\$ 31,474	\$ 1,733	\$ 81,990	\$ 3,214,275

September 30, 2012	One-to-Four Family	Multi-family	Non-residential	Commercial	Consumer Direct	Purchased Auto	Total
Balance at beginning of year	\$3,113,345	\$ 438,542	\$ 1,145,889	\$ 10,571	\$ 3,578	\$ 35,487	\$4,747,412
Provision charged to income	1,359,722	(112,800)	(7,013)	30,246	(1,449)	63,294	1,332,000
Loans charged off	(2,007,501)	(133,429)	(271,021)	(7,259)	(531)	(14,973)	(2,434,714)
Recoveries of loans previously charged off	7,283	-	-	-	181	6,427	13,891
Balance at end of period	\$2,472,849	\$ 192,313	\$ 867,855	\$ 33,558	\$ 1,779	\$ 90,235	\$3,658,589

OTTAWA SAVINGS BANCORP, INC.**Notes to Unaudited Consolidated Financial Statements****(continued)**

The following table presents the recorded investment in loans and the related allowances allocated by portfolio segment and based on impairment method as of September 30, 2013 and December 31, 2012:

September 30, 2013	One-to-four Family	Multi-family	Non-residential	Commercial	Consumer Direct	Purchased Auto	Total
Loans individually evaluated for impairment	\$3,289,437	\$-	\$2,031,956	\$-	\$-	\$-	\$5,321,393
Loans collectively evaluated for impairment	75,317,131	2,794,137	16,510,374	6,797,594	513,581	9,093,619	111,026,436
Ending Balance	\$78,606,568	\$2,794,137	\$18,542,330	\$6,797,594	\$513,581	\$9,093,619	\$116,347,829
Period-end amount allocated to:							
Loans individually evaluated for impairment	\$492,409	\$-	\$8,771	\$-	\$-	\$-	\$501,180
Loans collectively evaluated for impairment	1,862,235	146,495	589,168	31,474	1,733	81,990	2,713,095
Balance at end of period	\$2,354,644	\$146,495	\$597,939	\$31,474	\$1,733	\$81,990	\$3,214,275
December 31, 2012	One-to-four Family	Multi-family	Non-residential	Commercial	Consumer Direct	Purchased Auto	Total
Loans individually evaluated for impairment	\$2,891,821	\$-	\$2,726,297	\$-	\$-	\$-	\$5,618,118
Loans collectively evaluated for impairment	80,126,935	4,849,766	17,780,563	8,648,191	542,652	7,810,067	119,758,174
Ending Balance	\$83,018,756	\$4,849,766	\$20,506,860	\$8,648,191	\$542,652	\$7,810,067	\$125,376,292

Edgar Filing: Ottawa Savings Bancorp, Inc. - Form 10-Q

Period-end
amount allocated
to:

Loans individually evaluated for impairment	\$ 147,209	\$ -	\$ 31,208	\$ -	\$ -	\$ -	\$ 178,417
Loans collectively evaluated for impairment	1,910,127	161,901	980,911	75,130	1,465	73,490	3,203,024
Balance at end of year	\$ 2,057,336	\$ 161,901	\$ 1,012,119	\$ 75,130	\$ 1,465	\$ 73,490	\$ 3,381,441

OTTAWA SAVINGS BANCORP, INC.**Notes to Unaudited Consolidated Financial Statements****(continued)**

The allowance for loan losses is evaluated on a regular basis by management and is based upon management's periodic review of the collectability of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral and prevailing economic conditions.

The following table presents loans individually evaluated for impairment, by class of loans, as of September 30, 2013 and December 31, 2012:

September 30, 2013	Unpaid	Recorded	Recorded	Total Recorded Investment	Related Allowance	Average Recorded Investment
	Contractual	Investment	Investment			
	Principal Balance	With No Allowance	With Allowance			
One-to-four family	\$3,630,860	\$1,890,588	\$1,398,849	\$3,289,437	\$492,409	\$3,578,310
Multi-family	286,906	-	-	-	-	21,378
Non-residential	4,646,709	2,023,185	8,771	2,031,956	8,771	2,175,093
Commercial	-	-	-	-	-	-
Consumer direct	-	-	-	-	-	-
Purchased auto	-	-	-	-	-	-
	\$8,564,475	\$3,913,773	\$1,407,620	\$5,321,393	\$501,180	\$5,774,781

December 31, 2012	Unpaid	Recorded	Recorded	Total Recorded Investment	Related Allowance	Average Recorded Investment
	Contractual	Investment	Investment			
	Principal Balance	With No Allowance	With Allowance			
One-to-four family	\$3,664,253	\$820,150	\$2,071,671	\$2,891,821	\$147,209	\$6,141,106
Multi-family	-	-	-	-	-	104,209
Non-residential	6,596,593	683,589	2,042,708	2,726,297	31,208	1,814,361

Edgar Filing: Ottawa Savings Bancorp, Inc. - Form 10-Q

Commercial	-	-	-	-	-	605
Consumer direct	-	-	-	-	-	12,057
Purchased auto	-	-	-	-	-	12,057
	\$10,260,846	\$1,503,739	\$4,114,379	\$5,618,118	\$178,417	\$8,084,395

For the three and nine months ended September 30, 2013 and 2012, the Company recognized no accrued or cash basis interest income on impaired loans.

At September 30, 2013, there were 33 impaired loans totaling approximately \$5.3 million, compared to 22 impaired loans totaling approximately \$5.6 million at December 31, 2012. The change in impaired loans was a result of adding 28 loans totaling approximately \$3.0 million to the impaired loan list, offset by writing down and moving seven impaired loans totaling approximately \$614,000 to OREO, returning five impaired loans totaling approximately \$631,000 to performing status, writing down two impaired loans by a total of approximately \$147,000, and restructuring 12 impaired loans using A/B note restructurings in which there were five modified loans at market rates remaining which resulted in charge offs of approximately \$616,000. Additionally, there were four impaired loan payoffs totaling approximately \$1.2 million, and an impaired loan of approximately \$269,000 moved to held for sale which was subsequently sold.

Our loan portfolio also includes certain loans that have been modified in a troubled debt restructuring (“TDR”), where economic concessions have been granted to borrowers who have experienced financial difficulties. These concessions typically result from our loss mitigation activities and could include reductions in the interest rate, payment extensions, forbearance or other actions. TDRs are classified as nonperforming at the time of restructuring and typically are returned to performing status after considering the borrower’s sustained repayment performance for a reasonable period of at least six months.

When we modify loans in a TDR, we evaluate any possible impairment similar to other impaired loans based on the present value of expected future cash flows, discounted at the contractual interest rate of the original loan agreement, or use the current fair value of the collateral, less estimated selling costs, for collateral dependent loans. If we determine that the value of the modified loan is less than the recorded investment in the loan (net of previous charge-offs, deferred loan fees or costs and unamortized premium or discount), impairment is recognized through an allowance estimate or a charge-off to the allowance. In periods subsequent to modification, we evaluate all TDRs, including those that have payment defaults, for possible impairment and recognize impairment through the allowance.

Impaired loans at September 30, 2013 included \$3.5 million of loans whose terms have been modified in troubled debt restructurings compared to \$3.1 million at December 31, 2012. The restructured loans are being monitored as they have not attained per accounting guidelines the performance requirements for the set time period to achieve being returned to accrual status.

Loans classified as troubled debt restructuring during the three and nine months ended September 30, 2013 and 2012, segregated by class are shown in the tables below.

