NORTHEAST BANCORP /ME/
Form 10-Q
May 13, 2016

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

Quarterly report pursuant to Section 13 or 15 (d) of the Securities Exchange Act of 1934

For the quarterly period ended March 31, 2016

Commission File Number: 1-14588

Northeast Bancorp

(Exact name of registrant as specified in its charter)

Maine	**01-0425066**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
500 Canal Street, Lewiston, Maine	**04240**
(Address of Principal executive offices)	**(Zip Code)**

(207) 786-3245

Registrant's telephone number, including area code

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subjected 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 definition of "accelerated filer", "large accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (check one): Large accelerated filer __ Accelerated filer __ Non-accelerated filer ___ Smaller Reporting Company

Indicate by check mark whether the registrant is a shell company (as defined by 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. As of May 6, 2016, the registrant had outstanding 8,089,790 shares of voting common stock, $1.00 par value per share and 1,227,683 shares of non-voting common stock, $1.00 par value per share.

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PART 1- FINANCIAL INFORMATION

Item 1. Financial Statements (Unaudited)

NORTHEAST BANCORP AND SUBSIDIARY

CONSOLIDATED BALANCE SHEETS

(Unaudited)

(Dollars in thousands, except share and per share data)

	March 31, 2016	June 30, 2015
Assets		
Cash and due from banks	$4,025	$2,789
Short-term investments	87,427	87,061
Total cash and cash equivalents	91,452	89,850
Available-for-sale securities, at fair value	90,491	101,908
Residential real estate loans held for sale	3,475	7,093
SBA loans held for sale	1,880	1,942
Total loans held for sale	5,355	9,035
Loans		
Commercial real estate	423,234	348,676
Residential real estate	119,327	132,669
Commercial and industrial	150,217	123,133
Consumer	6,292	7,659
Total loans	699,070	612,137
Less: Allowance for loan losses	2,223	1,926
Loans, net	696,847	610,211
Premises and equipment, net	8,101	8,253
Real estate owned and other possessed collateral, net	690	1,651
Federal Home Loan Bank stock, at cost	2,571	4,102
Intangible assets, net	1,840	2,209
Bank owned life insurance	15,612	15,276
Other assets	9,730	8,223
Total assets	$922,689	$850,718
Liabilities and Stockholders' Equity		
Deposits		

Demand	$60,573	$60,383
Savings and interest checking	104,802	100,134
Money market	234,142	168,527
Time	353,432	345,715
Total deposits	752,949	674,759
Federal Home Loan Bank advances	30,103	30,188
Wholesale repurchase agreements	-	10,037
Short-term borrowings	2,753	2,349
Junior subordinated debentures issued to affiliated trusts	8,771	8,626
Capital lease obligation	1,190	1,368
Other liabilities	12,397	10,664
Total liabilities	808,163	737,991
Commitments and contingencies	-	-
Stockholders' equity		
Preferred stock, $1.00 par value, 1,000,000 shares authorized; no shares issued and outstanding at March 31, 2016 and June 30, 2015	-	-
Voting common stock, $1.00 par value, 25,000,000 shares authorized; 8,103,190 and 8,575,144 shares issued and outstanding at March 31, 2016 and June 30, 2015, respectively	8,103	8,575
Non-voting common stock, $1.00 par value, 3,000,000 shares authorized; 1,227,683 and 1,012,739 shares issued and outstanding at March 31, 2016 and June 30, 2015, respectively	1,228	1,013
Additional paid-in capital	82,983	85,506
Retained earnings	24,055	18,921
Accumulated other comprehensive loss	(1,843)	(1,288)
Total stockholders' equity	114,526	112,727
Total liabilities and stockholders' equity	$922,689	$850,718

The accompanying notes are an integral part of these unaudited consolidated financial statements.

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NORTHEAST BANCORP AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

(Dollars in thousands, except share and per share data)

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2016	2015	2016	2015
Interest and dividend income:				
Interest and fees on loans	$10,904	$10,619	$33,413	$32,487
Interest on available-for-sale securities	236	222	700	697
Other interest and dividend income	119	72	295	218
Total interest and dividend income	11,259	10,913	34,408	33,402
Interest expense:				
Deposits	1,566	1,271	4,356	3,681
Federal Home Loan Bank advances	255	257	774	845
Wholesale repurchase agreements	-	71	65	216
Short-term borrowings	5	5	19	21
Junior subordinated debentures issued to affiliated trusts	164	171	476	566
Obligation under capital lease agreements	15	18	49	56
Total interest expense	2,005	1,793	5,739	5,385
Net interest and dividend income before provision for loan losses	9,254	9,120	28,669	28,017
Provision for loan losses	236	44	1,301	477
Net interest and dividend income after provision for loan losses	9,018	9,076	27,368	27,540
Noninterest income:				
Fees for other services to customers	428	303	1,264	1,089
Gain on sales of residential loans held for sale	335	355	1,292	1,384
Gain on sales of portfolio loans	1,205	425	2,558	950
(Loss) gain recognized on real estate owned and other repossessed collateral, net	(54)	357	(127)	303
Bank-owned life insurance income	112	110	336	329
Other noninterest income	9	4	39	23
Total noninterest income	2,035	1,554	5,362	4,078
Noninterest expense:				
Salaries and employee benefits	4,846	4,316	13,956	13,586
Occupancy and equipment expense	1,327	1,278	3,937	3,662

