SI Financial Group, Inc.
Form 10-Q
November 06, 2015

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

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

For the Quarterly Period Ended September 30, 2015
OR

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

For the Transition Period from _______ to ______

Commission File Number: 0-54241

SI FINANCIAL GROUP, INC.
(Exact name of registrant as specified in its charter)

Maryland (State or other jurisdiction of incorporation or organization)	80-0643149 (I.R.S. Employer Identification No.)
803 Main Street, Willimantic, Connecticut (Address of principal executive offices)	06226 (Zip Code)

(860) 423-4581
(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 x No o

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 (Section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No o

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

Large Accelerated Filer o	Accelerated Filer x
Non-Accelerated Filer o	Smaller Reporting Company o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).
Yes o No x

As of November 2, 2015, there were 12,218,218 shares of the registrant's common stock outstanding.

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PART I. FINANCIAL INFORMATION
Item 1. Financial Statements.
SI FINANCIAL GROUP, INC.
CONSOLIDATED BALANCE SHEETS
(In Thousands, Except Share Amounts / Unaudited)

	September 30, 2015	December 31, 2014
ASSETS:		
Cash and due from banks:		
Noninterest-bearing	$14,011	$18,965
Interest-bearing	22,551	20,286
Total cash and cash equivalents	36,562	39,251
Available for sale securities, at fair value	176,177	173,040
Loans held for sale	165	747
Loans receivable (net of allowance for loan losses of $9,246 at September 30, 2015 and $7,797 at December 31, 2014)	1,142,998	1,044,864
Federal Home Loan Bank stock, at cost	12,421	10,333
Federal Reserve Bank stock, at cost	3,621	—
Bank-owned life insurance	21,755	21,306
Premises and equipment, net	21,669	21,711
Goodwill and other intangibles	18,246	18,697
Accrued interest receivable	4,230	3,853
Deferred tax asset, net	7,676	8,048
Other real estate owned, net	1,341	1,271
Other assets	6,785	7,412
Total assets	$1,453,646	$1,350,533
LIABILITIES AND SHAREHOLDERS' EQUITY:		
Liabilities:		
Deposits:		
Noninterest-bearing	$151,718	$146,062
Interest-bearing	891,412	864,651
Total deposits	1,043,130	1,010,713
Mortgagors' and investors' escrow accounts	1,946	3,600
Federal Home Loan Bank advances	224,459	148,277
Junior subordinated debt owed to unconsolidated trust	8,248	8,248
Accrued expenses and other liabilities	21,884	21,956
Total liabilities	1,299,667	1,192,794
Shareholders' Equity:		
Preferred stock ($.01 par value; 1,000,000 shares authorized; none issued)	—	—
Common stock ($.01 par value; 35,000,000 shares authorized; 12,224,153 and 12,776,426 shares issued and outstanding at September 30, 2015 and December 31, 2014, respectively)	122	128
Additional paid-in-capital	124,849	125,459
Unallocated common shares held by ESOP	(3,768)	(4,128)
Unearned restricted shares	(889)	(1,312)

Retained earnings	32,952	37,497
Accumulated other comprehensive income	713	95
Total shareholders' equity	153,979	157,739
Total liabilities and shareholders' equity	$1,453,646	$1,350,533

See accompanying notes to unaudited interim consolidated financial statements.

SI FINANCIAL GROUP, INC.
CONSOLIDATED STATEMENTS OF INCOME
(In Thousands, Except Per Share Amounts / Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
Interest and dividend income:				
Loans, including fees	$11,278	$10,735	$32,823	$32,489
Securities:				
Taxable interest	766	877	2,253	2,651
Tax-exempt interest	14	59	63	160
Dividends	140	46	281	143
Other	19	11	57	39
Total interest and dividend income	12,217	11,728	35,477	35,482
Interest expense:				
Deposits	1,403	1,355	4,150	4,033
Federal Home Loan Bank advances	846	602	2,124	1,921
Subordinated debt and other borrowings	84	84	251	251
Total interest expense	2,333	2,041	6,525	6,205
Net interest income	9,884	9,687	28,952	29,277
Provision for loan losses	1,017	350	1,712	1,195
Net interest income after provision for loan losses	8,867	9,337	27,240	28,082
Noninterest income:				
Service fees	1,699	1,762	5,039	5,265
Wealth management fees	303	293	916	926
Increase in cash surrender value of bank-owned life insurance	146	147	449	433
Net gain on sales of securities	14	—	146	64
Mortgage banking	139	81	416	396
Net gain (loss) on fair value of derivatives	(7)	78	(22)	69
Other	452	85	749	527
Total noninterest income	2,746	2,446	7,693	7,680
Noninterest expenses:				
Salaries and employee benefits	4,986	4,897	15,059	15,128
Occupancy and equipment	1,816	1,883	5,660	5,852
Computer and electronic banking services	1,413	1,417	4,168	4,082
Outside professional services	436	420	1,410	1,422
Marketing and advertising	259	216	779	754
Supplies	149	146	441	465
FDIC deposit insurance and regulatory assessments	255	303	748	953
Core deposit intangible amortization	150	150	451	463
Other real estate operations	160	72	444	303
Other	521	500	1,452	1,873
Total noninterest expenses	10,145	10,004	30,612	31,295

Income before income tax provision	1,468	1,779	4,321	4,467
Income tax provision	494	579	1,421	1,447
Net income	$974	$1,200	$2,900	$3,020
Earnings per share:				
Basic	$0.08	$0.10	$0.24	$0.25
Diluted	$0.08	$0.10	$0.24	$0.24

See accompanying notes to unaudited interim consolidated financial statements.

