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Waterstone Financial, Inc.
Form 10-K
March 03, 2017
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

F O R M 1 0 - K

[X] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2016

Commission file number: 001-36271

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

Maryland 90-1026709
(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

11200 W Plank Ct, Wauwatosa, Wisconsin 53226
(Address of principal executive offices) (Zip Code)

(414) 761-1000
Registrant's telephone number, including area code:

Securities registered pursuant to Section 12(b) of the Act:

Common Stock, \$0.01 Par Value The NASDAQ Stock Market, LLC
(Title of class) (Name of each exchange on which registered)

Securities registered pursuant to Section 12(g) of the Act:
NONE

Indicate by check mark whether the registrant is a well-known seasoned issuer (as defined in Rule 405 of the 1933 Act).

Yes No T

Indicate by check mark whether the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the 1934 Act.

Yes No T

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 T No

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Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files)

Yes T No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. []

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

| | | | |
|-------------------------|-------------------|---|---------------------------|
| | | Non-accelerated filer | |
| Large accelerated filer | Accelerated filer | (Do not check if a smaller reporting company) | Smaller Reporting Company |

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

Yes No T

The aggregate market value of the voting and non-voting common equity held by non-affiliates of the Registrant, computed by reference to the price at which the common equity was last sold on June 30, 2016 as reported by the NASDAQ Global Select Market® was approximately \$447.1 million.

As of February 28, 2017, 29,446,462 shares of the Registrant's Common Stock were issued and outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

| | |
|--|---------------------------------------|
| | Part of Form 10-K Into Which |
| Document | Portions of Document are Incorporated |
| Proxy Statement for Annual Meeting of Shareholders on May 16, 2017 | Part III |

WATERSTONE FINANCIAL, INC.

FORM 10-K ANNUAL REPORT TO THE SECURITIES AND EXCHANGE COMMISSION
FOR THE YEAR ENDED DECEMBER 31, 2016

TABLE OF CONTENTS

| ITEM | PAGE |
|---|----------|
| <u>PART I</u> | 3 |
| 1. <u>Business</u> | 3 - 31 |
| 1A. <u>Risk Factors</u> | 31 - 37 |
| 1B. <u>Unresolved Staff Comments</u> | 37 |
| 2. <u>Properties</u> | 38 |
| 3. <u>Legal Proceedings</u> | 39 |
| 4. <u>Mine Safety Disclosures</u> | 39 |
| <u>PART II</u> | 39 |
| 5. <u>Market for Registrant's Common Equity, Related Stockholders Matters and Issuer Purchases of Equity Securities</u> | 39 - 40 |
| 6. <u>Selected Financial Data</u> | 41 - 42 |
| 7. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u> | 43 - 56 |
| 7A. <u>Quantitative and Qualitative Disclosures About Market Risk</u> | 57 |
| 8. <u>Financial Statements and Supplementary Data</u> | 58 - 105 |
| 9. <u>Changes in and Disagreements with Accountants on Accounting and Financial Disclosure</u> | 106 |
| 9A. <u>Controls and Procedures</u> | 106 |
| 9B. <u>Other Information</u> | 107 |
| <u>PART III</u> | 107 |
| 10. <u>Directors, Executive Officers and Corporate Governance</u> | 107 |
| 11. <u>Executive Compensation</u> | 107 |
| 12. <u>Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters</u> | 108 |
| 13. <u>Certain Relationships and Related Transactions, and Director Independence</u> | 108 |
| 14. <u>Principal Accountant Fees and Services</u> | 108 |
| <u>PART IV</u> | 109 |
| 15. <u>Exhibits and Financial Statement Schedules</u> | 109 |
| <u>Signatures</u> | 110 |
| 16. <u>Form 10-K Summary</u> | 110 |

PART 1

Item 1. Business

Forward-Looking Statements

This Form 10-K may contain or incorporate by reference various forward-looking statements, which can be identified by the use of words such as "estimate," "project," "believe," "intend," "anticipate," "plan," "seek," "expect" and similar expressions and verbs in the future tense. These forward-looking statements include, but are not limited to:

- Statements of our goals, intentions and expectations;
- Statements regarding our business plans, prospects, growth and operating strategies;
- Statements regarding the quality of our loan and investment portfolio;
- Estimates of our risks and future costs and benefits.