Professional fees	348	386	1,042	1,153
Data processing fees	394	361	1,109	1,029
Marketing expense	64	54	200	203
Loan acquisition and collection expense	297	409	961	1,096
FDIC insurance premiums	125	137	354	371
Intangible asset amortization	108	128	369	460
Other noninterest expense	903	816	2,489	2,272
Total noninterest expense	8,412	7,885	24,417	23,832
Income before income tax expense	2,641	2,745	8,313	7,786
Income tax expense	832	993	2,892	2,810
Net income	1,809	1,752	5,421	4,976
Weighted-average shares outstanding:				
Basic	9,456,198	9,833,033	9,526,302	10,049,983
Diluted	9,459,611	9,833,033	9,531,747	10,049,983
Earnings per common share:				
Basic	$0.19	$0.18	$0.57	$0.50
Diluted	0.19	0.18	0.57	0.50
Cash dividends declared per common share	$0.01	$0.01	$0.03	$0.03

The accompanying notes are an integral part of these unaudited consolidated financial statements.

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NORTHEAST BANCORP AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited)

(Dollars in thousands)

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2016	2015	2016	2015
Net income	$1,809	$1,752	$5,421	$4,976
Other comprehensive loss, before tax:				
Available-for-sale securities:				
Change in net unrealized gain on available-for-sale securities	867	571	641	834
Derivatives and hedging activities:				
Change in accumulated lo ss on effective cash flow hedges	(982)	(566)	(1,536)	(1,341)
Reclassification adjustments for net gains included in net income	-	(16)	-	(49)
Total derivatives and hedging activities	(982)	(582)	(1,536)	(1,390)
Total other comprehensive loss, before tax	(115)	(11)	(895)	(556)
Income tax (benefit) expense related to other comprehensive loss	(44)	(4)	(340)	(191)
Other comprehensive loss, net of tax	(71)	(7)	(555)	(365)
Comprehensive income	$1,738	$1,745	$4,866	$4,611

The accompanying notes are an integral part of these unaudited consolidated financial statements.

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NORTHEAST BANCORP AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

(Unaudited)

(Dollars in thousands, except share and per share data)

	Preferred Stock		Voting Common Stock		Non-voting Common Stock		Additional Paid-in	Retained	Accumulated Other Comprehensive	Total Stockholders'
	Shares	Amount	Shares	Amount	Shares	Amount	Capital	Earnings	Loss	Equity
Balance at June 30, 2014	-	$ -	9,260,331	$ 9,260	880,963	$ 881	$ 90,914	$ 12,294	$ (1,283)	$ 112,066
Net income	-	-	-	-	-	-	-	4,976	-	4,976
Other comprehensive loss, net of tax	-	-	-	-	-	-	-	-	(365)	(365)
Common stock repurchased	-	-	(479,936)	(480)	-	-	(3,912)	-	-	(4,392)
Conversion of voting common stock to non-voting common stock	-	-	(30,525)	(30)	30,525	30	-	-	-	-
Dividends on common stock at $0.03 per share	-	-	-	-	-	-	-	(302)	-	(302)
Stock-based compensation	-	-	-	-	-	-	504	-	-	504
Issuance of restricted common stock	-	-	174,000	174	-	-	(174)	-	-	-
Cancellation and forfeiture of restricted common stock	-	-	(15,749)	(16)	-	-	16	-	-	-
Balance at March 31, 2015	-	$ -	8,908,121	$ 8,908	911,488	$ 911	$ 87,348	$ 16,968	$ (1,648)	$ 112,487
Balance at June 30, 2015	-	$ -	8,575,144	$ 8,575	1,012,739	$ 1,013	$ 85,506	$ 18,921	$ (1,288)	$ 112,727

Net income	-	-	-	-	-	-	-	5,421	-	5,421
Other comprehensive loss, net of tax	-	-	-	-	-	-	-	-	(555)	(555)
Common stock repurchased	-	-	(309,500)	(310)	-	-	(2,905)	-	-	(3,215)
Conversion of voting common stock to non-voting common stock	-	-	(214,944)	(215)	214,944	215	-	-	-	-
Dividends on common stock at $0.03 per share	-	-	-	-	-	-	-	(287)	-	(287)
Stock-based compensation	-	-	-	-	-	-	445	-	-	445
Issuance of restricted common stock	-	-	100,000	100	-	-	(100)	-	-	-
Cancellation and forfeiture of restricted common stock	-	-	(47,510)	(47)	-	-	37	-	-	(10)
Balance at March 31, 2016	-	$ -	8,103,190	$ 8,103	1,227,683	$ 1,228	$ 82,983	$ 24,055	$ (1,843)	$ 114,526

The accompanying notes are an integral part of these unaudited consolidated financial statements.

