WASHINGTON FEDERAL INC
Form 10-Q
August 07, 2012
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q
(Mark One)

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

For the quarterly period ended June 30, 2012
or

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

For the transition period from to
Commission file number 001-34654
WASHINGTON FEDERAL, INC.
(Exact name of registrant as specified in its charter)

Washington	91-1661606
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

425 Pike Street Seattle, Washington 98101
(Address of principal executive offices and zip code)
(206) 624-7930
(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report.)
Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No o
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files) Yes x No o
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	x	Accelerated filer	o
Non-accelerated filer	o	Smaller reporting company	o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes o No x
APPLICABLE ONLY TO CORPORATE ISSUERS
Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Title of class:	at August 3, 2012

Common stock, $1.00 par value	106,494,239

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WASHINGTON FEDERAL, INC. AND SUBSIDIARIES

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WASHINGTON FEDERAL, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION
(UNAUDITED)

	June 30, 2012	September 30, 2011
	(In thousands, except share data)	
ASSETS		
Cash and cash equivalents	$963,766	$816,002
Available-for-sale securities, including encumbered securities of $964,338 and $965,927, at fair value	3,626,115	3,255,144
Held-to-maturity securities, including encumbered securities of $34,433 and $45,086, at amortized cost	35,228	47,036
Loans receivable, net	7,616,205	7,935,877
Covered loans, net	302,681	382,183
Interest receivable	53,043	52,332
Premises and equipment, net	175,125	166,593
Real estate held for sale	107,457	159,829
Covered real estate held for sale	33,142	56,383
FDIC indemnification asset	97,380	101,634
FHLB stock	151,674	151,755
Intangible assets, net	256,431	256,271
Federal and state income taxes	2,514	—
Other assets	44,588	59,710
	$13,465,349	$13,440,749
LIABILITIES AND STOCKHOLDERS' EQUITY		
Liabilities		
Customer accounts		
Transaction deposit accounts	$2,868,442	$2,662,188
Time deposit accounts	5,814,739	6,003,715
	8,683,181	8,665,903
FHLB advances	1,957,146	1,962,066
Other borrowings	800,000	800,000
Advance payments by borrowers for taxes and insurance	24,313	39,548
Federal and State income taxes	—	1,535
Accrued expenses and other liabilities	67,428	65,164
	11,532,068	11,534,216
Stockholders' equity		
Common stock, $1.00 par value, 300,000,000 shares authorized; 129,936,563 and 129,853,534 shares issued; 106,884,239 and 108,976,410 shares outstanding	129,937	129,854
Paid-in capital	1,585,797	1,582,843
Accumulated other comprehensive income, net of taxes	62,736	85,789
Treasury stock, at cost; 23,052,324 and 20,877,124 shares	(298,972)	(268,665)
Retained earnings	453,783	376,712
	1,933,281	1,906,533
	$13,465,349	$13,440,749

SEE NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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WASHINGTON FEDERAL, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
(UNAUDITED)

	Quarter Ended June 30,		Nine Months Ended June 30,	
	2012	2011	2012	2011
	(In thousands, except per share data)			
INTEREST INCOME				
Loans	$118,115	$127,736	$369,366	$394,286
Mortgage-backed securities	25,101	30,529	80,079	80,386
Investment securities and cash equivalents	2,168	3,266	6,446	10,988
	145,384	161,531	455,891	485,660
INTEREST EXPENSE				
Customer accounts	20,903	27,581	66,868	89,765
FHLB advances and other borrowings	27,946	27,818	84,172	83,474
	48,849	55,399	151,040	173,239
Net interest income	96,535	106,132	304,851	312,421
Provision for loan losses	10,367	21,000	39,576	77,750
Net interest income after provision for loan losses	86,168	85,132	265,275	234,671
OTHER INCOME				
Gain on sale of investments	—	—	—	8,147
Other	3,590	4,277	13,263	13,067
	3,590	4,277	13,263	21,214
OTHER EXPENSE				
Compensation and benefits	19,281	18,471	58,141	54,018
Occupancy	3,952	3,628	11,977	10,780
FDIC insurance premiums	4,000	5,100	12,543	15,299
Other	8,730	6,975	24,479	21,677
	35,963	34,174	107,140	101,774
Gain (loss) on real estate acquired through foreclosure, net	1,146	(8,171)	(11,005)	(28,369)
Income before income taxes	54,941	47,064	160,393	125,742
Income tax provision	19,778	16,943	57,742	45,267
NET INCOME	$35,163	$30,121	$102,651	$80,475
PER SHARE DATA				
Basic earnings	$0.33	$0.27	$0.96	$0.72
Diluted earnings	0.33	0.27	0.96	0.72
Cash dividends per share	0.08	0.06	0.24	0.18
Basic weighted average number of shares outstanding	106,877,112	111,158,254	107,308,948	111,962,708
Diluted weighted average number of shares outstanding, including dilutive stock options	106,926,755	111,248,177	107,347,668	112,043,350