These forward-looking statements are based on current beliefs and expectations of our management and are inherently subject to significant business, economic and competitive uncertainties and contingencies, many of which are beyond our control. In addition, these forward-looking statements are subject to assumptions with respect to future business strategies and decisions that are subject to change.

The following factors, among others, could cause actual results to differ materially from the anticipated results or other expectations expressed in the forward-looking statements.

- general economic conditions, either nationally or in our market area, that are different than expected;
- competition among depository and other financial institutions;
- inflation and changes in the interest rate environment that reduce our margins and yields, our mortgage banking revenues or reduce the fair value of financial instruments or reduce the origination levels in our lending business, or
- increase the level of defaults, losses or prepayments on loans we have made and make whether held in portfolio or sold in the secondary markets;
- adverse changes in the securities or secondary mortgage markets;
- changes in laws or government regulations or policies affecting financial institutions, including changes in regulatory fees and capital requirements;
- our ability to manage market risk, credit risk and operational risk in the current economic conditions;
- our ability to enter new markets successfully and capitalize on growth opportunities;
- our ability to successfully integrate acquired entities;
- decreased demand for our products and services;
- changes in tax policies or assessment policies;
- the inability of third-party provider to perform their obligations to us;
- changes in consumer spending, borrowing and savings habits;
- changes in accounting policies and practices, as may be adopted by the bank regulatory agencies, the Financial Accounting Standards Board, the Securities and Exchange Commission or the Public Company Accounting Oversight Board;
- our ability to retain key employees;
- significant increases in our loan losses; and
- changes in the financial condition, results of operations or future prospects of issuers of securities that we own.

See also the factors regarding future operations discussed in "Management's Discussion and Analysis of Financial Condition and Results of Operations" and "Risk Factors" below.

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Waterstone Financial, Inc., a Maryland corporation ("New Waterstone"), was organized in June 2013. Upon completion of the mutual-to-stock conversion of Lamplighter Financial, MHC in January 2014, New Waterstone became the holding company of WaterStone Bank SSB and succeeded to all of the business and operations of Waterstone Financial, Inc., a Federal corporation ("Waterstone-Federal") and each of Waterstone-Federal and Lamplighter Financial, MHC ceased to exist. In this report, we refer to WaterStone Bank, our wholly owned subsidiary, both before and after the reorganization, as "WaterStone Bank" or the "Bank."

- 3 -

New Waterstone did not engage in any business prior to the completion of the mutual-to-stock conversion of Lamplighter Financial, MHC on January 22, 2014. Consequently, this Annual Report on Form 10-K reflects the financial condition and operating results of Waterstone-Federal and its subsidiaries, including the Bank, until January 22, 2014, and of New Waterstone, and its subsidiaries, including the Bank, thereafter. The words "Waterstone Financial," "we" and "our" thus are intended to refer to Waterstone-Federal and its subsidiaries with respect to matters and time periods occurring on or before January 22, 2014, and to New Waterstone and its subsidiaries with respect to matters and time periods occurring thereafter.

Waterstone Financial, Inc. and its subsidiaries, including WaterStone Bank, are referred to herein as the "Company," "Waterstone Financial," or "we."

The Company maintains a website at www.wsbonline.com. We make available through that website, free of charge, copies of our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, amendments to those reports and proxy materials as soon as is reasonably practical after the Company electronically files those materials with, or furnishes them to, the Securities and Exchange Commission. You may access those reports by following the links under "Investor Relations" at the Company's website. Information on this website is not and should not be considered a part of this document.