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NORTHEAST BANCORP AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(Dollars in thousands)

	Nine Months Ended March 31,	
	2016	2015
Operating activities:		
Net income	$5,421	$4,976
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	1,301	477
Loss (gain) on sale and impairment of real estate owned and other repossessed collateral, net	121	(303)
Loss on sale of premises and equipment, net	6	23
Accretion of fair value adjustments on loans, net	(7,348)	(9,149)
Accretion of fair value adjustments on deposits, net	(5)	(159)
Accretion of fair value adjustments on borrowings, net	23	(92)
Originations of loans held for sale	(66,929)	(68,734)
Net proceeds from sales of loans held for sale	69,959	77,624
Gain on sales of residential loans held for sale	(1,292)	(1,384)
Gain on sales of portfolio loans	(2,558)	(950)
Amortization of intangible assets	369	460
Bank-owned life insurance income, net	(336)	(329)
Depreciation of premises and equipment	1,230	1,259
Stock-based compensation	445	504
Amortization of available-for-sale securities, net	754	765
Changes in other assets and liabilities:		
Other assets	(378)	(687)
Other liabilities	197	1,197
Net cash provided by operating activities	980	5,498
Investing activities:		
Purchases of available-for-sale securities	(20,566)	-
Proceeds from maturities and principal payments on available-for-sale securities	31,870	8,427
Loan purchases	(81,245)	(57,896)
Proceeds from sales of portfolio loans	27,799	7,200
Loan originations, principal collections, and purchased loan paydowns, net	(24,095)	(4,434)
Purchases and disposals of premises and equipment, net	(1,084)	(242)
Redemption of Federal Home Loan Bank stock	1,531	-
Proceeds from sales of real estate owned and other repossessed collateral	1,503	713
Net cash used in investing activities	(64,287)	(46,232)
Financing activities:		
Net increase in deposits	78,195	81,007
Net increase (decrease) in short-term borrowings	404	(123)
Repurchase of common stock	(3,215)	(4,392)

Taxes paid for retirement of common stock	(10)	-
Dividends paid on common stock	(287)	(302)
Repayments of FHLB advances	-	(12,500)
Repayment of wholesale repurchase agreements	(10,000)	-
Repayment of capital lease obligation	(178)	(142)
Net cash provided by financing activities	64,909	63,548
Net increase in cash and cash equivalents	1,602	22,814
Cash and cash equivalents, beginning of period	89,850	82,259
Cash and cash equivalents, end of period	$91,452	$105,073
Supplemental schedule of noncash investing and financing activities:		
Transfers from loans to real estate owned and other repossessed collateral	$663	$2,041

The accompanying notes are an integral part of these unaudited consolidated financial statements.

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NORTHEAST BANCORP AND SUBSIDIARY

Notes to Unaudited Consolidated Financial Statements

March 31, 2016

1. Basis of Presentation

The accompanying unaudited condensed and consolidated interim financial statements include the accounts of Northeast Bancorp (“Northeast” or the “Company”) and its wholly-owned subsidiary, Northeast Bank (the “Bank”).

These financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (“US GAAP”) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and notes required by GAAP for complete financial statements. In the opinion of management, the accompanying consolidated financial statements contain all adjustments (consisting principally of normal recurring accruals) considered necessary for a fair presentation of the Company's financial position, results of operations, and cash flows for the interim periods presented. These financial statements and notes should be read in conjunction with the audited consolidated financial statements and notes thereto for the fiscal year ended June 30, 2015 (“Fiscal 2015”) included in the Company's Annual Report on Form 10-K filed with the Securities and Exchange Commission.

2. Recent Accounting Pronouncements

In January 2014, the FASB issued ASU No. 2014-01, Investments—Equity Method and Joint Ventures (Topic 323): Accounting for Investments in Qualified Affordable Housing Projects ("ASU 2014-01"). The amendments in ASU 2014-01 provide guidance on accounting for investments by a reporting entity in flow-through limited liability entities that manage or invest in affordable housing projects that qualify for the low-income housing tax credit. The amendments permit reporting entities to make an accounting policy election to account for their investments in qualified affordable housing projects using the proportional amortization method if certain conditions are met. Under the proportional amortization method, an entity amortizes the initial cost of the investment in proportion to the tax credits and other tax benefits received and recognizes the net investment performance in the income statement as a component of income tax expense (benefit). The amendments are effective for fiscal years, and interim periods within those years, beginning after December 15, 2014 and should be applied retrospectively to all periods presented. Early adoption is permitted. The Company adopted the standard in the current period. See Part I. Item I. “Notes to Unaudited Consolidated Financial Statements – Note 6: Investments in Qualified Affordable Housing Projects” for further discussion and related effect.