SI FINANCIAL GROUP, INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(In Thousands / Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
Net income	$974	$1,200	$2,900	$3,020
Other comprehensive income (loss), net of tax:				
Available for sale securities:				
Net unrealized holding gains (losses)	411	(382)	633	546
Reclassification adjustment for losses (gains) recognized in net income [(1)]	(9)	—	(96)	(42)
Net unrealized holding gains (losses) on available for sale securities	402	(382)	537	504
Net unrealized gain on interest-rate swap derivative	29	31	81	77
Other comprehensive income (loss)	431	(351)	618	581
Comprehensive income	$1,405	$849	$3,518	$3,601

[(1)] Amounts are included in net gain on sales of securities in noninterest income on the consolidated statements of income. Income tax expense (benefit) associated with the reclassification adjustment for the three and nine months ended September 30, 2015 was $5,000 and $50,000 and for the three and nine months ended September 30, 2014 was $0 and $22,000, respectively.

See accompanying notes to unaudited interim consolidated financial statements.

SI FINANCIAL GROUP, INC.
CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY
FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2015
(In Thousands, Except Share Data / Unaudited)

	Common Stock			Unallocated				
	Shares	Dollars	Additional Paid-in Capital	Common Shares Held by ESOP	Unearned Restricted Shares	Retained Earnings	Accumulated Other Comprehensive Income	Total Shareholders' Equity
Balance at December 31, 2014	12,776,426	$128	$125,459	$ (4,128)	$(1,312)	$37,497	$ 95	$ 157,739
Comprehensive income	—	—	—	—	—	2,900	618	3,518
Cash dividends declared ($0.12 per share)	—	—	—	—	—	(1,444)	—	(1,444)
Equity incentive plans compensation	—	—	230	—	453	—	—	683
Allocation of 36,477 ESOP shares	—	—	65	360	—	—	—	425
Restricted shares activity			30		(30)			—
Tax benefit from share-based compensation	—	—	5	—	—	—	—	5
Stock options exercised	297,546	3	3,268	—	—	—	—	3,271
Common shares repurchased	(849,819)	(9)	(4,208)	—	—	(6,001)	—	(10,218)
Balance at September 30, 2015	12,224,153	$122	$124,849	$ (3,768)	$(889)	$32,952	$ 713	$ 153,979

See accompanying notes to unaudited interim consolidated financial statements.

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SI FINANCIAL GROUP, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In Thousands / Unaudited)

	Nine Months Ended September 30,	
	2015	2014
Cash flows from operating activities:		
Net income	$2,900	$3,020
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	1,712	1,195
Employee stock ownership plan expense	425	416
Equity incentive plan expense	683	559
Excess tax benefit from share-based compensation	(5)	(4)
Amortization of investment premiums and discounts, net	851	724
Amortization of loan premiums and discounts, net	1,457	1,051
Depreciation and amortization of premises and equipment	2,036	1,921
Amortization of core deposit intangible	451	463
Amortization of deferred debt issue costs	16	79
Net gain on sales of securities	(146)	(64)
Net loss (gain) on fair value of derivatives	22	(69)
Deferred income tax provision	53	28
Loans originated for sale	(18,807)	(12,633)
Proceeds from sale of loans held for sale	19,524	13,353
Net gain on sales of loans held for sale	(234)	(201)
Net loss on sales or write-downs of other real estate owned	201	67
Increase in cash surrender value of bank-owned life insurance	(449)	(433)
Impairment charge on long-lived assets	—	175
Change in operating assets and liabilities:		
Accrued interest receivable	(377)	123
Other assets	727	1,947
Accrued expenses and other liabilities	33	1,143
Net cash provided by operating activities	11,073	12,860
Cash flows from investing activities:		
Purchases of available for sale securities	(35,450)	(24,626)
Proceeds from sales of available for sale securities	9,703	1,109
Proceeds from maturities of and principal repayments on available for sale securities	22,719	23,063
Purchases of Federal Home Loan Bank stock	(2,088)	—
Purchases of Federal Reserve Bank stock	(3,621)	—
Redemption of Federal Home Loan Bank stock	—	2,776
Loan principal collections, net of originations	(4,996)	42,628
Purchases of loans	(96,640)	(38,643)
Proceeds from sales of other real estate owned	62	1,109
Purchases of premises and equipment	(1,994)	(2,134)
Net cash provided by (used in) investing activities	(112,305)	5,282

SI FINANCIAL GROUP, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS (Concluded)
(In Thousands / Unaudited)

	Nine Months Ended September 30, 2015	2014
Cash flows from financing activities:		
Net increase in deposits	32,417	13,090
Net decrease in mortgagors' and investors' escrow accounts	(1,654)	(1,420)
Proceeds from Federal Home Loan Bank advances	120,478	10,000
Repayments of Federal Home Loan Bank advances	(44,312)	(32,203)
Excess tax benefit from share-based compensation	5	4
Cash dividends on common stock	(1,444)	(1,107)
Stock options exercised	708	552
Common shares repurchased	(7,655)	(761)
Net cash provided by (used in) financing activities	98,543	(11,845)
Net change in cash and cash equivalents	(2,689)	6,297
Cash and cash equivalents at beginning of period	39,251	27,321
Cash and cash equivalents at end of period	$36,562	$33,618
Supplemental cash flow information:		
Interest paid	$6,490	$6,234
Income taxes received (paid), net	989	(555)
Transfer of loans to other real estate owned	333	108
Stock options exercised by net-share settlement	2,563	190

See accompanying notes to unaudited interim consolidated financial statements.