Waterstone Financial's executive offices are located at 11200 West Plank Court, Wauwatosa, Wisconsin 53226, and its telephone number at this address is (414) 761-1000.

BUSINESS OF WATERSTONE BANK

General

WaterStone Bank is a community bank that has served the banking needs of its customers since 1921. WaterStone Bank also has an active mortgage banking subsidiary, Waterstone Mortgage Corporation, which had 77 offices in 22 states as of December 31, 2016.

WaterStone Bank conducts its community banking business from 11 banking offices located in Milwaukee, Washington and Waukesha Counties, Wisconsin, as well as a loan production office in Minneapolis, Minnesota. WaterStone Bank's principal lending activity is originating one- to four-family and multi-family residential real estate loans for retention in its portfolio. At December 31, 2016, such loans comprised 33.4% and 47.4%, respectively, of WaterStone Bank's loan portfolio. WaterStone Bank also offers home equity loans and lines of credit, construction and land loans, commercial real estate and commercial business loans, and consumer loans. WaterStone Bank funds its loan production primarily with retail deposits and Federal Home Loan Bank advances. Our deposit offerings include certificates of deposit, money market savings accounts, transaction deposit accounts, non-interest bearing demand accounts and individual retirement accounts. Our investment securities portfolio is comprised principally of mortgage-backed securities, government-sponsored enterprise bonds, municipal obligations, and other debt securities.

WaterStone Bank is subject to comprehensive regulation and examination by the Wisconsin Department of Financial Institutions (the "WDFI") and the Federal Deposit Insurance Corporation.

WaterStone Bank's executive offices are located at 11200 West Plank Court, Wauwatosa, Wisconsin 53226, and its telephone number is (414) 761-1000. Its website address is www.wsbonline.com.

WaterStone Bank's mortgage banking operations are conducted through its wholly-owned subsidiary, Waterstone Mortgage Corporation. Waterstone Mortgage Corporation originates single-family residential real estate loans for sale into the secondary market. Waterstone Mortgage Corporation utilizes lines of credit provided by WaterStone Bank as a primary source of funds, and also utilizes a line of credit with another financial institution as needed. On a

consolidated basis, Waterstone Mortgage Corporation originated approximately \$2.38 billion, which excludes the loans originated from Waterstone Mortgage Corporation and purchased by WaterStone Bank, in mortgage loans held for sale during the year ended December 31, 2016.

Market Area

WaterStone Bank. WaterStone Bank's market area is broadly defined as the Milwaukee, Wisconsin metropolitan market, which is geographically located in the southeast corner of the state. WaterStone Bank's primary market area is Milwaukee and Waukesha counties and the five surrounding counties of Ozaukee, Washington, Jefferson, Walworth and Racine. We have six branch offices in Milwaukee County, four branch offices in Waukesha County and one branch office in Washington County. At June 30, 2016 (the latest date for which information was publicly available), 49.2% of deposits in the State of Wisconsin were located in the seven-county metropolitan Milwaukee market and 43.3% of deposits in the State of Wisconsin were located in the three counties in which the Bank has a branch office.

WaterStone Bank's primary market area for deposits includes the communities in which we maintain our banking office locations. Our primary lending market area is broader than our primary deposit market area and includes all of the primary market area noted above but extends further west to the Madison, Wisconsin market and further north to the Appleton and Green Bay, Wisconsin markets. In addition, in October 2013 we opened a loan production office in Minneapolis, Minnesota, which has a primary lending market area of the Minneapolis-St. Paul, Minnesota metropolitan market.

Waterstone Mortgage Corporation. As of December 31, 2016, Waterstone Mortgage Corporation had 15 offices in Wisconsin, 13 offices in Florida, nine offices in Pennsylvania, six offices in Minnesota, five offices in Indiana, Ohio, and Texas, two offices in each of Arizona, California, Maryland, and Virginia, and one office in each of Colorado, Georgia, Idaho, Illinois, Iowa, Maine, Massachusetts, New Hampshire, Oregon, Tennessee, and Washington.

