NORTHEAST BANCORP /ME/
Form 10-Q
November 09, 2016
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 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 November 2, 2016, the registrant had outstanding 7,487,552 shares of voting common stock, $1.00 par value per share and 1,343,683 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)

	September 30, 2016	June 30, 2016
Assets		
Cash and due from banks	$ 3,574	$ 2,459
Short-term investments	122,675	148,698
Total cash and cash equivalents	126,249	151,157
Available-for-sale securities, at fair value	94,583	100,572
Residential real estate loans held for sale	4,623	6,449
SBA loans held for sale	2,630	1,070
Total loans held for sale	7,253	7,519
Loans		
Commercial real estate	449,553	426,568
Residential real estate	110,223	113,962
Commercial and industrial	156,110	145,956
Consumer	5,532	5,950
Total loans	721,418	692,436
Less: Allowance for loan losses	2,506	2,350
Loans, net	718,912	690,086
Premises and equipment, net	7,452	7,801
Real estate owned and other repossessed collateral, net	3,774	1,652
Federal Home Loan Bank stock, at cost	2,408	2,408
Intangible assets, net	1,623	1,732
Bank owned life insurance	15,839	15,725
Other assets	7,475	7,501
Total assets	$ 985,568	$ 986,153
Liabilities and Shareholders' Equity		
Liabilities		

Deposits		
Demand	$ 74,249	$ 66,686
Savings and interest checking	107,365	107,218
Money market	302,079	275,437
Time	321,716	351,091
Total deposits	805,409	800,432
Federal Home Loan Bank advances	30,046	30,075
Subordinated debt	23,393	23,331
Capital lease obligation	1,066	1,128
Other liabilities	14,101	14,596
Total liabilities	874,015	869,562
Commitments and contingencies	-	-
Shareholders' equity		
Preferred stock, $1.00 par value, 1,000,000 shares authorized; no shares issued and outstanding at September 30, 2016 and June 30, 2016	-	-
Voting common stock, $1.00 par value, 25,000,000 shares authorized; 7,487,552 and 8,089,790 shares issued and outstanding at September 30, 2016 and June 30, 2016, respectively	7,487	8,089
Non-voting common stock, $1.00 par value, 3,000,000 shares authorized; 1,343,683 and 1,227,683 shares issued and outstanding at September 30, 2016 and June 30, 2016, respectively	1,344	1,228
Additional paid-in capital	76,765	83,020
Retained earnings	27,818	26,160
Accumulated other comprehensive loss	(1,861)	(1,906)
Total shareholders' equity	111,553	116,591
Total liabilities and shareholders' equity	$ 985,568	$ 986,153

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 September 30, 2016	Three Months Ended September 30, 2015
Interest and dividend income:		
Interest and fees on loans	$11,803	$10,790
Interest on available-for-sale securities	239	228
Other interest and dividend income	215	95
Total interest and dividend income	12,257	11,113
Interest expense:		
Deposits	1,754	1,365
Federal Home Loan Bank advances	255	260
Wholesale repurchase agreements	-	67
Short-term borrowings	-	9
Subordinated debt	459	154
Obligation under capital lease agreements	14	17
Total interest expense	2,482	1,872
Net interest and dividend income before provision for loan losses	9,775	9,241
Provision for loan losses	193	169
Net interest and dividend income after provision for loan losses	9,582	9,072
Noninterest income:		
Fees for other services to customers	408	408
Gain on sales of residential loans held for sale	542	560
Gain on sales of SBA loans	743	675
Loss recognized on real estate owned and other repossessed collateral, net	(14)	(59)
Bank-owned life insurance income	114	112
Other noninterest income	15	9
Total noninterest income	1,808	1,705
Noninterest expense:		
Salaries and employee benefits	5,314	4,256
Occupancy and equipment expense	1,229	1,290

Professional fees	496	430
Data processing fees	421	349
Marketing expense	87	70
Loan acquisition and collection expense	227	451
FDIC insurance premiums	124	114
Intangible asset amortization	109	131
Other noninterest expense	619	719
Total noninterest expense	8,626	7,810
Income before income tax expense	2,764	2,967
Income tax expense	1,013	1,100
Net income	$1,751	$1,867
Weighted-average shares outstanding:		
Basic	9,106,144	9,562,812
Diluted	9,133,383	9,562,812
Earnings per common share:		
Basic	$0.19	$0.20
Diluted	0.19	0.20
Cash dividends declared per common share	$0.01	$0.01