	Three Months Ended			Three Months Ended		
	September 30, 2013			September 30, 2012		
	Number of Modifications	Recorded (as of period end)	Increase in Allowance	Number of Modifications	Recorded (as of period end)	Increase in Allowance
One-to-four family	5	\$ 657,180	\$ -	5	\$ 509,875	\$ -
Multi-family	-	-	-	-	-	-
Non-residential	-	-	-	-	-	-
Commercial	-	-	-	-	-	-
Consumer direct	-	-	-	-	-	-
Purchased auto	-	-	-	-	-	-
	5	\$ 657,180	\$ -	5	\$ 509,875	\$ -

During the three months ended September 30, 2013, all five of the one-to-four family loan modifications were classified as TDRs due to A/B note restructurings which involved principal reductions. One of the new modifications paid-off two existing TDRs, with one new note at a market rate. Another of the new modifications restructured 7 impaired loans into an A/B note structure with the new note at a market rate and the B note being charged off. The other three of the new modifications restructured 3 impaired loans for the same borrower into three A/B note structures with three new notes at market rates and the associated B notes being charged off. Total charge-offs were \$616,000 for these TDRs.

	Nine Months Ended			Nine Months Ended		
	September 30, 2013			September 30, 2012		
	Number of Modifications (as of period end)	Recorded Investment	Increase in Allowance	Number of Modifications (as of period end)	Recorded Investment	Increase in Allowance
One-to-four family	5	\$ 657,180	\$ -	6	\$ 629,770	\$ -
Multi-family	-	-	-	-	-	-
Non-residential	-	-	-	-	-	-
Commercial	-	-	-	-	-	-
Consumer direct	-	-	-	-	-	-
Purchased auto	-	-	-	-	-	-
	5	\$ 657,180	\$ -	6	\$ 629,770	\$ -

Troubled debt restructured loans that were restructured during the twelve months prior to the dates indicated and had payment defaults (i.e., 60 days or more past due following a modification), during the three and nine months ended September 30, 2013 and 2012, segregated by class are shown below.

There were no payment defaults during the three months ended September 30, 2013 and 2012.

	Nine Months Ended		Nine Months Ended	
	September 30, 2013		September 30, 2012	
	Number of Defaults (as of period end)	Investment Recorded (as of period end)	Number of Defaults (as of period end)	Investment Recorded (as of period end)
One-to-four family	-	\$ -	1	\$ 212,014
Multi-family	-	-	-	-
Non-residential	-	-	-	-
Commercial	-	-	-	-
Consumer direct	-	-	-	-
Purchased auto	-	-	-	-
	-	\$ -	1	\$ 212,014

All TDRs are evaluated for possible impairment and any impairment identified is recognized through the allowance. Additionally, the qualitative factors are updated quarterly for trends in economic and nonperforming factors, including consideration of TDRs.

The following table presents the recorded investment in nonaccrual loans and loans past due over 90 days still on accrual status, by class of loans, as of September 30, 2013 and December 31, 2012:

		Loans Past Due
September 30, 2013	Nonaccrual	Over 90 Days Still
		Accruing
One-to-four family	\$3,384,846	\$ -
Multi-family	-	-
Non-residential	2,031,956	-
Commercial	-	-
Consumer direct	-	-
Purchased auto	-	-
	\$5,416,802	\$ -

		Loans Past Due
December 31, 2012	Nonaccrual	Over 90 Days Still
		Accruing
One-to-four family	\$3,067,190	\$106,457
Multi-family	-	-
Non-residential	2,985,987	164,305
Commercial	-	-
Consumer direct	-	-
Purchased auto	-	-
	\$6,053,177	\$270,762

The following table presents the aging of the recorded investment in loans, by class of loans, as of September 30, 2013 and December 31, 2012:

	Loans 30-59 Days Past Due	Loans 60- 89 Days Past Due	Loans 90 or More Days Past Due	Total Past Due Loans	Current Loans	Total Loans
September 30, 2013						
One-to-four family	\$2,437,129	\$300,780	\$897,682	\$3,635,591	\$74,970,977	\$78,606,568
Multi-family	265,611	-	-	265,611	2,528,526	2,794,137
Non-residential	436,748	235,000	-	671,748	17,870,582	18,542,330
Commercial	-	-	-	-	6,797,594	6,797,594
Consumer direct	-	-	-	-	513,581	513,581
Purchased auto	-	-	-	-	9,093,619	9,093,619
	\$3,139,488	\$535,780	\$897,682	\$4,572,950	\$111,774,879	\$116,347,829

	Loans 30-59 Days Past Due	Loans 60- 89 Days Past Due	Loans 90 or More Days Past Due	Total Past Due Loans	Current Loans	Total Loans
December 31, 2012						
One-to-four family	\$2,322,111	\$616,274	\$1,621,408	\$4,559,793	\$78,458,963	\$83,018,756
Multi-family	97,267	-	-	97,267	4,752,499	4,849,766
Non-residential	473,458	334,389	516,414	1,324,261	19,182,599	20,506,860

Edgar Filing: Ottawa Savings Bancorp, Inc. - Form 10-Q

Commercial	23,601	-	-	23,601	8,624,590	8,648,191
Consumer direct	-	-	-	-	542,652	542,652
Purchased auto	6,422	19,257	-	25,679	7,784,388	7,810,067
	\$2,922,859	\$969,920	\$2,137,822	\$6,030,601	\$119,345,691	\$125,376,292

Credit Quality Indicators:

The Company categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, public information and current economic trends, among other factors. The Company analyzes loans individually by classifying the loans as to credit risk. For commercial and non-residential real estate loans, the Company's credit quality indicator is internally assigned risk ratings. Each commercial and non-residential real estate loan is assigned a risk rating upon origination. The risk rating is reviewed annually, at a minimum, and on an as needed basis depending on the specific circumstances of the loan.

For residential real estate loans, multi-family, consumer direct and purchased auto loans, the Company's credit quality indicator is performance determined by delinquency status. Delinquency status is updated regularly by the Company's loan system for real estate loans, multi-family and consumer direct loans. The Company receives monthly reports on the delinquency status of the purchased auto loan portfolio from the servicing company.

The Company uses the following definitions for risk ratings:

Pass – loans classified as pass are of a higher quality and do not fit any of the other “rated” categories below (e.g. special mention, substandard or doubtful). The likelihood of loss is considered remote.

Special Mention – loans classified as special mention have a potential weakness that deserves management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or of the institution's credit position at some future date.

Substandard – loans classified as substandard are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected.

Doubtful – loans classified as doubtful have all the weaknesses inherent in those classified as substandard, with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable and improbable.

Not Rated – loans in this bucket are not evaluated on an individual basis.

As of September 30, 2013 and December 31, 2012, the risk category of loans by class is as follows:

September 30, 2013	Pass	Special	Substandard	Doubtful	Not rated
		Mention			
One-to-four family	\$-	\$2,284,598	\$3,289,437	\$ -	\$73,032,533
Multi-family	-	-	-	-	2,794,137
Non-residential	14,654,770	1,855,604	2,031,956	-	-
Commercial	6,638,131	159,463	-	-	-
Consumer direct	-	859	-	-	512,722
Purchased auto	-	-	-	-	9,093,619
Total	\$21,292,901	\$4,300,524	\$5,321,393	\$ -	\$85,433,011

December 31, 2012	Pass	Special	Substandard	Doubtful	Not rated
		Mention			
One-to-four family	\$-	\$3,925,077	\$2,891,821	\$ -	\$76,201,858
Multi-family	-	3,826	-	-	4,845,940
Non-residential	17,466,220	314,343	2,726,297	-	-
Commercial	8,486,147	162,044	-	-	-
Consumer direct	-	3,766	-	-	538,886
Purchased auto	-	-	-	-	7,810,067
Total	\$25,952,367	\$4,409,056	\$5,618,118	\$ -	\$89,396,751

NOTE 9 – STOCK COMPENSATION

Total stock-based compensation expense was approximately \$20,000 and \$11,000 for the nine months ended September 30, 2013 and 2012, respectively. In accordance with FASB ASC 718, *Compensation-Stock Compensation*, compensation expense is recognized on a straight-line basis over the grantees' vesting period or to the grantees' retirement eligibility date, if earlier. During the nine months ended September 30, 2013 and 2012, the Company did not grant additional options or shares under the MRP.