Competition

WaterStone Bank. WaterStone Bank faces competition within our market area both in making real estate loans and attracting deposits. The Milwaukee-Waukesha-West Allis metropolitan statistical area has a high concentration of financial institutions, including large commercial banks, community banks and credit unions. The Federal Deposit Insurance Corporation has determined that our market area is a "high-rate" area with regard to deposit pricing as compared to the rest of the United States. As of June 30, 2016, based on the Federal Deposit Insurance Corporation's annual Summary of Deposits Report, we had the eighth largest market share in our metropolitan statistical area out of 51 financial institutions in our metropolitan statistical area, representing 1.5% of all deposits.

Our competition for loans and deposits comes principally from commercial banks, savings institutions, mortgage banking firms and credit unions. We face additional competition for deposits from money market funds, brokerage firms, and mutual funds. Some of our competitors offer products and services that we do not offer, such as trust services and private banking.

Our primary focus is to build and develop profitable consumer and commercial customer relationships while maintaining our role as a community bank.

Waterstone Mortgage Corporation. Waterstone Mortgage Corporation faces competition for originating loans both directly within the markets in which it operates and from entities that provide services throughout the United States through internet services. Waterstone Mortgage Corporation's competition comes principally from other mortgage banking firms, as well as from commercial banks, savings institutions and credit unions.

Lending Activities

The scope of the discussion included under "Lending Activities" is limited to lending operations related to loans originated for investment. A discussion of the lending activities related to loans originated for sale is included under "Mortgage Banking Activities."

Historically, our principal lending activity has been originating mortgage loans for the purchase or refinancing of residential real estate. Generally, we retain the loans that we originate, which we refer to as loans originated for investment. One- to four-family residential mortgage loans represented \$392.8 million, or 33.4%, of our total loan portfolio at December 31, 2016. Multi-family residential mortgage loans represented \$558.6 million, or 47.4%, of our total loan portfolio at December 31, 2016. We also offer construction and land loans, commercial real estate loans, home equity lines of credit and commercial loans. At December 31, 2016, commercial real estate loans, commercial business loans, home equity loans, and land and construction loans totaled \$159.4 million, \$26.8 million, \$21.8 million and \$18.2 million, respectively.

Loan Portfolio Composition. The following table sets forth the composition of our loan portfolio in dollar amounts and as a percentage of the total portfolio at the dates indicated.

| | At December 31, | | 2015 | | 2014 | | 2013 | | 2012 | |
|--------------------------|------------------------|----------------|---------------|----------------|---------------|----------------|---------------|----------------|---------------|----------------|
| | <u>Amount</u> | <u>Percent</u> | <u>Amount</u> | <u>Percent</u> | <u>Amount</u> | <u>Percent</u> | <u>Amount</u> | <u>Percent</u> | <u>Amount</u> | <u>Percent</u> |
| | (Dollars in Thousands) | | | | | | | | | |
| Mortgage loans: | | | | | | | | | | |
| Residential real estate: | | | | | | | | | | |
| One- to four-family | \$392,817 | 33.35% | \$381,992 | 34.26% | \$411,979 | 37.62% | \$413,614 | 37.85% | \$460,821 | 40.65% |

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| | | | | | | | | | | |
|--------------------------|---------|---------|---------|---------|---------|---------|---------|---------|---------|---------|
| Multi-family | 558,592 | 47.42 % | 547,250 | 49.08 % | 522,281 | 47.70 % | 521,597 | 47.75 % | 514,363 | 45.37 % |
| Home equity | 21,778 | 1.85 % | 24,326 | 2.18 % | 29,207 | 2.67 % | 35,432 | 3.24 % | 36,494 | 3.22 % |
| Construction and land | 18,179 | 1.54 % | 19,148 | 1.72 % | 17,081 | 1.56 % | 31,905 | 2.92 % | 33,818 | 2.98 |