In May 2014, the Financial Accounting Standards Board ("FASB") issued ASU 2014-09*, Revenue from Contracts with Customers (Topic 606)* ("ASU 2014-09"). ASU 2014-09 implements a common revenue standard that clarifies the principles for recognizing revenue. The core principle of ASU 2014-09 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. To achieve that core principle, an entity should apply the following steps: (i) identify the contract(s) with a customer, (ii) identify the performance obligations in the contract, (iii) determine the transaction price, (iv) allocate the transaction price to the performance obligations in the contract and (v) recognize revenue when (or as) the entity satisfies a performance obligation. ASU 2015-14, *Revenue from Contracts with Customers (Topic 606)* ("ASU 2014-09") was issued in August 2015 which defers adoption to annual reporting periods beginning after December 15, 2017.

In June 2014, the FASB issued ASU 2014-11, Transfers and Servicing (Topic 860): Repurchase-to-Maturity Transactions, Repurchase Financings, and Disclosures ("ASU 2014-11"). ASU 2014-11 requires that repurchase-to-maturity transactions be accounted for as secured borrowings consistent with the accounting for other repurchase agreements. In addition, ASU 2014-11 requires separate accounting for repurchase financings, which entails the transfer of a financial asset executed contemporaneously with a repurchase agreement with the same counterparty. ASU 2014-11 requires entities to disclose certain information about transfers accounted for as sales in transactions that are economically similar to repurchase agreements. In addition, ASU 2014-11 requires disclosures related to collateral, remaining contractual tenor and of the potential risks associated with repurchase agreements, securities lending transactions and repurchase-to-maturity transactions. ASU 2014-11 was effective July 1, 2015 and did not have a significant impact on the Company's financial statements.

In August 2014, the FASB issued ASU 2014-14, Receivables - Troubled Debt Restructurings by Creditors (Subtopic 310-40): Classification of Certain Government-Guaranteed Mortgage Loans upon Foreclosure ("ASU 2014-14"). ASU 2014-14 affects creditors that hold government-guaranteed mortgage loans, including those guaranteed by the Federal Housing Administration (FHA) of the U.S. Department of Housing and Urban Development (HUD), and the U.S. Department of Veterans Affairs (VA). The update requires that, upon foreclosure, a guaranteed mortgage loan be derecognized and a separate other receivable be recognized when specific criteria are met. ASU 2014-14 is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2014. The adoption of this guidance did not have a significant impact on the Company's financial statements.

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In May 2015, the FASB issued ASU 2015-07, Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent) (“ASU 2015-07”). The amendment affects reporting entities that elect to measure the fair value of an investment using the net asset value per share as a practical expedient. The Company adopted the standard in the current period. See Part I. Item I. “Notes to Unaudited Consolidated Financial Statements – Note 11: Fair Value Measurements” for further discussion and related effect.

In January 2016, the FASB issued ASU 2016-01, *Financial Instruments—Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities* (“ASU 2016-01”). This guidance changes how entities account for equity investments that do not result in consolidation and are not accounted for under the equity method of accounting. Entities will be required to measure these investments at fair value at the end of each reporting period and recognize changes in fair value in net income. A practicability exception will be available for equity investments that do not have readily determinable fair values, however; the exception requires the Company to adjust the carrying amount for impairment and observable price changes in orderly transactions for the identical or a similar investment of the same issuer. This guidance also changes certain disclosure requirements and other aspects of current US GAAP. This guidance is effective for fiscal years beginning after December 15, 2017, including interim periods within the fiscal year. The Company is currently evaluating the impact of the adoption of ASU 2016-01 on its consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, *Leases (Topic 842)* (“ASU 2016-02”). The new guidance establishes the principles to report transparent and economically neutral information about the assets and liabilities that arise from leases. Entities will be required to recognize the lease assets and lease liabilities that arise from leases in the statement of financial position and to disclose qualitative and quantitative information about lease transactions, such as information about variable lease payments and options to renew and terminate leases. This guidance is effective for fiscal years beginning after December 15, 2018, including interim periods within the fiscal year. The Company is currently evaluating the impact of the adoption of ASU 2016-02 on its consolidated financial statements.

In March 2016, the FASB issued ASU 2016-05, *Derivatives and Hedging (Topic 815): Effect of Derivative Contract Novations on Existing Hedge Accounting Relationships* (“ASU 2016-05”). The new guidance clarifies that a change in the counterparty to a derivative instrument that has been designated as the hedging instrument under Topic 815 does not, in and of itself, require de-designation of that hedging relationship provided that all other hedge accounting criteria continue to be met. This guidance is effective for fiscal years beginning after December 15, 2016, and interim periods within those fiscal years. The adoption of this guidance is not expected to have a significant impact on the Company’s financial statements.

In March 2016, the FASB issued ASU 2016-09, *Compensation-Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting* (“ASU 2016-09”). The new guidance simplifies several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. Entities will be required to recognize the income tax effects of awards in the income statement when the awards vest or are settled. This guidance is effective for fiscal years beginning after December 15, 2016, and interim periods within those annual periods. The adoption of this guidance is not expected to have a significant impact on the Company’s financial statements.

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3. Securities Available-for-Sale

The following presents a summary of the amortized cost, gross unrealized holding gains and losses, and fair value of securities available for sale.