SI FINANCIAL GROUP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
SEPTEMBER 30, 2015 AND 2014 AND DECEMBER 31, 2014

NOTE 1. NATURE OF BUSINESS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Business

SI Financial Group, Inc. (the “Company”) is the holding company for Savings Institute Bank and Trust Company (the “Bank”). Established in 1842, the Bank is a community-oriented financial institution headquartered in Willimantic, Connecticut. The Bank provides a variety of financial services to individuals, businesses and municipalities through its twenty-six offices in eastern Connecticut and Rhode Island. Its primary products include savings, checking and certificate of deposit accounts, residential and commercial mortgage loans, commercial business loans and consumer loans. In addition, wealth management services, which include trust, financial planning, life insurance and investment services, are offered to individuals and businesses through the Bank’s offices. The Company does not conduct any material business other than owning all of the stock of the Bank and making payments on the subordinated debentures held by the Company.

Principles of Consolidation

The accompanying consolidated financial statements include the accounts of the Company, its wholly-owned subsidiary, the Bank, and the Bank’s wholly-owned subsidiaries, SI Mortgage Company and SI Realty Company, Inc. All significant intercompany accounts and transactions have been eliminated.

Basis of Financial Statement Presentation

The interim consolidated financial statements and related notes have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) for interim financial information, with the instructions to Form 10-Q and Rule 10.01 of Regulation S-X of the Securities and Exchange Commission ("SEC") and general practices within the banking industry. Accordingly, certain information and footnote disclosures required by GAAP for complete financial statements have been omitted. Information in the accompanying interim consolidated financial statements and notes to the financial statements of the Company as of September 30, 2015 and for the three and nine months ended September 30, 2015 and 2014 is unaudited. These unaudited interim consolidated financial statements and related notes should be read in conjunction with the audited financial statements of the Company and the accompanying notes for the year ended December 31, 2014 contained in the Company’s Form 10-K.

In the opinion of management, the accompanying unaudited interim consolidated financial statements reflect all of the adjustments, consisting only of normal and recurring adjustments, necessary for a fair presentation of the financial condition, results of operations and cash flows as of and for the periods covered herein. The results of operations for the three and nine months ended September 30, 2015 are not necessarily indicative of the operating results for the year ending December 31, 2015 or for any other period.

In preparing the consolidated financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosures of contingent assets and liabilities, as of the date of the balance sheets and reported amounts of revenues and expenses for the periods presented. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses, deferred income taxes and the impairment of long-lived assets.

Reclassifications

Amounts in the Company’s prior year consolidated financial statements are reclassified to conform to the current year presentation. Such reclassifications have no effect on net income.

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Loans Receivable
Loans receivable are stated at current unpaid principal balances, net of the allowance for loan losses and deferred loan origination fees and costs. Management has the ability and intent to hold its loans receivable for the foreseeable future or until maturity or pay-off.

A loan is impaired when, based on current information and events, it is probable the Company will be unable to collect all contractual principal and interest payments due in accordance with the 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. Impairment is measured on a loan by loan basis for residential and commercial mortgage loans and commercial business loans by either the present value of expected future cash flows discounted at the loan's effective interest rate or, as a practical expedient, at the loan's observable market price or the fair value of the collateral if the loan is collateral dependent. Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. Accordingly, the Company does not typically identify individual consumer loans for impairment disclosures, unless such loans are subject to a troubled debt restructuring ("TDR") agreement.

Troubled Debt Restructurings
The Company periodically may agree to modify the contractual terms of loans. When a loan is modified and concessions have been made by the Company to the original contractual terms that would not otherwise be considered for a borrower with similar risk characteristics, such as below market interest rate reductions, deferral of interest or principal payments, or maturity extensions due to the borrower’s financial condition, the modification is considered a TDR. Modified terms are dependent upon the financial position and needs of the individual borrower. If the modification agreement is violated, the loan is handled by the Company’s Collections Department for resolution which may result in foreclosure.

Management considers all nonaccrual loans, with the exception of certain consumer loans, to be impaired. Also, all TDRs are initially classified as impaired and follow the Company's nonaccrual policy. If the loan was current prior to modification, nonaccrual status would not be required. If the loan was on nonaccrual prior to modification or if the payment amount significantly increases, the loan will remain on nonaccrual for a period of at least six months. Loans qualify for return to accrual status once the borrower has demonstrated the willingness and the ability to perform in accordance with the restructured terms of the loan agreement for a period of not less than six consecutive months. In most cases, loan payments less than 90 days past due are considered minor collection delays and the related loans are generally not considered impaired.

Impaired classification may be removed after a year following the restructure if the borrower demonstrates compliance with the modified terms and the restructuring agreement specifies an interest rate equal to that which would be provided to a borrower with similar risk characteristics at the time of restructuring.

Allowance for Loan Losses
The allowance for loan losses, a material estimate which could change significantly in the near-term, is established through a provision for loan losses charged to earnings to account for losses that are inherent in the loan portfolio and estimated to occur, and is maintained at a level that management considers adequate to absorb losses in the loan portfolio. Loan losses are charged against the allowance for loan losses when management believes the

uncollectibility of the principal loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance for loan losses when received. In the determination of the allowance for loan losses, management may obtain independent appraisals for significant properties, if necessary.