NOTE 10 – RECENT ACCOUNTING DEVELOPMENTS

In February 2013, the FASB issued ASU No. 2013-02, *Comprehensive Income (Topic 220): Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income*. The Update improves the reporting of reclassifications out of accumulated other comprehensive income by requiring an entity to report the effect of significant reclassifications out of accumulated other comprehensive income on the respective line items in net income if the amount being reclassified is required under U.S. generally accepted accounting principles (GAAP) to be reclassified in its entirety to net income. For other amounts that are not required under U.S. GAAP to be reclassified in their entirety to net income in the same reporting period, an entity is required to cross-reference other disclosures required under U.S. GAAP that provide additional detail about those amounts. The adoption of ASU No. 2013-02 on January 1, 2013 did not have an impact on the Company's financial position, results of operation or cash flows.

NOTE 11 – FAIR VALUE MEASUREMENT AND DISCLOSURE

FASB ASC Topic 820, Fair Value Measurements and Disclosures, clarifies that fair value is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants and is not adjusted for transaction costs. This guidance also establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurement inputs) and the lowest priority to unobservable inputs (Level 3 measurement inputs). The three levels of the fair value hierarchy under FASB ASC 820 are described below:

Basis of Fair Value Measurement:

- Level 1 - Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets.

- Level 2 - Significant other observable inputs other than Level 1 prices such as quoted prices in markets that are not active, quoted prices for similar assets, or other inputs that are observable, either directly or indirectly, for substantially the full term of the asset.

- Level 3 - Prices or valuation techniques that require inputs that are both significant to the fair value measurement and unobservable (i.e., supported by little or no market activity).

Following is a description of valuation methodologies used for assets and liabilities recorded at fair value:

Securities Available for Sale

Securities classified as available for sale are recorded at fair value on a recurring basis using pricing obtained from an independent pricing service. Where quoted market prices are available in an active market, securities are classified within Level 1. The Company has no securities classified within Level 1. If quoted market prices are not available, the pricing service estimates the fair values by using pricing models or quoted prices of securities with similar characteristics. For these securities, the inputs used by the pricing service to determine fair value consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information and bonds' terms and conditions, among other things resulting in classification within Level 2. Level 2 securities include state and municipal securities, and residential mortgage-backed securities. In cases where Level 1 or Level 2 inputs are not available, securities are classified within Level 3. The Company has no securities classified within Level 3.

Foreclosed Assets

Foreclosed assets consisting of foreclosed real estate and repossessed assets, are adjusted to fair value less estimated costs to sell upon transfer of the loans to foreclosed assets. Subsequently, foreclosed assets are carried at the lower of cost or fair value. Fair value is based upon independent market prices, appraised values of the collateral or management's estimation of the value of the collateral. When the fair value of the collateral is based on an observable market price or a current appraised value, the Company records the foreclosed asset as non-recurring Level 2. When an appraised value is not available or management determines the fair value of the collateral is further impaired below the appraised value and there is no observable market price, the Company records the foreclosed asset as non-recurring Level 3.

Impaired Loans

Impaired loans are evaluated and adjusted to the lower of carrying value or fair value less estimated costs to sell at the time the loan is identified as impaired. Impaired loans are carried at the lower of cost or fair value. Fair value is measured based on the value of the collateral securing these loans. When the fair value of the collateral is based on an

observable market price or a current appraised value, the Company records the impaired loan as non-recurring Level 2. When an appraised value is not available or management determines the fair value of the collateral is further impaired below the appraised value and there is no observable market price, the Company records the impaired loan as non-recurring Level 3.

The Company did not have any transfers of assets or liabilities between Levels 1 and 2 of the fair value hierarchy during the nine months ended September 30, 2013 and the year ended December 31, 2012. The Company's policy for determining transfers between levels occurs at the end of the reporting period when circumstances in the underlying valuation criteria change and result in transfers between levels.

The tables below present the recorded amount of assets measured at fair value on a recurring basis at September 30, 2013 and December 31, 2012.

September 30, 2013	Level 1	Level 2	Level 3	Total Fair Value
State and municipal securities available for sale	\$ -	\$8,460,769	\$ -	\$8,460,769
Residential mortgage-backed securities available for sale	-	26,491,691	-	26,491,691
	\$ -	\$34,952,460	\$ -	\$34,952,460

December 31, 2012	Level 1	Level 2	Level 3	Total Fair Value
State and municipal securities available for sale	\$ -	\$7,120,522	\$ -	\$7,120,522
Residential mortgage-backed securities available for sale	-	21,743,081	-	21,743,081
	\$ -	\$28,863,603	\$ -	\$28,863,603

The tables below present the recorded amount of assets measured at fair value on a non-recurring basis at September 30, 2013 and December 31, 2012.

September 30, 2013	Level 1	Level 2	Level 3	Total
				Fair Value
Foreclosed assets	\$ -	\$ -	\$955,785	\$955,785
Impaired loans, net	-	-	906,440	906,440

December 31, 2012	Level 1	Level 2	Level 3	Total
				Fair Value
Foreclosed assets	\$ -	\$ -	\$1,305,921	\$1,305,921
Impaired loans, net	-	-	3,597,690	3,597,690

In accordance with accounting pronouncements, the carrying value and estimated fair value of the Company's financial instruments as of September 30, 2013 and December 31, 2012 are as follows:

	Carrying Amount	Fair Value Measurements at			Total
		September 30, 2013 using:			
		Level 1	Level 2	Level 3	
Financial Assets:					
Cash and cash equivalents	\$5,208,959	\$5,208,959	\$-	\$-	\$5,208,959
Federal funds sold	2,885,000	2,885,000	-	-	2,885,000
Securities	36,185,996	-	36,185,996	-	36,185,996
Accrued interest receivable	670,709	670,709	-	-	670,709
Net loans	113,133,554	-	-	114,264,000	114,264,000
Loans held for sale	-	-	-	-	-
Mortgage servicing rights	160,532	-	-	160,532	160,532
Financial Liabilities:					
Non-interest bearing deposits	5,015,782	5,015,782	-	-	5,015,782
Interest bearing deposits	142,644,024	-	-	142,634,218	142,634,218
Accrued interest payable	2,780	2,780	-	-	2,780

	Carrying Amount	Fair Value Measurements at			Total
		December 31, 2012 using:			
		Level 1	Level 2	Level 3	

Edgar Filing: Ottawa Savings Bancorp, Inc. - Form 10-Q

Financial Assets:

Cash and cash equivalents	\$10,787,989	\$10,787,989	\$-	\$-	\$10,787,989
Federal funds sold	1,666,000	1,666,000	-	-	1,666,000
Securities	30,198,051	-	30,198,052	-	30,198,052
Accrued interest receivable	696,638	696,638	-	-	696,638
Net loans	121,994,851	-	-	123,748,000	123,748,000
Loans held for sale	171,095	171,095	-	-	171,095
Mortgage servicing rights	152,873	-	-	152,873	152,873
Financial Liabilities:					
Non-interest bearing deposits	4,313,635	4,313,635	-	-	4,313,635
Interest bearing deposits	150,761,010	-	-	150,921,365	150,921,365
Accrued interest payable	806	806	-	-	806

The following methods and assumptions were used by the Bank in estimating the fair value of financial instruments:

Cash and Cash Equivalents: The carrying amounts reported in the balance sheets for cash and cash equivalents approximate fair values.

Federal Funds Sold: The carrying amounts reported in the balance sheets for federal funds sold approximate fair values.