	March 31, 2016			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(Dollars in thousands)			
U.S. Government agency securities	$39,479	$ 31	$ (7)	$39,503
Agency mortgage-backed securities	46,137	29	(276)	45,890
Other investments measured at net asset value	5,070	28	-	5,098
	$90,686	$ 88	$ (283)	$90,491

	June 30, 2015			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(Dollars in thousands)			
U.S. Government agency securities	$48,191	$ 40	$ (1)	$48,230
Agency mortgage-backed securities	54,553	2	(877)	53,678
Other investments measured at net asset value	-	-	-	-
	$102,744	$ 42	$ (878)	$101,908

When securities are sold, the adjusted cost of the specific security sold is used to compute the gain or loss on sale. There were no securities sold during the three and nine months ended March 31, 2016 or 2015. At March 31, 2016, no investment securities were pledged as collateral to secure outstanding borrowings.

The following summarizes the Company’s gross unrealized losses and fair values aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position.

	March 31, 2016		
	Less than 12 Months	More than 12 Months	Total

	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	(Dollars in thousands)					
U.S. Government agency securities	$12,429	$ (7)	$-	$ -	$12,429	$ (7)
Agency mortgage-backed securities	1,774	(2)	39,451	(274)	41,225	(276)
Other investments measured at net asset value	-	-	-	-	-	-
	$14,203	$ (9)	$39,451	$ (274)	$53,654	$ (283)

	June 30, 2015					
	Less than 12 Months		More than 12 Months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	(Dollars in thousands)					
U.S. Government agency securities	$2,999	$ (1)	$-	$ -	$2,999	$ (1)
Agency mortgage-backed securities	10,295	(106)	41,349	(771)	51,644	(877)
Other investments measured at net asset value	-	-	-	-	-	-
	$13,294	$ (107)	$41,349	$ (771)	$54,643	$ (878)

There were no other-than-temporary impairment losses on securities during the three and nine months ended March 31, 2016 or 2015.

At March 31, 2016, the Company had eighteen securities in a continuous loss position for greater than twelve months. At March 31, 2016, all of the Company’s available-for-sale securities were issued or guaranteed by either government agencies or government-sponsored enterprises. The decline in fair value of the Company’s available-for-sale securities at March 31, 2016 is attributable to changes in interest rates.

In addition to considering current trends and economic conditions that may affect the quality of individual securities within the Company’s investment portfolio, management of the Company also considers the Company’s ability and intent to hold such securities to maturity or recovery of cost. At March 31, 2016, it was more likely than not that the Company will not sell or be required to sell the investment securities before recovery of its amortized cost. As such, management does not believe any of the Company’s available-for-sale securities were other-than-temporarily impaired at March 31, 2016.

The investment measured at net asset value is a fund that seeks to invest in securities either issued or guaranteed by the U.S. government or its agencies ("the fund"). The underlying composition of the fund is primarily government agencies or other investment-grade investments. The effective duration of the investments is 4.56 years.

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The amortized cost and fair values of available-for-sale debt securities by contractual maturity are shown below as of March 31, 2016. Actual maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Amortized Cost	Fair Value
	(Dollars in thousands)	
Due within one year	$24,037	$24,042
Due after one year through five years	15,442	15,461
Due after five years through ten years	21,394	21,342
Due after ten years	24,743	24,548
Total	$85,616	$85,393

4. Loans, Allowance for Loan Losses and Credit Quality

Loans are carried at the principal amounts outstanding, or amortized acquired fair value in the case of acquired loans, adjusted by partial charge-offs and net of deferred loan costs or fees. Loan fees and certain direct origination costs are deferred and amortized into interest income over the expected term of the loan using the level-yield method. When a loan is paid off, the unamortized portion is recognized in interest income. Interest income is accrued based upon the daily principal amount outstanding except for loans on nonaccrual status.

Loans purchased by the Company are accounted for under ASC 310-30, *Receivables — Loans and Debt Securities Acquired with Deteriorated Credit Quality* (“ASC 310-30”). At acquisition, the effective interest rate is determined based on the discount rate that equates the present value of the Company’s estimate of cash flows with the purchase price of the loan. Prepayments are not assumed in determining a purchased loan’s effective interest rate and income accretion. The application of ASC 310-30 limits the yield that may be accreted on the purchased loan, or the “accretable yield,” to the excess of the Company’s estimate, at acquisition, of the expected undiscounted principal, interest, and other cash flows over the Company’s initial investment in the loan. The excess of contractually required payments receivable over the cash flows expected to be collected on the loan represents the purchased loan’s “nonaccretable difference.” Subsequent improvements in expected cash flows of loans with nonaccretable differences result in a prospective increase to the loan’s effective yield through a reclassification of some, or all, of the nonaccretable difference to accretable yield. The effect of subsequent credit-related declines in expected cash flows of purchased loans are recorded through a specific allocation in the allowance for loan losses.