Management's judgment in determining the adequacy of the allowance is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available. The allowance for loan losses is evaluated on a monthly basis by management and is based on the evaluation of the known and inherent risk characteristics and size and composition of the loan portfolio, the assessment of current economic and real estate market conditions, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral, historical loan loss experience, the level and trends of nonperforming loans, delinquencies, classified assets and loan charge-offs and evaluations of loans and other relevant factors.

The allowance for loan losses consists of the following key elements:

- Specific allowance for identified impaired loans. For loans identified as impaired, an allowance is established when the present value of expected cash flows (or observable market price of the loan or fair value of the collateral if the loan is collateral dependent) of the impaired loan is lower than the carrying value of that loan.

- General valuation allowance. The general component represents a valuation allowance on the remainder of the loan portfolio, after excluding impaired loans. For this portion of the allowance, loans are segregated by category and assigned an allowance percentage based on historical loan loss experience adjusted for qualitative factors stratified by the following loan segments: residential one- to four-family, multi-family and commercial real estate, construction, commercial business and consumer. Management uses a rolling average of historical losses based on the time frame appropriate to capture relevant loss data for each loan segment. This historical loss factor is adjusted for the following qualitative factors: changes in lending policies and procedures, including changes in underwriting standards and collection, charge-off and recovery practices; changes in international, national, regional and local economic and business conditions and developments that affect the collectibility of the portfolio, including the condition of various market segments; changes in the size and composition of the loan portfolio and in the terms of the loans; changes in the experience, ability, and depth of lending management and other relevant staff; changes in the volume and severity of past due loans, the volume of nonaccrual loans and the volume and severity of adversely classified or graded loans; changes in the quality of the loan review system; changes in the underlying collateral for collateral-dependent loans; the existence and effect of any concentrations of credit and changes in the level of such concentrations; the effect of other external factors such as competition and legal and regulatory capital requirements on the level of estimated credit losses in the portfolio.

The qualitative factors are determined based on the following various risk characteristics for each loan segment. Risk characteristics relevant to each portfolio segment are as follows:

- Residential – One- to Four-Family – The Bank primarily originates conventional loans with loan-to-value ratios less than 95% and generally originates loans with loan-to-value ratios in excess of 80% only when secured by first liens on owner-occupied one- to four-family residences. Loans with loan-to-value ratios in excess of 80% generally require private mortgage insurance or additional collateral. All loans in this segment are collateralized by owner-occupied residential real estate and repayment is dependent on the credit quality of the individual borrower. The overall health of the economy, including unemployment rates and housing prices, will have an effect on the credit quality of this segment.

- Multi-family and Commercial – Loans in this segment are originated for the purpose of acquiring, developing, improving or refinancing multi-family and commercial real estate where the property is the primary collateral securing the loan, and the income generated from the property is the primary repayment source. The underlying cash flows generated by the properties can be adversely impacted by the economy as evidenced by increased vacancy rates.

Payments on loans secured by income-producing properties often depend on the successful operation and management of the properties. Management continually monitors the cash flows of these loans.

- Construction – This segment includes loans to individuals and, to a lesser extent, builders to finance the construction of residential dwellings. The Bank also originates construction loans for commercial development projects. Upon the completion of construction, the loan generally converts to a permanent mortgage loan. Credit risk is affected by cost overruns, correct estimates of the sale price of the property, time to sell at an adequate price and market conditions.

- Commercial Business – Loans in this segment are made to businesses and are generally secured by assets of the business. Repayment is expected from the cash flows of the business. A weakened economy and reduced viability of the industry in which the customer operates will have a negative impact on the credit quality in this segment. The Bank also provides loans to investors in the time share industry, which are secured by consumer receivables, and provides loans for capital improvements to condominium associations, which are secured by the assigned rights to levy special assessments to condominium owners.

- Consumer – Loans in this segment primarily include home equity lines of credit (representing both first and second liens), indirect automobile loans and, to a lesser extent, loans secured by marketable securities, passbook or certificate accounts, motorcycles, automobiles and recreational vehicles, as well as unsecured loans. Consumer loan collections depend on the borrower’s continuing financial stability and, therefore, are more likely to be adversely affected by job loss, divorce, illness or personal bankruptcy.

In computing the allowance for loan losses, we do not assign a general valuation allowance to the Small Business Administration (“SBA”) and United States Department of Agriculture (“USDA”) loans that we purchase as such loans are fully guaranteed. These loans are included in commercial business loans. See Note 4 for details.

The majority of the Company's loans are collateralized by real estate located in eastern Connecticut and Rhode Island. To a lesser extent, certain commercial real estate loans are secured by collateral located outside of our primary market area. Accordingly, the collateral value of a substantial portion of the Company's loan portfolio and real estate acquired through foreclosure is susceptible to changes in local market conditions.

Although management believes it uses the best information available to establish the allowance for loan losses, future adjustments to the allowance for loan losses may be necessary and the Company’s results of operations could be adversely affected if circumstances differ substantially from the assumptions used in making the determinations. Furthermore, while management believes it has established the allowance for loan losses in conformity with GAAP, our regulators, in reviewing the loan portfolio, may request us to increase our allowance for loan losses based on judgments different from ours. In addition, because future events affecting borrowers and collateral cannot be predicted with certainty, the existing allowance for loan losses may not be adequate or increases may be necessary should the quality of any loans deteriorate as a result of the factors discussed above. Any material increase in the allowance for loan losses would adversely affect the Company’s financial condition and results of operations.