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 September 30,	
	2016	2015
Net income	$1,751	$1,867
Other comprehensive income (loss), before tax:		
Available-for-sale securities:		
Change in net unrealized (loss) gain on available-for-sale securities	(78)	466
Derivatives and hedging activities:		
Change in accumulated gain (loss) on effective cash flow hedges	154	(838)
Reclassification adjustments included in net income	-	-
Total derivatives and hedging activities	154	(838)
Total other comprehensive income (loss), before tax	76	(372)
Income tax (benefit) expense related to other comprehensive loss	31	(141)
Other comprehensive income (loss), net of tax	45	(231)
Comprehensive income	$1,796	$1,636

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 SHAREHOLDERS' EQUITY

(Unaudited)

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

	Preferred Stock		Voting Common Stock		Non-voting Common Stock		Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Total Shareholders' Equity
	Shares	Amount	Shares	Amount	Shares	Amount				
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	-	-	-	-	-	-	-	1,867	-	1,867
Other comprehensive loss, net of tax	-	-	-	-	-	-	-	-	(231)	(231)
Common stock repurchased	-	-	(52,500)	(53)	-	-	(495)	-	-	(548)
Conversion of voting common stock to non-voting common stock	-	-	(9,978)	(10)	9,978	10	-	-	-	-
Dividends on common stock at $0.01 per share	-	-	-	-	-	-	-	(95)	-	(95)
Stock-based compensation	-	-	-	-	-	-	(16)	-	-	(16)
Issuance of restricted common stock	-	-	97,500	98	-	-	(98)	-	-	-
Cancellation and forfeiture of restricted common stock	-	-	(40,554)	(40)	-	-	40	-	-	-
Balance at September 30, 2015	-	$ -	8,569,612	$ 8,570	1,022,717	$ 1,023	$ 84,937	$ 20,693	$ (1,519)	$ 113,704

Balance at June 30, 2016	-	-	8,089,790	$ 8,089	1,227,683	$ 1,228	$ 83,020	$ 26,160	$ (1,906)	$ 116,591
Net income	-	-	-	-	-	-	-	1,751	-	1,751
Other comprehensive loss, net of tax	-	-	-	-	-	-	-	-	45	45
Common stock repurchased	-	-	(645,238)	(645)	-	-	(6,298)	-	-	(6,943)
Conversion of voting common stock to non-voting common stock	-	-	(116,000)	(116)	116,000	116	-	-	-	-
Dividends on common stock at $0.01 per share	-	-	-	-	-	-	-	(93)	-	(93)
Stock-based compensation	-	-	-	-	-	-	202	-	-	202
Issuance of restricted common stock	-	-	160,000	160	-	-	(160)	-	-	-
Cancellation and forfeiture of restricted common stock	-	-	(1,000)	(1)	-	-	1	-	-	-
Balance at September 30, 2016	-	$ -	7,487,552	$ 7,487	1,343,683	$ 1,344	$ 76,765	$ 27,818	$ (1,861)	$ 111,553

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)

	Three Months Ended September 30,	
	2016	2015
Operating activities:		
Net income	$1,751	$1,867
Adjustments to reconcile net income to net cash used in operating activities:		
Provision for loan losses	193	169
Loss on sale and impairment of real estate owned and other repossessed collateral, net	13	53
Loss on sale and disposal of premises and equipment, net	1	6
Accretion of fair value adjustments on loans, net	(2,133)	(2,248)
Accretion of fair value adjustments on deposits, net	(1)	(3)
Accretion of fair value adjustments on borrowings, net	(29)	(18)
Amortization of subordinated debt issuance costs	62	-
Originations of loans held for sale	(33,459)	(26,877)
Net proceeds from sales of loans held for sale	33,758	35,318
Gain on sales of residential loans held for sale	(542)	(560)
Gain on sales of SBA loans held for sale	(743)	(675)
Amortization of intangible assets	109	131
Bank-owned life insurance income, net	(114)	(112)
Depreciation of premises and equipment	395	405
Stock-based compensation	202	(16)
Amortization of available-for-sale securities, net	286	222
Changes in other assets and liabilities:		
Other assets	(15)	521
Other liabilities	(345)	(3,059)
Net cash (used in) provided by operating activities	(611)	5,124
Investing activities:		
Purchases of available-for-sale securities	(9,056)	(5,000)
Proceeds from maturities and principal payments on available-for-sale securities	14,681	5,808
Loan purchases	(13,853)	(23,458)
Loan originations, principal collections, and purchased loan paydowns, net	(13,969)	5,712
Purchases and disposals of premises and equipment, net	(47)	(618)
Proceeds from sales of real estate owned and other repossessed collateral	67	642
Net cash used in investing activities	(22,177)	(16,914)
Financing activities:		
Net increase in deposits	4,978	18,722
Net increase (decrease) in short-term borrowings	-	130