Loans are generally placed on nonaccrual status when they are past due 90 days as to either principal or interest, or when in management’s judgment the collectability of interest or principal of the loan has been significantly impaired. Loans accounted for under ASC 310-30 are placed on nonaccrual when it is not possible to reach a reasonable expectation of the timing and amount of cash flows to be collected on the loan. When a loan has been placed on nonaccrual status, previously accrued and uncollected interest is reversed against interest on loans. Interest on nonaccrual loans is accounted for on a cash-basis or using the cost-recovery method when collectability is doubtful. A loan is returned to accrual status when collectability of principal is reasonably assured and the loan has performed for a reasonable period of time.

In cases where a borrower experiences financial difficulties and the Company makes certain concessionary modifications to contractual terms, the loan is classified as a troubled debt restructuring (“TDR”), and therefore by definition is an impaired loan. Concessionary modifications may include adjustments to interest rates, extensions of maturity, and other actions intended to minimize economic loss and avoid foreclosure or repossession of collateral. For loans accounted for under ASC 310-30, the Company evaluates whether it has granted a concession by comparing the restructured debt terms to the expected cash flows at acquisition plus any additional cash flows expected to be collected arising from changes in estimate after acquisition, and also qualitative considerations surrounding the modification. As a result, if an ASC 310-30 loan is modified to be consistent with, or better than, the Company’s expectations at acquisition, quantitatively and qualitatively, the loan would not qualify as a TDR. Nonaccrual loans that are restructured generally remain on nonaccrual status for a minimum period of six months to demonstrate that the borrower can meet the restructured terms. If the restructured loan is on accrual status prior to being modified, it is reviewed to determine if the modified loan should remain on accrual status. If the borrower's ability to meet the revised payment schedule is not reasonably assured, the loan is classified as a nonaccrual loan. With limited exceptions, loans classified as TDRs remain classified as such until the loan is paid off.

The composition of the Company's loan portfolio is as follows on the dates indicated.

	March 31, 2016			June 30, 2015		
	Originated	Purchased	Total	Originated	Purchased	Total
	(Dollars in thousands)					
Residential real estate	$97,566	$2,638	$100,204	$106,275	$2,068	$108,343
Home equity	19,123	-	19,123	24,326	-	24,326
Commercial real estate	192,432	230,802	423,234	148,425	200,251	348,676
Commercial and industrial	150,007	210	150,217	122,860	273	123,133
Consumer	6,292	-	6,292	7,659	-	7,659
Total loans	$465,420	$233,650	$699,070	$409,545	$202,592	$612,137

Total loans include deferred loan origination fees, net, of $44 thousand and $236 thousand as of March 31, 2016 and June 30, 2015, respectively.

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Past Due and Nonaccrual Loans

The following is a summary of past due and non-accrual loans:

	March 31, 2016							
	30-59 Days	60-89 Days	Past Due 90 Days or More-Still Accruing	Past Due 90 Days or More-Nonaccrual	Total Past Due	Total Current	Total Loans	Non-Accrual Loans
	(Dollars in thousands)							
Originated portfolio:								
Residential real estate	$665	$89	$ -	$ 1,754	$2,508	$95,058	$97,566	$3,270
Home equity	350	99	-	82	531	18,592	19,123	296
Commercial real estate	702	-	-	333	1,035	191,397	192,432	602
Commercial and industrial	1,910	17	-	-	1,927	148,080	150,007	2
Consumer	149	2	-	101	252	6,040	6,292	216
Total originated portfolio	3,776	207	-	2,270	6,253	459,167	465,420	4,386
Purchased portfolio:								
Residential real estate	-	-	-	1,185	1,185	1,453	2,638	1,185
Commercial and industrial	-	-	-	-	-	210	210	-
Commercial real estate	6,700	300	-	3,179	10,179	220,623	230,802	3,179
Total purchased portfolio	6,700	300	-	4,364	11,364	222,286	233,650	4,364
Total loans	$10,476	$507	$ -	$ 6,634	$17,617	$681,453	$699,070	$8,750

	June 30, 2015							
	30-59 Days	60-89 Days	Past Due 90 Days or More-Still Accruing	Past Due 90 Days or More-Nonaccrual	Total Past Due	Total Current	Total Loans	Non-Accrual Loans
	(Dollars in thousands)							
Originated portfolio:								
Residential real estate	$239	$973	$ -	$ 1,393	$2,605	$103,670	$106,275	$3,021

Home equity	9	-	-	11	20	24,306	24,326	11
Commercial real estate	300	-	-	704	1,004	147,421	148,425	994
Commercial and industrial	-	-	-	2	2	122,858	122,860	2
Consumer	105	29	-	56	190	7,469	7,659	190
Total originated portfolio	653	1,002	-	2,166	3,821	405,724	409,545	4,218
Purchased portfolio:								
Residential real estate	-	-	-	-	-	2,068	2,068	-
Commercial and industrial	-	-	-	-	-	273	273	-
Commercial real estate	86	299	-	2,410	2,795	197,456	200,251	6,532
Total purchased portfolio	86	299	-	2,410	2,795	199,797	202,592	6,532
Total loans	$739	$1,301	$ -	$ 4,576	$6,616	$605,521	$612,137	$10,750

Allowance for Loan Losses and Impaired Loans

The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. For residential and consumer loans, a charge-off is recorded no later than the point at which a loan is 180 days past due if the loan balance exceeds the fair value of the collateral, less costs to sell. For commercial loans, a charge-off is recorded on a case-by-case basis when all or a portion of the loan is deemed to be uncollectible. Subsequent recoveries, if any, are credited to the allowance.