Securities: The Company obtains fair value measurements of available for sale securities from an independent pricing service. See Note 11 - Fair Value Measurement and Disclosure for further detail on how fair values of securities available for sale are determined. The carrying value of non-marketable equity securities approximates fair value.

Loans: For variable-rate loans that re-price frequently and with no significant change in credit risk, fair values are based on carrying amounts. The fair values for other loans (for example, fixed rate commercial real estate and rental property mortgage loans and commercial and industrial loans) are estimated using discounted cash flow analysis, based on market interest rates currently being offered for loans with similar terms to borrowers of similar credit quality. Loan fair value estimates include judgments regarding future expected loss experience and risk characteristics. Fair values for impaired loans are estimated using underlying collateral values, where applicable or discounted cash flows.

Loans held for sale: The carrying amounts reported in the balance sheets for loans held for sale approximate fair values, as usually these loans are originated with the intent to sell and funding of the sales usually occurs within three days.

Accrued Interest Receivable and Payable: The carrying amounts of accrued interest receivable and payable approximate fair values.

Mortgage Servicing Rights: The carrying amounts of mortgage servicing rights approximate their fair values.

Deposits: The fair values disclosed for demand deposits are, by definition, equal to the amount payable on demand at the reporting date (that is, their carrying amounts). The carrying amounts of variable-rate, fixed-term money market accounts and certificates of deposit approximate their fair values. Fair values for fixed-rate certificates of deposit are estimated using a discounted cash flow calculation that applies market interest rates currently offered on certificates to a schedule of aggregated expected monthly maturities on time deposits.

Loan Commitments: Commitments to extend credit were evaluated and fair value was estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present creditworthiness of the counter-parties. For fixed-rate loan commitments, fair value also considers the difference between current levels of interest rates and the committed rates. The Bank does not charge fees to enter into these agreements. As of September 30, 2013 and December 31, 2012, the fair values of the commitments are immaterial in nature.

In addition, other assets and liabilities of the Bank that are not defined as financial instruments, such as property and equipment are not included in the above disclosures. Also, non-financial instruments typically not recognized in financial statements nevertheless may have value but are not included in the above disclosures. These include, among other items, the estimated earnings power of core deposit accounts, the trained work force, customer goodwill and similar items.

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

Management's discussion and analysis of the financial condition and results of operations is intended to assist in understanding the financial condition and results of operations of the Company. The information contained in this section should be read in conjunction with the Unaudited Consolidated Financial Statements and footnotes appearing in Part I, Item 1 of this document.

FORWARD-LOOKING INFORMATION

Statements contained in this report that are not historical facts may constitute forward-looking statements (within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended), which involve significant risks and uncertainties. The Company intends such forward-looking statements to be covered by the safe harbor provisions for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995, and is including this statement for purposes of invoking these safe harbor provisions. Forward-looking statements, which are based on certain assumptions and describe future plans, strategies and expectations of the Company, are generally identifiable by the use of the words “believe,” “expect,” “intend,” “anticipate,” “estimate,” “project,” “plan,” or similar expressions. The Company’s ability to predict results or the actual effect of future plans or strategies is inherently uncertain and actual results may differ from those predicted. The Company undertakes no obligation to update these forward-looking statements in the future. The Company cautions readers of this report that a number of important factors could cause the Company’s actual results subsequent to September 30, 2013 to differ materially from those expressed in forward-looking statements. Factors that could cause actual results to differ from those predicted and could affect the future prospects of the Company include, but are not limited to, fluctuations in market rates of interest and loan and deposit pricing, changes in the securities or financial market, a deterioration of general economic conditions either nationally or locally, delays in obtaining the necessary regulatory approvals, our ability to consummate proposed transactions in a timely manner, legislative or regulatory changes that adversely affect our business, adverse developments or changes in the composition of our loan or investment portfolios, significant increases in competition, changes in real estate values, difficulties in identifying attractive acquisition opportunities or strategic partners to complement our Company’s approach and the products and services the Company offers, the possible dilutive effect of potential acquisitions or expansion, and our ability to raise new capital as needed and the timing, amount and type of such capital raises. These risks and uncertainties should be considered in evaluating forward-looking statements. Additionally, other risks and uncertainties may be described in the Company’s Annual Report on form 10-K as filed with the Securities and Exchange Commission on March 28, 2013.

GENERAL

The Bank is a community and customer-oriented savings bank. The Bank's business has historically consisted of attracting deposits from the general public and using those funds to originate and purchase one-to-four family, multi-family and non-residential real estate, construction, commercial and consumer loans, which the Bank primarily holds for investment. The Bank has continually diversified its products to meet the needs of the community. The Bank completed its reorganization pursuant to its Plan of Conversion on July 11, 2005, upon which the Bank converted from an Illinois-chartered mutual savings bank to a federally-chartered mutual savings bank, and on that same date, converted from a federally-chartered mutual savings bank to a federally-chartered stock savings bank, all of the outstanding stock of which was issued to the Company. As part of the reorganization, the Company issued 1,001,210 shares to the public and 1,223,701 shares to Ottawa Savings Bancorp MHC, a mutual holding company.

COMPARISON OF FINANCIAL CONDITION AT SEPTEMBER 30, 2013 AND DECEMBER 31, 2012

The Company's total assets decreased \$7.2 million, or 4.0%, to \$171.9 million at September 30, 2013, from \$179.0 million at December 31, 2012. The decrease in assets was primarily due to a decrease in loans of \$8.9 million, and a decrease in cash and cash equivalents of \$5.6 million. The decrease in assets was partially offset by an increase in securities available for sale of \$6.1 million and an increase in federal funds sold of \$1.2 million.

Cash and cash equivalents decreased \$5.6 million, or 51.7%, to \$5.2 million at September 30, 2013 from \$10.8 million at December 31, 2012, primarily as a result of cash used in investing and financing activities exceeding the cash provided by operating activities, and decrease in deposits which resulted from management strategically pricing deposits based on market conditions.

Securities available for sale increased \$6.1 million, or 21.1%, to \$35.0 million at September 30, 2013 from \$28.9 million at December 31, 2012. The increase was primarily the result of \$12.8 million in purchases offset by pay-downs of \$5.5 million.

Loans, net of the allowance for loan losses, decreased \$8.9 million, or 7.3%, to \$113.1 million at September 30, 2013 from \$122.0 million at December 31, 2012. The decrease in loans, net of the allowance for loan losses, was primarily caused by a combination of normal attrition, pay-downs, loan charge-offs and strategic initiatives to reduce lending exposure in one-to-four family residential, non-residential loans, and multifamily residential loans, augmented by a decrease in the allowance for loan losses of \$0.2 million and partially offset by an increase of \$1.3 million in the purchased auto loan portfolio. The Company is focusing its lending efforts on customers based primarily in its local market and purchased auto loans from regulated financial institutions.

Foreclosed real estate decreased approximately \$0.4 million, or 30.1%, to \$0.9 million at September 30, 2013 from \$1.3 million at December 31, 2012. The decrease was primarily due to the sale of 19 properties for aggregate proceeds of \$0.8 million offset by the addition of 11 properties valued at \$0.6 million acquired through loan foreclosures due to the continued stress the economic environment has placed on the Company's customers and further write-downs of \$0.1 million due to declines in real estate values.

Other assets comprised primarily of prepaid expenses, deferred director compensation accounts, and auto loan repossessions, increased approximately \$0.4 million, or 25.2%, to \$1.8 million at September 30, 2013 from \$1.4 million at December 31, 2012.

Total deposits decreased \$7.4 million, or 4.8%, to \$147.7 million at September 30, 2013, from \$155.1 million at December 31, 2012. The decrease is primarily due to a decrease in certificates of deposit of \$8.7 million, or 8.5% and a decrease in money market accounts of \$0.6 million, or 3.0%, from December 31, 2012 to September 30, 2013. The decrease was partially offset by an increase in savings accounts of \$0.8 million, or 5.0%, and an increase in checking accounts of \$1.2 million, or 6.9% from December 31, 2012 to September 30, 2013. The increase in savings and checking accounts is primarily due to customers moving funds into non-term products as they wait for a better rate environment. The reduction in certificate of deposit accounts is due to management's strategic initiative to pay competitive rates, but not the highest rates in the market.