Repurchase of common stock	(6,943)	(548)
Dividends paid on common stock	(93)	(95)
Repayment of wholesale repurchase agreements	-	(10,000)
Repayment of capital lease obligation	(62)	(56)
Net cash (used in) provided by financing activities	(2,120)	8,153
Net decrease in cash and cash equivalents	(24,908)	(3,637)
Cash and cash equivalents, beginning of period	151,157	89,850
Cash and cash equivalents, end of period	$126,249	$86,213
Supplemental schedule of noncash investing activities:		
Transfers from loans to real estate owned and other repossessed collateral	$2,188	$323

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

September 30, 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, 2016 (“Fiscal 2016”) included in the Company's Annual Report on Form 10-K filed with the Securities and Exchange Commission.

2. Recent Accounting Pronouncements

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. The Company is currently evaluating the impact of the adoption of ASU 2014-09 on its consolidated financial statements.

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. Early adoption is permitted for only one of the six amendments. 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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In June 2016, the FASB issued ASU 2016-13, *Financial Instruments – Credit Losses (Topic 326)* (“ASU 2016-13”). This update is intended to provide financial statement users with more decision-useful information about the expected credit losses on financial instruments and other commitments to extend credit held by a reporting entity at each reporting date. To achieve this objective, the amendments in this update replace the incurred loss impairment methodology in current US GAAP with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. This ASU will be effective for fiscal years beginning after December 15, 2019. Early adoption is available as of the fiscal year beginning after December 15, 2018. The Company is currently evaluating the impact of this ASU on its consolidated financial statements.

In August 2016, the FASB issued ASU 2016-15, *Statement of Cash Flows (Topic 230)* (“ASU 2016-15”). This update clarifies and provides guidance on several cash receipt and cash payment classification issues, including debt prepayment and extinguishment costs, settlement of zero-coupon debt instruments, contingent consideration payments made after a business combination, proceeds from the settlement of insurance claims, proceeds from the settlement of corporate-owned life insurance policies, including bank-owned life insurance policies, distributions received from equity method investees, beneficial interests in securitization transactions, and separately identifiable cash flows and application of the predominance principle. The amendments in this Update are effective for public business entities for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. Early adoption is permitted, including adoption in an interim period. 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.

	September 30, 2016			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(Dollars in thousands)			
U.S. Government agency securities	$48,856	$ 24	$ (31)	$48,849
Agency mortgage-backed securities	40,483	117	(29)	40,571
Other investment measured at net asset value	5,125	38	-	5,163
	$94,464	$ 179	$ (60)	$94,583

	June 30, 2016			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(Dollars in thousands)			
U.S. Government agency securities	$51,948	$ 98	$ -	$52,046
Agency mortgage-backed securities	43,330	90	(52)	43,368
Other investment measured at net asset value	5,097	61	-	5,158
	$100,375	$ 249	$ (52)	$100,572

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 months ended September 30, 2016 or 2015. At September 30, 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.

September 30, 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	$36,671	$ (31)	$-	$ -	$36,671	$ (31)
Agency mortgage-backed securities	2,082	(1)	15,780	(28)	17,862	(29)
Other investment measured at net asset value	-	-	-	-	-	-
	$38,753	$ (32)	$15,780	$ (28)	$54,533	$ (60)

	June 30, 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	$-	$ -	$-	$ -	$-	$ -
Agency mortgage-backed securities	-	-	25,350	(52)	25,350	(52)
Other investment measured at net asset value	-	-	-	-	-	-
	$-	$ -	$25,350	$ (52)	$25,350	$ (52)

There were no other-than-temporary impairment losses on securities during the three months ended September 30, 2016 or 2015.