The allowance for loan losses consists of general, specific, and unallocated reserves and reflects management's estimate of probable loan losses inherent in the loan portfolio at the balance sheet date. Management uses a consistent and systematic process and methodology to evaluate the appropriateness of the allowance for loan losses on a quarterly basis. The calculation of the allowance for loan losses is segregated by portfolio segments, which include: commercial real estate, commercial and industrial, consumer, residential real estate, and purchased loans. Risk characteristics relevant to each portfolio segment are as follows:

Residential real estate: All loans in this segment are collateralized by residential real estate and repayment is primarily dependent on the credit quality, loan-to-value ratio and income of the individual borrower. The overall health of the economy, particularly unemployment rates and housing prices, has a significant effect on the credit quality in this segment. For purposes of the Company's allowance for loan loss calculation, home equity loans and lines of credit are included in residential real estate.

Commercial real estate: Loans in this segment are primarily income-producing properties. For owner-occupied properties, the cash flows are derived from an operating business, and the underlying cash flows may be adversely affected by deterioration in the financial condition of the operating business. The underlying cash flows generated by non-owner occupied properties may be adversely affected by increased vacancy rates. Management periodically obtains rent rolls, with which it monitors the cash flows of these loans. Adverse developments in either of these areas will have an adverse effect on the credit quality of this segment. For purposes of the allowance for loan losses, this segment also includes construction loans.

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Commercial and industrial: Loans in this segment are made to businesses and are generally secured by the assets of the business. Repayment is expected from the cash flows of the business. Weakness in national or regional economic conditions, and a corresponding weakness in consumer or business spending, will have an adverse effect on the credit quality of this segment.

Consumer: Loans in this segment are generally secured, and repayment is dependent on the credit quality of the individual borrower. Repayment of consumer loans is generally based on the earnings of individual borrowers, which may be adversely impacted by regional labor market conditions.

Purchased: Loans in this segment are typically secured by commercial real estate, multi-family residential real estate, or business assets and have been acquired by the Bank's Loan Acquisition and Servicing Group ("LASG"). Loans acquired by the LASG are, with limited exceptions, performing loans at the date of purchase. Repayment of loans in this segment is largely dependent on cash flow from the successful operation of the property, in the case of non-owner occupied property, or operating business, in the case of owner-occupied property. Loan performance may be adversely affected by factors affecting the general economy or conditions specific to the real estate market, such as geographic location or property type. Loans in this segment are evaluated for impairment under ASC 310-30. The Company reviews expected cash flows from purchased loans on a quarterly basis. The effect of a decline in expected cash flows subsequent to the acquisition of the loan is recognized through a specific allocation in the allowance for loan losses.

The general component of the allowance for loan losses for loans accounted for under ASC 310-20 is based on historical loss experience adjusted for qualitative factors stratified by loan segment. The Company does not weight periods used in that analysis to determine the average loss rate in each portfolio segment. This historical loss factor is adjusted for the following qualitative factors:

- Levels and trends in delinquencies and nonperforming loans
- Trends in the volume and nature of loans
- Trends in credit terms and policies, including underwriting standards, procedures and practices, and the experience and ability of lending management and staff
- Trends in portfolio concentration
- National and local economic trends and conditions

Effects of changes or trends in internal risk ratings

Other effects resulting from trends in the valuation of underlying collateral

The allocated component of the allowance for loan losses relates to loans that are classified as impaired. Impairment is measured on a loan-by-loan basis for commercial and industrial, and commercial real estate loans by either the present value of expected future cash flows discounted at the loan's effective interest rate or the fair value of the collateral if the loan is collateral dependent. An allowance is established when the discounted cash flows or collateral value of the impaired loan is lower than the carrying value of that loan. Large groups of smaller-balance homogeneous loans, such as consumer and residential real estate loans are collectively evaluated for impairment based on the group's historical loss experience adjusted for qualitative factors. Accordingly, the Company does not separately identify individual consumer and residential loans for individual impairment and disclosure. However, all TDRs are individually reviewed for impairment.

For all portfolio segments, except loans accounted for under ASC 310-30, a loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. 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. For the purchased loan segment, a loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to realize cash flows as expected at acquisition. For loans accounted for under ASC 310-30 for which cash flows can reasonably be estimated, loan impairment is measured based on the decrease in expected cash flows from those estimated at acquisition, excluding changes due to changes in interest rate indices and other non-credit related factors, discounted at the loan's effective rate assumed at acquisition. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting the scheduled principal and interest payments when due.

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The following table sets forth activity in the Company’s allowance for loan losses.