Interest and Fees on Loans
Interest on loans is accrued and included in net interest income based on contractual rates applied to principal amounts outstanding. Accrual of interest is discontinued when loan payments are 90 days or more past due, based on contractual terms, or when, in the judgment of management, collectibility of the loan or loan interest becomes uncertain. Subsequent recognition of income occurs only to the extent payment is received subject to management's assessment of the collectibility of the remaining interest and principal. A nonaccrual loan is restored to accrual status

when it is no longer delinquent and collectibility of interest and principal is no longer in doubt and the borrower has made regular payments in accordance with the terms of the loan over a period of at least six months. Interest collected on nonaccrual loans is recognized only to the extent cash payments are received, and may be recorded as a reduction to principal if the collectibility of the principal balance of the loan is unlikely.

Loan origination fees, direct loan origination costs and loan purchase premiums are deferred, and the net amount is recognized as an adjustment of the related loan's yield utilizing the interest method over the contractual life of the loan. In addition, discounts related to fair value adjustments for loans receivable acquired in a business combination or asset purchase are accreted into earnings over the contractual term as an adjustment of the loan's yield. The Company periodically evaluates the cash flows expected to be collected for loans acquired with deteriorated credit quality. Changes in the expected cash flows compared to the expected cash flows as of the date of acquisition may impact the accretable yield or result in a charge to the provision for loan losses to the extent of a shortfall.

Common Share Repurchases

The Company is chartered in the state of Maryland. Maryland law does not provide for treasury shares, rather shares repurchased by the Company constitute authorized but unissued shares. GAAP states that accounting for treasury stock shall conform to state law. Therefore, the cost of shares repurchased by the Company has been allocated to common stock, additional paid-in capital and retained earnings balances.

Recent Accounting Pronouncements

Receivables - Troubled Debt Restructurings by Creditors (Subtopic 310-40): Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure. In January 2014, the Financial Accounting Standards Board ("FASB") issued amended guidance that clarifies when a creditor should be considered to have received physical possession of residential real estate property collateralizing a consumer mortgage loan such that the loan receivable should be derecognized and the real estate property recognized. The amended guidance clarifies that an in substance repossession or foreclosure occurs, and a creditor is considered to have received physical possession of residential real estate property collateralizing a consumer mortgage loan, upon either (1) the creditor obtaining legal title to the residential real estate property upon completion of a foreclosure or (2) the borrower conveying all interest in the residential real estate property to the creditor to satisfy that loan through completion of a deed in lieu of foreclosure or through a similar legal agreement. In addition, the amended guidance requires interim and annual disclosures of both (1) the amount of foreclosed residential real estate property held by the creditor and (2) the recorded investment in consumer mortgage loans collateralized by residential real estate property that are in the process of foreclosure according to local requirements of the applicable jurisdiction. The adoption of the amended guidance on January 1, 2015 did not have a material impact on the Company’s consolidated financial statements.

Receivables - Troubled Debt Restructurings by Creditors (Subtopic 310-40): Classification of Certain Government-Guaranteed Mortgage Loans upon Foreclosure - In August 2014, the FASB issued amended guidance that addresses the diversity in practice regarding the classification and measurement of foreclosed loans which were part of a government-sponsored loan guarantee program (e.g. HUD, FHA, VA). The amended guidance outlines certain criteria that, if met, the loan (residential or commercial) should be derecognized and a separate other receivable should be recorded upon foreclosure at the amount of the loan balance (principal and interest) expected to be recovered from the guarantor. The adoption of the amended guidance on January 1, 2015 did not have a material impact on the Company’s consolidated financial statements.

Interest - Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs - In April 2015, the FASB issued guidance simplifying the presentation of debt issuance costs. The amended guidance requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The amended guidance should be applied on a retrospective basis and is effective for fiscal years, and interim periods within those years, beginning after December 15, 2015, with early adoption permitted. The adoption of the amended guidance is not expected to have a material impact on the Company's consolidated financial statements.

Interest - Imputation of Interest (Subtopic 835-30): Presentation and Subsequent Measurement of Debt Issuance Costs Associated with Line-of-Credit Arrangements - In August 2015, the FASB issued amended guidance pursuant to the SEC Staff Announcement at the June 18, 2015 Emerging Issues Task Force meeting that the update issued in April 2015 does not address presentation or subsequent measurement of debt issuance costs related to line-of-credit arrangements. Given the absence of authoritative guidance within the previous update for debt issuance costs related to line-of-credit-arrangements, the SEC staff would not object to an entity deferring and presenting debt issuance costs as an asset and subsequently amortizing the deferred debt issuance costs ratably over the term of the line-of-credit arrangement, regardless of whether there were any outstanding borrowings on the line-of-credit arrangement. The Company does not expect the adoption of this guidance to have a material impact on its consolidated financial statements.