Other liabilities comprised of primarily deferred compensation expenses, accrued expenses and escrow payable, remained constant, increasing about \$42,000, or 1.6%, to remain at \$2.7 million at September 30, 2013.

Equity increased approximately \$129,000, or 0.6%, to \$21.2 million at September 30, 2013, from \$21.0 million at December 31, 2012. The increase in equity is primarily a result of net income for the nine months ended September 30, 2013 of approximately \$0.6 million, offset by other comprehensive losses on available for sale securities during the period of approximately \$0.5 million.

The ongoing state of economic uncertainty continues to affect our asset quality. We continue to experience a decline in the market values of homes in our market area in general and also on specific properties held as collateral. In addition, higher unemployment locally continues to affect some of our borrowers' ability to timely repay their obligations to the Company. These conditions have resulted in nonperforming loans totaling 4.6% of total loan receivables as of September 30, 2013, which is down slightly from 5.0% at December 31, 2012.

The Company's nonperforming assets consist of non-accrual loans, loans past due greater than 90 days and still accruing and foreclosed real estate. Loans are generally placed on non-accrual status when it is apparent all of the contractual payments (i.e. principal and interest) will not be received; however, they may be placed on non-accrual status sooner if management has significant doubt as to the collection of all amounts due. Interest previously accrued but uncollected is reversed and charged against interest income. During the first nine months of 2013, nonaccrual loans decreased 8.8% to \$5.5 million from \$6.1 million as of December 31, 2012. The decrease is a result of payoffs on four loans totaling approximately \$1.2 million, five loans totaling approximately \$0.6 million that were upgraded to performing status, two loans with partial charge-offs totaling approximately \$0.1 million, one loan of approximately \$0.3 million was moved to held for sale and subsequently sold, and seven loans of approximately \$0.6 million were moved to foreclosed real estate. The decreases were offset by the addition of 26 one-to-four family loans totaling approximately \$2.8 million and two non-residential loans totaling approximately \$0.2 million that were placed on non-accrual status, as certain customers continue to be challenged by local economic conditions during these difficult economic times.

The following table summarizes nonperforming assets for the prior five quarters.

	September 30, 2013	June 30, 2013	March 31, 2013	December 31, 2012	September 30, 2012
	(In Thousands)				
Non-accrual:					
One-to-four family	\$3,385	\$3,433	\$4,153	\$ 3,067	\$ 5,687
Multi-family	-	-	-	-	5
Non-residential real estate	2,032	2,480	2,355	2,986	1,618
Commercial	-	-	-	-	-
Consumer direct	-	-	-	-	-
Purchased auto	-	-	-	-	17
Total non-accrual loans	5,417	5,913	6,508	6,053	7,327
Past due greater than 90 days and still accruing:					
One-to-four family	-	15	15	107	64
Non-residential real estate	-	51	-	164	-
Commercial	-	23	-	-	-
Consumer direct	-	1	1	-	-
Total nonperforming loans	5,417	6,003	6,524	6,324	7,391
Foreclosed real estate	907	763	900	1,297	1,122
Other repossessed assets	48	50	12	9	19
Total nonperforming assets	\$6,372	\$6,816	\$7,436	\$ 7,630	\$ 8,532

The table below presents selected asset quality ratios for the prior five quarters.

	September 30, 2013		June 30, 2013		March 31, 2013		December 31, 2012		September 30, 2012	
Allowance for loan losses as a percent of gross loans receivable	2.73	%	3.21	%	2.90	%	2.69	%	2.80	%
Allowance for loan losses as a percent of total nonperforming loans	59.33	%	64.13	%	55.13	%	53.46	%	49.47	%
Nonperforming loans as a percent of gross loans receivable	4.61	%	5.01	%	5.25	%	5.04	%	5.66	%
Nonperforming loans as a percent of total assets	3.15	%	3.39	%	3.58	%	3.53	%	4.06	%
Nonperforming assets as a percent of total assets	3.71	%	3.85	%	4.08	%	4.26	%	4.68	%

COMPARISON OF RESULTS OF OPERATION FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2013 AND 2012

General. Net income for the three months ended September 30, 2013 was \$169,000 compared to net income of \$179,000 for the three months ended September 30, 2012. Net income decreased slightly during the third quarter of 2013 primarily due to lower interest and dividend income, decreases in other income, and an increase in operating costs. The decreases were slightly offset by lower levels of provision for loan losses than in the 2012 period, lower funding costs, and decreased tax expenses.

Net Interest Income. The following table summarizes interest and dividend income and interest expense for the three months ended September 30, 2013 and 2012.

	Nine Months Ended			
	September 30,		\$ change	% change
	2013	2012		
	(Dollars in thousands)			
Interest and dividend income:				
Interest and fees on loans	\$4,761	\$5,291	\$ (530)	(10.02)%
Securities:				
Residential mortgage-backed securities	334	499	(165)	(33.07)
U.S. agency securities	-	38	(38)	(100.00)
State and municipal securities	197	151	46	30.46
Dividends on non-marketable equity securities	3	3	-	-
Interest-bearing deposits	4	3	1	33.33
Total interest and dividend income	5,299	5,985	(686)	(11.46)
Interest expense:				
Deposits	1,152	1,670	(518)	(31.02)
Total interest expense	1,152	1,670	(518)	(31.02)
Net interest income	\$4,147	\$4,315	\$ (168)	(3.89)%

The following table presents for the periods indicated the total dollar amount of interest income from average interest-earning assets and the resultant yields, as well as the interest expense on average interest bearing liabilities, expressed both in dollars and rates. No tax equivalent adjustments were made. All average balances are monthly average balances. Non-accruing loans have been included in the table as loans carrying a zero yield. The amortization of loan fees is included in computing interest income; however, such fees are not material.

	Three Months Ended September 30,							
	2013		2012		2013		2012	
	AVERAGE	AVERAGE	INTERESTYIELD/	AVERAGE	AVERAGE	INTERESTYIELD/	AVERAGE	
	BALANCE	BALANCE	COST	BALANCE	BALANCE	COST	COST	
	(Dollars in thousands)							
Interest-earning assets								
Loans receivable, net (1)	\$ 113,958	\$ 1,495	5.25	%	\$ 127,504	\$ 1,708	5.36	%
Securities, net (2)	34,681	183	2.11	%	31,822	211	2.65	%
Non-marketable equity securities	1,234	1	0.32	%	1,475	1	0.27	%
Interest-bearing deposits	7,461	1	0.05	%	5,758	-	0.00	%
Total interest-earning assets	157,334	1,680	4.27	%	166,559	1,920	4.61	%
Interest-bearing liabilities								
Money Market accounts	\$ 20,375	\$ 12	0.24	%	\$ 20,328	\$ 19	0.37	%
Passbook accounts	16,324	3	0.07	%	15,097	4	0.11	%
Certificates of Deposit accounts	94,488	328	1.39	%	107,337	505	1.88	%
Checking accounts	13,130	1	0.03	%	11,980	2	0.07	%
Total interest-bearing liabilities	144,317	344	0.95	%	154,742	530	1.37	%
NET INTEREST INCOME		\$ 1,336				\$ 1,390		
NET INTEREST RATE SPREAD (3)			3.32	%			3.24	%
NET INTEREST MARGIN (4)			3.40	%			3.34	%
RATIO OF AVERAGE INTEREST-EARNING ASSETS TO AVERAGE INTEREST-BEARING LIABILITIES			109.02	%			107.64	%

(1) Amount is net of deferred loan origination (costs) fees, undisbursed loan funds, unamortized discounts and allowance for loans and includes non-performing loans.