At September 30, 2016, the Company had seven securities in a continuous loss position for greater than twelve months. At September 30, 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 September 30, 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 September 30, 2016, the Company does not intend to sell and it is not more likely than not that the Company will 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 are other-than-temporarily impaired at September 30, 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 underlying composition of such fund is primarily government agencies or other investment-grade investments. The effective duration of the investments is 4.67 years at September 30, 2016.

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The amortized cost and fair values of available-for-sale debt securities by contractual maturity are shown below as of September 30, 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	$-	$-
Due after one year through five years	48,856	48,849
Due after five years through ten years	18,104	18,217
Due after ten years	22,379	22,354
Total	$89,339	$89,420

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. As a result, if an ASC 310-30 loan is modified to be consistent with, or better than, the Company's expectations at acquisition, the modified 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.

	September 30, 2016			June 30, 2016		
	Originated	Purchased	Total	Originated	Purchased	Total
	(Dollars in thousands)					
Residential real estate	$90,230	$2,895	$93,125	$93,391	$2,559	$95,950
Home equity	17,098	-	17,098	18,012	-	18,012
Commercial real estate	218,236	231,317	449,553	189,616	236,952	426,568
Commercial and industrial	154,008	2,102	156,110	145,758	198	145,956
Consumer	5,532	-	5,532	5,950	-	5,950
Total loans	$485,104	$236,314	$721,418	$452,727	$239,709	$692,436

Total loans include deferred loan origination costs of $367 thousand and fees of $58 thousand as of September 30, 2016 and June 30, 2016, respectively.

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Past Due and Nonaccrual Loans

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

	September 30, 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	$75	$637	$ -	$ 2,367	$3,079	$87,151	$90,230	$3,273
Home equity	50	-	-	48	98	17,000	17,098	48
Commercial real estate	256	-	-	94	350	217,886	218,236	361
Commercial and industrial	-	-	-	-	-	154,008	154,008	347
Consumer	92	8	-	95	195	5,337	5,532	121
Total originated portfolio	473	645	-	2,604	3,722	481,382	485,104	4,150
Purchased portfolio:								
Residential real estate	1,108	-	-	-	1,108	1,787	2,895	1,107
Commercial and industrial	-	93	-	-	93	2,009	2,102	48
Commercial real estate	179	1,411	-	3,269	4,859	226,458	231,317	3,618
Total purchased portfolio	1,287	1,504	-	3,269	6,060	230,254	236,314	4,773
Total loans	$1,760	$2,149	$ -	$ 5,873	$9,782	$711,636	$721,418	$8,923

	June 30, 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	$302	$910	$ -	$ 1,555	$2,767	$90,624	$93,391	$2,613
Home equity	146	-	-	48	194	17,818	18,012	48
Commercial real estate	132	-	-	188	320	189,296	189,616	474
Commercial and industrial	-	-	-	15	15	145,743	145,758	17
Consumer	73	56	-	74	203	5,747	5,950	163
Total originated portfolio	653	966	-	1,880	3,499	449,228	452,727	3,315
Purchased portfolio:								
Residential real estate	-	-	-	-	-	2,559	2,559	1,125

Commercial and industrial	-	-	-	-	-	198	198	-
Commercial real estate	-	19	-	3,387	3,406	233,546	236,952	3,387
Total purchased portfolio	-	19	-	3,387	3,406	236,303	239,709	4,512
Total loans	$653	$985	$ -	$ 5,267	$6,905	$685,531	$692,436	$7,827

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 originated loans 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;
- 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; and

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 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.