NOTE 2. EARNINGS PER SHARE

Basic earnings per share is calculated by dividing the net income available to common shareholders by the weighted average number of common shares outstanding during the period. Unvested restricted shares are considered outstanding in the computation of basic earnings per share since the shares participate in dividends and the rights to the dividends are non-forfeitable. Diluted earnings per share is computed in a manner similar to basic earnings per share except that the weighted average number of common shares outstanding is increased to include the incremental common shares (as computed using the treasury stock method) that would have been outstanding if all potentially dilutive common stock equivalents were issued during the period. The Company's common stock equivalents relate solely to stock options. Repurchased common shares and unallocated common shares held by the Bank's ESOP are not deemed outstanding for earnings per share calculations.

Anti-dilutive shares are common stock equivalents with weighted average exercise prices in excess of the weighted average market value for the periods presented, and are not considered in diluted earnings per share calculations. The Company had anti-dilutive common shares outstanding of 321,793 and 342,819 for the three and nine months ended September 30, 2015, respectively, and 677,590 and 485,459 for the three and nine months ended September 30, 2014, respectively.

The computation of earnings per share is as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
	(Dollars in Thousands, Except Per Share Amounts)			
Net income	$974	$1,200	$2,900	$3,020
Weighted average common shares outstanding:				
Basic	11,793,218	12,310,368	12,036,573	12,315,829
Effect of dilutive stock options	21,713	23,065	28,485	38,382
Diluted	11,814,931	12,333,433	12,065,058	12,354,211
Earnings per share:				

Basic	$0.08	$0.10	$0.24	$0.25
Diluted	$0.08	$0.10	$0.24	$0.24

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NOTE 3. SECURITIES

Available for Sale Securities

The amortized cost, gross unrealized gains and losses and fair values of available for sale securities at September 30, 2015 and December 31, 2014 are as follows:

	September 30, 2015			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(In Thousands)			
Debt securities:				
U.S. Government and agency obligations	$68,172	$620	$(224)	$68,568
Government-sponsored enterprises	30,329	335	—	30,664
Mortgage-backed securities:[1]				
Agency - residential	69,527	872	(519)	69,880
Non-agency - residential	161	—	(5)	156
Corporate debt securities	1,000	—	—	1,000
Collateralized debt obligation	1,155	—	(25)	1,130
Obligations of state and political subdivisions	1,535	2	—	1,537
Tax-exempt securities	3,183	59	—	3,242
Total available for sale securities	$175,062	$1,888	$(773)	$176,177

[1] Agency securities refer to debt obligations issued or guaranteed by government corporations or government-sponsored enterprises (“GSEs”). Non-agency securities, or private-label securities, are the sole obligation of their issuer and are not guaranteed by any of the GSEs or the U.S. Government.

	December 31, 2014			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(In Thousands)			
Debt securities:				
U.S. Government and agency obligations	$66,232	$385	$(226)	$66,391
Government-sponsored enterprises	27,435	120	(67)	27,488
Mortgage-backed securities:[1]				
Agency - residential	67,008	907	(1,065)	66,850
Non-agency - residential	254	3	(4)	253
Corporate debt securities	1,000	—	—	1,000
Collateralized debt obligation	1,188	—	(7)	1,181
Obligations of state and political subdivisions	3,039	167	(6)	3,200
Tax-exempt securities	6,583	97	(3)	6,677
Total available for sale securities	$172,739	$1,679	$(1,378)	$173,040

[1] Agency securities refer to debt obligations issued or guaranteed by government corporations or GSEs. Non-agency securities, or private-label securities, are the sole obligation of their issuer and are not guaranteed by any of the GSEs or the U.S. Government.

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The amortized cost and fair value of debt securities by contractual maturities at September 30, 2015 are presented below. Maturities are based on the final contractual payment dates and do not reflect the impact of potential prepayments or early redemptions. Because mortgage-backed securities ("MBS") are not due at a single maturity date, they are not included in the maturity categories in the following maturity summary.

	Amortized Cost	Fair Value
	(In Thousands)	
Within 1 year	$2,536	$2,539
After 1 but within 5 years	52,956	53,554
After 5 but within 10 years	12,250	12,216
After 10 years	37,632	37,832
	105,374	106,141
Mortgage-backed securities	69,688	70,036
Total debt securities	$175,062	$176,177

The following is a summary of realized gains and losses on the sales/calls of securities for the three and nine months ended September 30, 2015 and 2014:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
	(In Thousands)			
Gross gains on sales/calls	$14	$—	$169	$64
Gross losses on sales/calls	—	—	(23)	—
Net gain on sales/calls of securities	$14	$—	$146	$64

There were no sales of available for sale securities for the three months ended September 30, 2015 and 2014. Proceeds from the sale of available for sale securities were $9.7 million and $1.1 million for the nine months ended September 30, 2015 and 2014, respectively.

The following tables present information pertaining to securities with gross unrealized losses at September 30, 2015 and December 31, 2014, aggregated by investment category and length of time the individual securities have been in a continuous unrealized loss position.