(2) Includes unamortized discounts and premiums.

(3) Net interest rate spread represents the difference between the yield on average interest-earning assets and the average cost of interest-bearing liabilities.

(4) Net interest margin represents net interest income divided by average interest-earning assets.

(1) Amount is net of deferred loan origination (costs) fees, undisbursed loan funds, unamortized discounts and allowance for loan losses and includes

The following table summarizes the changes in net interest income due to rate and volume for the three months ended September 30, 2013 and 2012. The column "Net" is segmented into the changes attributable to variations in volume and the changes attributable to changes in interest rates. The variations attributable to simultaneous volume and rate changes have been proportionately allocated to rate and volume.

	Three Months Ended		
	September 30,		
	2013 Compared to		
	2012		
	Increase (Decrease)		
	Due to		
	VOLUME	RATE	NET
	(Dollars in		
	Thousands)		
Interest and dividends earned on			
Loans receivable, net	\$(177)	\$(36)	\$(213)
Securities, net	15	(43)	(28)
Non-marketable equity securities	-	-	-
Interest-bearing deposits	-	1	1
Total interest-earning assets	\$(162)	\$(78)	\$(240)
Interest expense on			
Money Market accounts	\$-	\$(7)	\$(7)
Passbook accounts	-	(1)	(1)
Certificates of Deposit accounts	(45)	(132)	(177)
Checking	-	(1)	(1)
Total interest-bearing liabilities	(45)	(141)	(186)
Change in net interest income	\$(117)	\$63	\$(54)

Net interest income decreased \$54,000, or 3.9%, to \$1.3 million for the three months ended September 30, 2013 compared to \$1.4 million for the three months ended September 30, 2012. Interest and dividend income decreased \$240,000 due to the decline in average interest earning assets of \$9.2 million and the yield decreasing on interest earning assets from 4.6% to 4.3%. The decline in the loan portfolios contributed to a significant amount of the decline in earning assets. The yield on the investment portfolio and the loan portfolio declined as the low rate environment continued during the third quarter of 2013. This decline in interest income was offset by an \$186,000, or 35.1%, reduction in interest expense. The cost of funds declined 42 basis points, or 30.7%, for the three months ended September 30, 2013 compared to the three months ended September 30, 2012, due to the continued low rate environment. Additionally, the average balance of interest bearing liabilities declined by \$10.4 million, or 6.7%. Net interest margin improved during the three months ended September 30, 2013 to 3.4% compared to 3.3% at September 30, 2012.

Provision for Loan Losses. Management recorded a loan loss provision of \$225,000 for the three months ended September 30, 2013, compared to \$330,000 for the three months ended September 30, 2012. The provision is primarily attributed to the reserves required for the one-to-four family segment as the economic conditions in the local market continue to negatively impact collateral values of real estate and the ability of borrowers to keep current per terms of their obligations. The slow payment activity and continued degradation of property values are the result of local economic conditions continuing to lag national indicators, including higher levels of unemployment locally of 11.3%, versus 9.2% for the State of Illinois and the national level of 7.3%. For the three months ended September 30, 2013, charge-offs increased due to several A/B note restructurings in which \$616,000 related to the B notes was charged off. This level is elevated in comparison to the first and second quarters of 2013 but lower than the charge-off levels experienced for the three months ended September 30, 2012.

Management uses available information to establish the appropriate level of the allowance for loan losses. Future additions or reductions to the allowance may be necessary based on estimates that are susceptible to change as a result of changes in economic conditions and other factors. As a result, our allowance for loan losses may not be sufficient to cover actual loan losses, and future provisions for loan losses could materially adversely affect the Company's operating results. In addition, various regulatory agencies, as an integral part of their examination process, periodically review the Company's allowance for loan losses. Such agencies may require the Company to recognize adjustments to the allowance based on their judgments about information available to them at the time of their examination.

Other Income. The following table summarizes other income for the three months ended September 30, 2013 and 2012.

Three months ended			
September 30,			
2013	2012	\$	%
		change	change
(Dollars in thousands)			

Other income:

Gain on sale of securities	\$-	\$-	\$ -	-	%
Gain on sale of loans	18	19	(1)	(5.26)	
Gain on sale of OREO	-	27	(27)	(100.00)	
Origination of mortgage servicing rights, net of amortization	3	(6)	9	150.00	
Customer service fees	81	73	8	10.96	
(Loss) income on bank owned life insurance	(2)	8	(10)	(125.00)	
Other	16	22	(6)	(27.27)	
Total other income	\$116	\$143	\$ (27)	(18.88)%	

The decrease in total other income was primarily a result of no gains on the sale of OREO for the three months ended September 30, 2013, compared to gains of \$27,000 for the three months ended September 30, 2012. Also contributing to the decrease were losses on bank owned life insurance, offset by increases in mortgage servicing rights and customer service fees.

Other Expenses. The following table summarizes other expenses for the three months ended September 30, 2013 and 2012.

	Three months ended			
	September 30,		\$ change	% change
2013	2012			
	(Dollars in thousands)			
Other expenses:				
Salaries and employee benefits	\$389	\$400	\$ (11)	(2.75)%
Directors fees	25	21	4	19.05
Occupancy	116	111	5	4.50
Deposit insurance premium	57	62	(5)	(8.06)
Legal and professional services	80	53	27	50.94
Data processing	68	81	(13)	(16.05)
Valuation adjustments and expenses on foreclosed real estate	72	61	11	18.03
Loss on sale of OREO	18	-	18	100.00
Other	131	120	11	9.17
Total other expenses	\$956	\$909	\$ 47	5.17 %
Efficiency ratio (1)	65.84%	59.30%		

(1) Computed as other expenses divided by the sum of net interest income and other income.

The increase in other expenses was primarily due to increases in valuation adjustments and expenses on foreclosed real estate, increases in losses on the sale of OREO due to the number of OREO properties, and an increase in legal and professional services due to compliance related activities. The increases were slightly offset by decreases in salaries and employee benefits, decreases in data processing, and decreases in deposit insurance premium during the three months ended September 30, 2013 as compared to the three months ended September 30, 2012. The efficiency ratio increased due to higher costs for the period and lower revenue levels.

Income Taxes. The Company recorded income tax expenses of \$102,000 and \$115,000 for the three months ended September 30, 2013 and 2012, respectively.

COMPARISON OF RESULTS OF OPERATION FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2013 AND 2012

General. Net income for the nine months ended September 30, 2013 was \$635,000 compared to net income of \$574,000 for the nine months ended September 30, 2012. Net income improved during the nine months of 2013 primarily due to lower levels of provision for loan losses than in the 2012 period, lower funding costs, and increases in other income. These positive variances were slightly offset by lower interest and dividend income, an increase in operating costs, and increased tax expenses.

Net Interest Income. The following table summarizes interest and dividend income and interest expense for the nine months ended September 30, 2013 and 2012.

	Nine Months Ended			
	September 30,		\$ change	% change
	2013	2012		
	(Dollars in thousands)			
Interest and dividend income:				
Interest and fees on loans	\$4,761	\$5,291	\$ (530)	(10.02)%
Securities:				
Residential mortgage-backed securities	334	499	(165)	(33.07)
U.S. agency securities	-	38	(38)	(100.00)
State and municipal securities	197	151	46	30.46
Dividends on non-marketable equity securities	3	3	-	-
Interest-bearing deposits	4	3	1	33.33
Total interest and dividend income	5,299	5,985	(686)	(11.46)
Interest expense:				
Deposits	1,152	1,670	(518)	(31.02)
Total interest expense	1,152	1,670	(518)	(31.02)
Net interest income	\$4,147	\$4,315	\$ (168)	(3.89)%

The following table presents for the periods indicated the total dollar amount of interest income from average interest-earning assets and the resultant yields, as well as the interest expense on average interest bearing liabilities, expressed both in dollars and rates. No tax equivalent adjustments were made. All average balances are monthly average balances. Non-accruing loans have been included in the table as loans carrying a zero yield. The amortization of loan fees is included in computing interest income; however, such fees are not material.