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 September 30, 2016						
	Residential Real Estate	Commercial Real Estate	Commercial and Industrial	Consumer	Purchased	Unallocated	Total
	(Dollars in thousands)						
Beginning balance	$663	$ 1,195	$ 297	$ 62	$ 133	$ -	$2,350
Provision	(99)	226	17	24	25	-	193
Recoveries	2	-	5	11	-	-	18
Charge-offs	(25)	-	(1)	(29)	-	-	(55)
Ending balance	$541	$ 1,421	$ 318	$ 68	$ 158	$ -	$2,506

	Three Months Ended September 30, 2015						
	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	(21)	62	16	31	81	-	169
Recoveries	12	5	1	2	-	-	20
Charge-offs	-	(28)	-	(22)	-	-	(50)
Ending balance	$732	$ 733	$ 134	$ 46	$ 364	$ 56	$2,065

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

	September 30, 2016						
	Residential Real Estate	Commercial Real Estate	Commercial and Industrial	Consumer	Purchased	Unallocated	Total
	(Dollars in thousands)						
Allowance for loan losses:							
Individually evaluated	$326	$ 50	$ 2	$ 22	$ -	$ -	$400
Collectively evaluated	215	1,371	316	46	-	-	1,948
ASC 310-30	-	-	-	-	158	-	158
Total	$541	$ 1,421	$ 318	$ 68	$158	$ -	$2,506

Loans:							
Individually evaluated	$5,790	$ 1,565	$ 346	$ 330	$-	$ -	$8,031
Collectively evaluated	101,538	216,671	153,662	5,202	-	-	477,073
ASC 310-30	-	-	-	-	236,314	-	236,314
Total	$107,328	$ 218,236	$ 154,008	$ 5,532	$236,314	$ -	$721,418

	June 30, 2016						
	Residential Real Estate	Commercial Real Estate	Commercial and Industrial	Consumer	Purchased	Unallocated	Total
	(Dollars in thousands)						
Allowance for loan losses:							
Individually evaluated	$386	$ 59	$ 2	$ 23	$-	$ -	$470
Collectively evaluated	277	1,136	295	39	-	-	1,747
ASC 310-30	-	-	-	-	133	-	133
Total	$663	$ 1,195	$ 297	$ 62	$133	$ -	$2,350
Loans:							
Individually evaluated	$5,039	$ 1,686	$ 17	$ 362	$-	$ -	$7,104
Collectively evaluated	106,364	187,930	145,741	5,588	-	-	445,623
ASC 310-30	-	-	-	-	239,709	-	239,709
Total	$111,403	$ 189,616	$ 145,758	$ 5,950	$239,709	$ -	$692,436

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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.

	September 30, 2016			June 30, 2016		
	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	$4,268	$4,320	$ -	$3,192	$3,299	$ -
Consumer	228	263	-	257	282	-
Commercial real estate	443	445	-	451	453	-
Commercial and industrial	344	344	-	15	15	-
Purchased:						
Residential real estate	1,108	1,150	-	1,125	1,125	-
Commercial real estate	4,897	5,939	-	4,574	4,886	-
Commercial and industrial	48	88	-	-	-	-
Total	11,336	12,549	-	9,614	10,060	-
Impaired loans with a valuation allowance:						
Originated:						
Residential real estate	1,522	1,510	326	1,847	1,802	386
Consumer	102	114	22	105	112	23
Commercial real estate	1,122	1,114	50	1,235	1,223	59
Commercial and industrial	2	2	2	2	2	2
Purchased:						
Commercial real estate	1,574	1,865	111	1,484	1,812	66
Total	4,322	4,605	511	4,673	4,951	536
Total impaired loans	$15,658	$17,154	$ 511	$14,287	$15,011	$ 536

The following tables set forth information regarding interest income recognized on impaired loans.

Three Months Ended September 30,			
2016		2015	
Average Recorded Investment	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized
(Dollars in thousands)			

Impaired loans without a valuation allowance:				
Originated:				
Residential real estate	$3,730	$ 49	$2,520	$ 39
Consumer	243	3	290	5
Commercial real estate	447	8	1,200	7
Commercial and industrial	180	3	2	-
Purchased:				
Residential real estate	1,117	3	-	-
Commercial real estate	4,736	52	7,842	14
Commercial and industrial	24	-	-	-
Total	10,477	118	11,854	65
Impaired loans with a valuation allowance:				
Originated:				
Residential real estate	1,685	16	2,064	23
Consumer	104	2	23	1
Commercial real estate	1,179	18	924	12
Commercial and industrial	2	-	-	-
Purchased:				
Commercial real estate	1,529	17	1,976	36
Total	4,499	53		