September 30, 2015	Less Than 12 Months		12 Months Or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	(In Thousands)					
U.S. Government and agency obligations	$3,880	$15	$15,703	$209	$19,583	$224
Mortgage-backed securities:						
Agency - residential	4,731	19	28,634	500	33,365	519
Non-agency - residential	—	—	115	5	115	5

Collateralized debt obligation	—	—	1,130	25	1,130	25
Total	$8,611	$34	$45,582	$739	$54,193	$773

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December 31, 2014	Less Than 12 Months		12 Months Or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	(In Thousands)					
U.S. Government and agency obligations	$9,273	$15	$16,655	$211	$25,928	$226
Government-sponsored enterprises	6,974	4	3,973	63	10,947	67
Mortgage-backed securities:						
Agency - residential	4,251	122	32,127	943	36,378	1,065
Non-agency - residential	—	—	127	4	127	4
Collateralized debt obligation	1,181	7	—	—	1,181	7
Obligations of state and political subdivisions	—	—	668	6	668	6
Tax-exempt securities	1,141	3	—	—	1,141	3
Total	$22,820	$151	$53,550	$1,227	$76,370	$1,378

At September 30, 2015, twenty-three debt securities with gross unrealized losses had aggregate depreciation of approximately 1.41% of the Company’s amortized cost basis. The majority of the unrealized losses are related to the Company’s agency MBS. There were no investments deemed other-than-temporarily impaired for the three and nine months ended September 30, 2015 and 2014. The following summarizes, by security type, the basis for management’s determination during the preparation of the financial statements that the applicable investments within the Company’s securities portfolio were not other-than-temporarily impaired at September 30, 2015.

U.S. Government and Agency Obligations. The unrealized losses on the Company’s U.S. Government and agency obligations related primarily to a widening of the rate spread to comparable treasury securities. Because the decline in market value was attributable to changes in interest rates and not credit quality, and because the Company does not intend to sell these securities and it is not more likely than not that the Company will be required to sell the securities before their anticipated recovery, which may be at maturity, the Company did not consider these securities to be other-than-temporarily impaired at September 30, 2015.

Mortgage-backed Securities - Agency - Residential. The unrealized losses on the Company’s agency–residential mortgage-backed securities were caused by increases in the rate spread to comparable treasury securities. The Company does not expect these securities to settle at a price less than the amortized cost basis of the investments. Because the Company does not intend to sell the investments and it is not more likely than not the Company will be required to sell the investments before the recovery of their amortized cost basis, which may be at maturity, the Company did not consider these investments to be other-than-temporarily impaired at September 30, 2015.

Mortgage-backed Securities - Non-agency - Residential. The unrealized losses on the Company's non-agency - residential mortgage-backed securities relate to one investment which has been evaluated by management and no potential credit losses were identified. Because the Company does not intend to sell this security and it is not more likely than not that the Company will be required to sell this security before the recovery of its amortized cost basis, which may be maturity, the Company did not consider this investment to be other-than-temporarily impaired at September 30, 2015.

Collateralized Debt Obligations. The unrealized losses on the Company's collateralized debt obligations relate to one investment in a pooled trust preferred security ("PTPS"). The PTPS market has stabilized at depressed market values as a result of market saturation. The Company's PTPS was upgraded to investment grade and based on its senior credit profile, management does not believe this investment will suffer from any further credit-related losses. Because the Company does not intend to sell the investment and it is not more likely than not the

Company will be required to sell the investment before recovery of its amortized cost basis, which may be at maturity, the Company did not record impairment losses as of September 30, 2015.

NOTE 4. LOANS RECEIVABLE AND ALLOWANCE FOR LOAN LOSSES

Loan Portfolio

The composition of the Company's loan portfolio at September 30, 2015 and December 31, 2014 is as follows:

	September 30, 2015	December 31, 2014
	(In Thousands)	
Real estate loans:		
Residential - 1 to 4 family	$430,287	$430,575
Multi-family and commercial	339,682	298,320
Construction	17,409	13,579
Total real estate loans	787,378	742,474
Commercial business loans:		
SBA and USDA guaranteed	153,811	118,466
Time share	57,760	45,669
Condominium association	26,237	21,386
Other	68,307	66,446
Total commercial business loans	306,115	251,967
Consumer loans:		
Home equity	52,985	51,093
Indirect automobile	2,239	3,692
Other	1,915	1,864
Total consumer loans	57,139	56,649
Total loans	1,150,632	1,051,090
Deferred loan origination costs, net of fees	1,612	1,571
Allowance for loan losses	(9,246)	(7,797)
Loans receivable, net	$1,142,998	$1,044,864

The Company purchased commercial business loans totaling $96.6 million during the nine months ended September 30, 2015.

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Allowance for Loan Losses

Changes in the allowance for loan losses for the three and nine months ended September 30, 2015 and 2014 are as follows:

Three Months Ended September 30, 2015	Residential - 1 to 4 Family	Multi-family and Commercial	Construction	Commercial Business	Consumer	Total
	(In Thousands)					
Balance at beginning of period	$986	$3,766	$434	$2,618	$633	$8,437
Provision (credit) for loan losses	30	666	(7)	322	6	1,017
Loans charged-off	—	(136)	—	(140)	—	(276)
Recoveries of loans previously charged-off	41	22	—	5	—	68
Balance at end of period	$1,057	$4,318	$427	$2,805	$639	$9,246

Nine Months Ended September 30, 2015	Residential - 1 to 4 Family	Multi-family and Commercial	Construction	Commercial Business	Consumer	Total
	(In Thousands)					
Balance at beginning of period	$955	$3,607	$254	$2,382	$599	$7,797
Provision for loan losses	74	843	173	582	40	1,712
Loans charged-off	(46)	(156)	—	(165)	—	(367)
Recoveries of loans previously charged-off	74	24	—	6	—	104
Balance at end of period	$1,057	$4,318	$427	$2,805	$639	$9,246