	Nine Months Ended September 30,							
	2013		2012		2013		2012	
	AVERAGE	AVERAGE	AVERAGE	AVERAGE	AVERAGE	AVERAGE	AVERAGE	AVERAGE
	BALANCE	INTERESTYIELD/ COST	BALANCE	INTERESTYIELD/ COST	BALANCE	INTERESTYIELD/ COST	BALANCE	INTERESTYIELD/ COST
	(Dollars in thousands)							
Interest-earning assets								
Loans receivable, net (1)	\$ 116,950	\$ 4,761	5.43	%	\$ 125,977	\$ 5,291	5.60	%
Securities, net (2)	33,186	531	2.13	%	33,437	688	2.74	%
Non-marketable equity securities	1,278	3	0.31	%	1,807	3	0.22	%
Interest-bearing deposits	9,346	4	0.06	%	6,049	3	0.07	%
Total interest-earning assets	160,760	5,299	4.39	%	167,270	5,985	4.77	%
Interest-bearing liabilities								
Money Market accounts	\$ 20,835	\$ 38	0.24	%	\$ 20,363	\$ 67	0.44	%
Passbook accounts	16,534	11	0.09	%	15,008	15	0.13	%
Certificates of Deposit accounts	98,099	1,098	1.49	%	108,833	1,580	1.94	%
Checking accounts	13,358	5	0.05	%	12,642	8	0.08	%
Total interest-bearing liabilities	148,826	1,152	1.03	%	156,846	1,670	1.42	%
NET INTEREST INCOME		\$ 4,147				\$ 4,315		
NET INTEREST RATE SPREAD (3)			3.36	%			3.35	%
NET INTEREST MARGIN (4)			3.44	%			3.44	%
RATIO OF AVERAGE INTEREST-EARNING ASSETS TO AVERAGE INTEREST-BEARING LIABILITIES			108.02	%			106.65	%

(1) Amount is net of deferred loan origination (costs) fees, undisbursed loan funds, unamortized discounts and allowance for loans and includes non-performing loans.

(2) Includes unamortized discounts and premiums.

(3) Net interest rate spread represents the difference between the yield on average interest-earning assets and the average cost of interest-bearing liabilities.

(4) Net interest margin represents net interest income divided by average interest-earning assets.

Edgar Filing: Ottawa Savings Bancorp, Inc. - Form 10-Q

The following table summarizes the changes in net interest income due to rate and volume for the nine months ended September 30, 2013 and 2012. The column "Net" is segmented into the changes attributable to variations in volume and the changes attributable to changes in interest rates. The variations attributable to simultaneous volume and rate changes have been proportionately allocated to rate and volume.

	Nine Months Ended September 30,		
	2013 Compared to 2012		
	Increase (Decrease) Due to		
	VOLUME	RATE	NET
	(Dollars in Thousands)		
Interest and dividends earned on			
Loans receivable, net	\$(367)	\$(163)	\$(530)
Securities, net	(4)	(153)	(157)
Non-marketable equity securities	(1)	1	-
Interest-bearing deposits	1	-	1
Total interest-earning assets	\$(371)	\$(315)	\$(686)
Interest expense on			
Money Market accounts	\$1	\$(30)	\$(29)
Passbook accounts	1	(5)	(4)
Certificates of Deposit accounts	(120)	(362)	(482)
Checking	-	(3)	(3)
Total interest-bearing liabilities	(118)	(400)	(518)
Change in net interest income	\$(253)	\$ 85	\$(168)

Net interest income decreased \$168,000, or 3.9%, to \$4.1 million for the nine months ended September 30, 2013 compared to \$4.3 million for the nine months ended September 30, 2012. Interest and dividend income decreased \$686,000 due to the decline in average interest earning assets of \$6.5 million and the yield decreasing on interest earning assets from 4.8% to 4.4%. The decline in the loan portfolio contributed to a significant amount of the decline in earning assets. The yield on the investment portfolio and the loan portfolio declined as the low rate environment continued during the first nine months of 2013. This decline in interest income was offset by a \$518,000, or 31.0%, reduction in interest expense. The cost of funds declined 39 basis points, or 27.5%, for the nine months ended September 30, 2013 compared to the nine months ended September 30, 2012, due to the continued low rate environment. Additionally, the average balance of interest bearing liabilities decreased by \$8.0 million, or 5.1%. The net interest margin for the nine months ended September 30, 2013 and 2012 remained constant at 3.4%.

Provision for Loan Losses. Management recorded a loan loss provision of \$775,000 for the nine months ended September 30, 2013, compared to \$1.3 million for the nine months ended September 30, 2012. The provision is primarily attributed to the reserves required for the one-to-four family segment as the economic conditions in the local market continue to negatively impact collateral values of real estate and the ability of borrowers to keep current per terms of their obligations. The slow payment activity and continued degradation of property values are the result of local economic conditions continuing to lag national indicators, including higher levels of unemployment locally of 11.3%, versus 9.2% for the State of Illinois and the national level of 7.3%. During the nine months ended September 30, 2013, the level of charge-off has declined by about \$1.5 million in comparison to the nine months ended September 30, 2012 due to a slight improvement in asset quality.

Management uses available information to establish the appropriate level of the allowance for loan losses. Future additions or reductions to the allowance may be necessary based on estimates that are susceptible to change as a result of changes in economic conditions and other factors. As a result, our allowance for loan losses may not be sufficient to cover actual loan losses, and future provisions for loan losses could materially adversely affect the Company's operating results. In addition, various regulatory agencies, as an integral part of their examination process, periodically review the Company's allowance for loan losses. Such agencies may require the Company to recognize adjustments to the allowance based on their judgments about information available to them at the time of their examination.

Other Income. The following table summarizes other income for the nine months ended September 30, 2013 and 2012.

Nine months ended			
September 30,			
2013	2012	\$	%
		change	change
(Dollars in thousands)			

Other income:

Gain on sale of securities	\$-	\$14	\$ (14)	(100.00)%
Gain on sale of loans	65	77	(12)	(15.58)
Gain on sale of OREO	-	97	(97)	(100.00)
Origination of mortgage servicing rights, net of amortization	8	(3)	11	366.67
Customer service fees	224	212	12	5.66
Income on bank owned life insurance	10	23	(13)	(56.52)
Other	174	52	122	234.62
Total other income	\$481	\$472	\$ 9	1.91 %

The increase in total other income was primarily a result of the receipt of a \$108,000 recovery of fraud losses on consumer loans, related to frauds which occurred during 2011 and 2012. The increase was partially offset by decreases in gains on the sales of OREO, securities, and loans. During the first nine months of 2013 the Company sold 19 of its OREO properties for a net loss of \$4,000 and during the first nine months of 2012 the Company sold ten of its OREO properties for a net gain of \$97,000. The decrease in gain on sale of securities is a result of there being no securities sold during 2013, while six securities were sold for a net gain of \$14,000 during 2012. The decrease in gain on sale of loans is a result of fewer loan originations and sales of loans during 2013 as compared to 2012.

Other Expenses. The following table summarizes other expenses for the nine months ended September 30, 2013 and 2012.