	Three Months Ended March 31, 2016						
	Residential Real Estate	Commercial Real Estate	Commercial and Industrial	Consumer	Purchased	Unallocated	Total
	(Dollars in thousands)						
Beginning balance	$861	$ 844	$ 179	$ 36	$ 209	$ -	$2,129
Provision	20	48	96	7	62	3	236
Recoveries	20	-	6	2	-	-	28
Charge-offs	(87)	-	(73)	(10)	-	-	(170)
Ending balance	$814	$ 892	$ 208	$ 35	$ 271	$ 3	$2,223

	Three Months Ended March 31, 2015						
	Real Estate	Commercial Real Estate	Commercial and Industrial	Consumer	Purchased	Unallocated	Total
	(Dollars in thousands)						
Beginning balance	$796	$ 288	$ 54	$ 59	$ 413	$ 54	$1,664
Provision	(38)	187	(45)	(13)	(87)	40	44
Recoveries	1	-	35	4	-	-	40
Charge-offs	-	-	(1)	(6)	-	-	(7)
Ending balance	$759	$ 475	$ 43	$ 44	$ 326	$ 94	$1,741

	Nine Months Ended March 31, 2016						
	Residential Real Estate	Commercial Real Estate	Commercial and Industrial	Consumer	Purchased	Unallocated	Total
	(Dollars in thousands)						
Beginning balance	$741	$ 694	$ 117	$ 35	$ 283	$ 56	$1,926
Provision	146	235	154	32	787	(53)	1,301
Recoveries	33	5	11	7	-	-	56
Charge-offs	(106)	(42)	(74)	(39)	(799)	-	(1,060)
Ending balance	$814	$ 892	$ 208	$ 35	$ 271	$ 3	$2,223

	Nine Months Ended March 31, 2015						
	Residential	Commercial	Commercial	Consumer	Purchased	Unallocated	Total

	Real Estate	Real Estate	and Industrial				
	(Dollars in thousands)						
Beginning balance	$580	$ 358	$ 48	$ 79	$ 267	$ 35	$1,367
Provision	322	116	(39)	(40)	59	59	477
Recoveries	17	1	35	17	-	-	70
Charge-offs	(160)	-	(1)	(12)	-	-	(173)
Ending balance	$759	$ 475	$ 43	$ 44	$ 326	$ 94	$1,741

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The following table sets forth information regarding the allowance for loan losses by portfolio segment and impairment methodology.

	March 31, 2016						
	Residential Real Estate	Commercial Real Estate	Commercial and Industrial	Consumer	Purchased	Unallocated	Total
	(Dollars in thousands)						
Allowance for loan losses:							
Individually evaluated	$510	$ 36	$ 2	$ 2	$ -	$ -	$550
Collectively evaluated	304	856	206	33	-	3	1,402
ASC 310-30	-	-	-	-	271	-	271
Total	$814	$ 892	$ 208	$ 35	$271	$ 3	$2,223
Loans:							
Individually evaluated	$5,404	$ 1,823	$ 19	$ 422	$ -	$ -	$7,668
Collectively evaluated	111,285	190,609	149,988	5,870	-	-	457,752
ASC 310-30	-	-	-	-	233,650	-	233,650
Total	$116,689	$ 192,432	$ 150,007	$ 6,292	$233,650	$ -	$699,070

	June 30, 2015						
	Residential Real Estate	Commercial Real Estate	Commercial and Industrial	Consumer	Purchased	Unallocated	Total
	(Dollars in thousands)						
Allowance for loan losses:							
Individually evaluated	$435	$ 21	$ -	$ -	$ -	$ -	$456
Collectively evaluated	306	673	117	35	-	56	1,187
ASC 310-30	-	-	-	-	283	-	283
Total	$741	$ 694	$ 117	$ 35	$283	$ 56	$1,926
Loans:							
Individually evaluated	$4,095	$ 2,381	$ 2	$ 253	$ -	$ -	$6,731
Collectively evaluated	126,506	146,044	122,858	7,406	-	-	402,814
ASC 310-30	-	-	-	-	202,592	-	202,592
Total	$130,601	$ 148,425	$ 122,860	$ 7,659	$202,592	$ -	$612,137

The following table sets forth information regarding impaired loans. Loans accounted for under ASC 310-30 that have performed based on cash flow and accretable yield expectations determined at date of acquisition are not considered impaired assets and have been excluded from the tables below.

	March 31, 2016			June 30, 2015		
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Recorded Investment	Unpaid Principal Balance	Related Allowance
	(Dollars in thousands)					
Impaired loans without a valuation allowance:						
Originated:						
Residential real estate	$3,193	$3,373	$ -	$1,975	$2,076	$ -
Consumer	400	433	-	253	262	-
Commercial real estate	696	698	-	1,505	1,510	-
Commercial and industrial	17	17	-	2	2	-
Purchased:						
Residential real estate	1,184	1,227	-	-	-	-
Commercial real estate	4,124	5,583	-	7,673	9,606	-
Total	9,614	11,331	-	11,408	13,456	-
Impaired loans with a valuation allowance:						
Originated:						
Residential real estate	2,211	2,150	510	2,120	2,060	435
Consumer	22	23	2	-	-	-
Commercial real estate	1,127	1,115	36	876	870	21
Commercial and industrial	2	2	2	-	-	-
Purchased:						