Three Months Ended September 30, 2014	Residential - 1 to 4 Family	Multi-family and Commercial	Construction	Commercial Business	Consumer	Total
	(In Thousands)					
Balance at beginning of period	$984	$3,465	$221	$2,208	$567	$7,445
Provision for loan losses	123	135	26	21	45	350
Loans charged-off	(137)	(1)	—	—	(42)	(180)
Recoveries of loans previously charged-off	—	—	—	1	3	4
Balance at end of period	$970	$3,599	$247	$2,230	$573	$7,619

Nine Months Ended September 30, 2014	Residential - 1 to 4 Family	Multi-family and Commercial	Construction	Commercial Business	Consumer	Total

	(In Thousands)					
Balance at beginning of period	$975	$3,395	$169	$1,875	$502	$6,916
Provision for loan losses	281	347	78	364	125	1,195
Loans charged-off	(317)	(144)	—	(13)	(75)	(549)
Recoveries of loans previously charged-off	31	1	—	4	21	57
Balance at end of period	$970	$3,599	$247	$2,230	$573	$7,619

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Further information pertaining to the allowance for loan losses at September 30, 2015 and December 31, 2014 is as follows:

September 30, 2015	Residential - 1 to 4 Family	Multi-family and Commercial	Construction	Commercial Business	Consumer	Total
	(In Thousands)					
Allowance for loans individually evaluated and deemed to be impaired	$310	$40	$—	$—	$—	$350
Allowance for loans individually or collectively evaluated and not deemed to be impaired	747	4,278	427	2,805	639	8,896
Allowance for loans acquired with deteriorated credit quality	—	—	—	—	—	—
Total loan loss allowance	$1,057	$4,318	$427	$2,805	$639	$9,246
Loans individually evaluated and deemed to be impaired	$5,893	$3,765	$—	$485	$77	$10,220
Loans individually or collectively evaluated and not deemed to be impaired	424,394	332,193	17,409	304,876	57,062	1,135,934
Amount of loans acquired with deteriorated credit quality	—	3,724	—	754	—	4,478
Total loans	$430,287	$339,682	$17,409	$306,115	$57,139	$1,150,632

December 31, 2014	Residential - 1 to 4 Family	Multi-family and Commercial	Construction	Commercial Business	Consumer	Total
	(In Thousands)					
Allowance for loans individually evaluated and deemed to be impaired	$287	$52	$—	$20	$—	$359
Allowance for loans individually or collectively evaluated and not deemed to be impaired	668	3,555	254	2,362	599	7,438
Allowance for loans acquired with deteriorated credit quality	—	—	—	—	—	—
Total loan loss allowance	$955	$3,607	$254	$2,382	$599	$7,797

Loans individually evaluated and deemed to be impaired	$5,318	$1,872	$—	$470	$—	$7,660
Loans individually or collectively evaluated and not deemed to be impaired	424,885	292,215	13,579	251,140	56,649	1,038,468
Amount of loans acquired with deteriorated credit quality	372	4,233	—	357	—	4,962
Total loans	$430,575	$298,320	$13,579	$251,967	$56,649	$1,051,090

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Past Due Loans

The following represents an aging of loans at September 30, 2015 and December 31, 2014:

September 30, 2015	30-59 Days Past Due	60-89 Days Past Due	90 Days or More Past Due	Total 30 Days or More Past Due	Current	Total Loans
	(In Thousands)					
Real Estate:						
Residential - 1 to 4 family	$14	$1,050	$926	$1,990	$428,297	$430,287
Multi-family and commercial	3,310	657	2,060	6,027	333,655	339,682
Construction	—	—	—	—	17,409	17,409
Commercial Business:						
SBA and USDA guaranteed	—	—	—	—	153,811	153,811
Time share	—	—	—	—	57,760	57,760
Condominium association	—	—	—	—	26,237	26,237
Other	—	155	815	970	67,337	68,307
Consumer:						
Home equity	—	—	270	270	52,715	52,985
Indirect automobile	26	3	7	36	2,203	2,239
Other	—	1	—	1	1,914	1,915
Total	$3,350	$1,866	$4,078	$9,294	$1,141,338	$1,150,632

December 31, 2014	30-59 Days Past Due	60-89 Days Past Due	90 Days or More Past Due	Total 30 Days or More Past Due	Current	Total Loans	Past Due 90 Days or More and Accruing
	(In Thousands)						
Real Estate:							
Residential - 1 to 4 family	$4,194	$258	$1,602	$6,054	$424,521	$430,575	$—
Multi-family and commercial	768	794	775	2,337	295,983	298,320	—
Construction	—	—	—	—	13,579	13,579	—
Commercial Business:							
SBA and USDA guaranteed	1,536	—	459	1,995	116,471	118,466	459
Time share	—	—	—	—	45,669	45,669	—
Condominium association	—	—	—	—	21,386	21,386	—
Other	50	—	446	496	65,950	66,446	—
Consumer:							
Home equity	20	158	23	201	50,892	51,093	—
Indirect automobile	103	10	—	113	3,579	3,692	—
Other	—	—	—	—	1,864	1,864	—
Total	$6,671	$1,220	$3,305	$11,196	$1,039,894	$1,051,090	$459

The Company did not have any loans that were past due 90 days or more and still accruing interest at September 30, 2015.

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Impaired and Nonaccrual Loans

The following is a summary of impaired loans and nonaccrual loans at September 30, 2015 and December 31, 2014:

	Impaired Loans[1]			
September 30, 2015	Recorded Investment	Unpaid Principal Balance	Related Allowance	Nonaccrual Loans