	Nine months ended			
	September 30,		\$ change	% change
	2013	2012		
Other expenses:				
Salaries and employee benefits	\$1,144	\$1,103	\$ 41	3.72 %
Directors fees	76	63	13	20.63
Occupancy	336	328	8	2.44
Deposit insurance premium	172	182	(10)	(5.49)
Legal and professional services	223	165	58	35.15
Data processing	219	242	(23)	(9.50)
Valuation adjustments and expenses on foreclosed real estate	247	107	140	130.84
Loss on sale of OREO	4	-	4	100.00
Loss on sale of repossessed assets	-	14	(14)	(100.00)
Loss on consumer loans	-	42	(42)	(100.00)
Other	429	378	51	13.49
Total other expenses	\$2,850	\$2,624	\$ 226	8.61 %
Efficiency ratio (1)	61.58%	54.82%		

(1) Computed as other expenses divided by the sum of net interest income and other income.

The increase in other expenses was primarily due to increases in valuation adjustments and expenses on foreclosed real estate and increased insurance expenses, both due to the number of OREO properties, increases in salaries and employee benefits, and an increase in legal and professional services due to compliance related activities. The increases were offset by decreases in deposit insurance premiums, decreases in data processing, the absence of losses on the sale of repossessed assets, and the absence of losses on consumer loans during the nine months ended September 30, 2013 as compared to the nine months ended September 30, 2012. The efficiency ratio increased due to higher costs for the period and lower revenues.

Income Taxes. The Company recorded income tax expense of \$367,000 for the nine months ended September 30, 2013 and income tax expense of \$258,000 for the nine months ended September 30, 2012.

LIQUIDITY AND CAPITAL RESOURCES

Liquidity. Liquidity management for the Bank is measured and monitored on both a short and long-term basis, allowing management to better understand and react to emerging balance sheet trends. After assessing actual and projected cash flow needs, management seeks to obtain funding at the most economical cost to the Bank. Our primary sources of funds are deposits, amortization, prepayments and maturities of outstanding loans and mortgage-backed and related securities, and other short-term investments, and funds provided from operations. While scheduled payments from amortization of loans and mortgage-backed related securities and maturing investment securities and short-term investments are relatively predictable sources of funds, deposit flows and loan prepayments are greatly influenced by general interest rates, economic conditions and competition. We invest excess funds in short-term interest-earning assets, including federal funds sold, which enable us to meet lending requirements or long-term investments when loan demand is low.

At September 30, 2013 the Bank had outstanding commitments to originate \$0.3 million in loans, unfunded lines of credit of \$8.5 million, a commitment to purchase \$5.5 million in auto loans, and \$1.2 million in commitments on construction loans. In addition, as of September 30, 2013, the total amount of certificates of deposit that were scheduled to mature in the next 12 months was \$45.5 million, as compared to \$54.7 million as of June 30, 2013 and \$62.0 million as of December 31, 2012. Based on prior experience, management believes that a majority of such deposits will remain with us, although there can be no assurance that this will be the case. In the event a significant portion of our deposits are not retained by us, we will have to utilize other funding sources, such as Federal Home Loan Bank of Chicago (“FHLBC”) advances, in order to maintain our level of assets. Alternatively, we could reduce our level of liquid assets, such as our cash and cash equivalents. As of September 30, 2013, the Bank had \$51.6 million of available credit from the FHLBC. There were no FHLBC advances outstanding at September 30, 2013. In addition, as of September 30, 2013, the Bank had \$5.0 million of available credit from Bankers Bank of Wisconsin to purchase Federal Funds.

The Company is a separate legal entity from the Bank and must provide for its own liquidity. In addition to its operating expenses, the Company is responsible for paying any dividends declared to its shareholders and for any repurchased shares of its common stock. Whether dividends are declared, and the timing and amount of any dividends declared, is subject to the discretion of our Board of Directors and depends on various factors, including our net earnings, financial condition, cash requirements, future prospects and other factors that our Board of Directors deems relevant to its analysis and decision making. The Company's primary source of income is dividends received from the Bank. The amount of dividends that the Bank may declare and pay to the Company in any calendar year, without the receipt of prior approval from the regulatory agencies but with prior notice to the regulatory agencies, cannot exceed net income for that year to date plus retained net income (as defined) for the preceding two calendar years. At September 30, 2013, the Company had cash and cash equivalents of \$238,000.

Capital. The Bank is required to maintain regulatory capital sufficient to meet Tier 1 leverage, Tier 1 risk-based and total risk-based capital ratios of at least 4.0%, 4.0% and 8.0%, respectively. The Bank exceeded each of its minimum capital requirements and was considered "well capitalized" within the meaning of federal regulatory requirements with ratios at September 30, 2013 of 11.01%, 18.08% and 19.35%, respectively, compared to ratios at December 31, 2012 of 10.30%, 16.92% and 18.19%, respectively.

OFF-BALANCE SHEET ARRANGEMENTS

For the nine months ended September 30, 2013, we did not engage in any off-balance sheet transactions reasonably likely to have a material effect on our financial condition, results of operations or cash flows.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

This Item is not applicable as the Company is a smaller reporting company.

ITEM 4. CONTROLS AND PROCEDURES

Controls and Procedures

As of the end of the period covered by this report, the Company carried out an evaluation under the supervision and with the participation of the Company's principal executive officer and principal financial officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures. Based on this evaluation, the Company's principal executive officer and principal financial officer concluded that the Company's disclosure controls and procedures were effective as of the end of the period covered by this report for the purpose of ensuring that the information required to be disclosed in the reports that the Company files or submits under the Securities Exchange Act of 1934, as amended, with the Securities and Exchange Commission (the "SEC") (1) is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and (2) is accumulated and communicated to the Company's management, including, its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure. It should be noted that the design of any system of controls is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions, regardless of how remote.

In addition, there have been no changes in the Company's internal control over financial reporting during the most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Part II – Other Information

ITEM 1 - LEGAL PROCEEDINGS

The Company is not involved in any pending legal proceedings other than routine legal proceedings occurring in the ordinary course of business that, in the aggregate, are believed by management to be material to the financial condition and results of operations of the Company.

ITEM 1A – RISK FACTORS

In addition to the other information set forth in this report, you should carefully consider the factors discussed in Part 1, “Item 1A. Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2012, which could materially affect our business, financial condition or future results. As of September 30, 2013, the risk factors of the Company have not changed materially from those reported in the Company’s Annual Report on Form 10-K. However, the risks described in our Annual Report on Form 10-K are not the only risks that we face. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition and/or operating results.

ITEM 2 - UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

Not applicable.

ITEM 3 - DEFAULTS UPON SENIOR SECURITIES

Not applicable.

ITEM 4 - MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5 - OTHER INFORMATION

Not applicable.

ITEM 6 - EXHIBITS

Exhibit
No. Description

- 3.1 Certificate of Incorporation of Ottawa Savings Bancorp, Inc. (incorporated by reference to Exhibit 3.1 to Company's Registration Statement on Form SB-2, No. 333-123455, filed on May 3, 2005, as amended)
- 3.2 Bylaws of Ottawa Savings Bancorp, Inc. (incorporated by reference to Exhibit 3.2 to Company's Registration Statement on Form SB-2, No. 333-123455, filed on May 3, 2005, as amended)
- 31.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2 Certifications of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 32.1 Certifications pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

101.0 The following materials from the Ottawa Savings Bancorp, Inc. Quarterly Report on form 10-Q for the quarter ended September 30, 2013 formatted in Extensible Business Reporting Language (XBRL): (i) the Condensed Consolidated Statements of Financial Condition, (ii) the Condensed Consolidated Statements of Operations, (iii) the Condensed Consolidated Statements of Cash Flows and (iv) related notes.

Signature

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.

OTTAWA SAVINGS BANCORP, INC.
Registrant

Date: November 13, 2013 /s/ Jon L. Kranov
Jon L. Kranov
President and Chief Executive Officer
(Principal Executive Officer)

Date: November 13, 2013 /s/ Marc N. Kingry
Marc N. Kingry
Chief Financial Officer
(Principal Financial Officer)