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WASHINGTON FEDERAL, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(UNAUDITED)

	Quarter Ended June 30,		Nine Months Ended June 30,	
	2012	2011	2012	2011
	(In thousands)			
Net income	$35,163	$30,121	$102,651	$80,475
Other comprehensive income (loss) net of tax:				
Net unrealized gain (loss) on available-for-sales securities, net of quarter-to-date tax of $1,422 and $14,154, and year-to-date tax of $13,394 and $4,498, respectively	(2,447)	24,360	(23,053)	(12,895)
Reclassification adjustment of net gain from sale of available-for-sale securities included in net income	—	—	—	5,153
Other comprehensive income (loss)	(2,447)	24,360	(23,053)	(7,742)
Comprehensive income	$32,716	$54,481	$79,598	$72,733

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WASHINGTON FEDERAL, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

	Nine Months Ended	
	June 30, 2012	June 30, 2011
	(In thousands)	
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$102,651	$80,475
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization (accretion) of fees, discounts, premiums and intangible assets, net	40,397	32,456
Cash received from FDIC under loss share	276	20,977
Depreciation	5,625	4,950
Stock option compensation expense	900	815
Provision for loan losses	39,576	77,750
Loss (gain) on real estate held for sale, net	(8,366)	20,222
Increase in accrued interest receivable	(460)	(2,853)
Increase in FDIC loss share receivable	(5,742)	(3,143)
Increase in income taxes payable	9,345	3,575
Decrease in other assets	15,908	11,671
Increase (decrease) in accrued expenses and other liabilities	1,229	(25,175)
Net cash provided by operating activities	201,339	221,720
CASH FLOWS FROM INVESTING ACTIVITIES		
Net principal collections (loan originations)	372,802	336,426
FHLB stock redemptions	1,830	—
Available-for-sale securities purchased	(1,499,227)	(1,279,983)
Principal payments and maturities of available-for-sale securities	1,065,254	485,597
Available-for-sale securities sold	3,500	131,361
Principal payments and maturities of held-to-maturity securities	11,899	31,383
Net cash received from acquisition	50,576	—
Proceeds from sales of real estate held for sale	138,689	63,575
Proceeds from sales of covered REO	28,343	—
Increase in intangible assets	(1,061)	—
Premises and equipment purchased	(14,157)	(7,695)
Net cash provided (used) by investing activities	158,448	(239,336)
CASH FLOWS FROM FINANCING ACTIVITIES		
Net decrease in customer accounts	(118,505)	(138,850)
Net decrease in borrowings	(22,595)	(2,551)
Proceeds from exercise of common stock options	199	1,045
Dividends paid on common stock	(25,580)	(20,232)
Treasury stock purchased	(30,307)	(36,620)
Decrease in advance payments by borrowers for taxes and insurance	(15,235)	(15,638)
Net cash used by financing activities	(212,023)	(212,846)
Increase (decrease) in cash and cash equivalents	147,764	(230,462)
Cash and cash equivalents at beginning of period	816,002	888,622
Cash and cash equivalents at end of period	$963,766	$658,160

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WASHINGTON FEDERAL, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS (CONTINUED)
(UNAUDITED)

	Nine Months Ended	
	June 30, 2012	June 30, 2011
	(In thousands)	
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION		
Non-cash investing activities		
Non-covered real estate acquired through foreclosure	$124,482	$64,873
Covered real estate acquired through foreclosure	13,094	46,008
Cash paid during the period for		
Interest	151,805	174,511
Income taxes	48,331	41,627
The following summarizes the non-cash activities related to acquisitions		
Fair value of assets acquired	$124,594	$—
Fair value of liabilities assumed	(154,493)	—
Net fair value of liabilities assumed	(29,899)	—

SEE NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

WASHINGTON FEDERAL, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
QUARTERS AND NINE MONTHS ENDED JUNE 30, 2012 AND 2011
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NOTE A – Summary of Significant Accounting Policies

The consolidated unaudited interim financial statements included in this report have been prepared by Washington Federal, Inc. ("Company"). The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America ("GAAP") requires management to make estimates and assumptions that affect amounts reported in the financial statements. Actual results could differ from these estimates. In the opinion of management, all adjustments (consisting only of normal recurring accruals) necessary for a fair presentation are reflected in the interim financial statements. The September 30, 2011 Consolidated Statement of Financial Condition was derived from audited financial statements.

The information included in this Form 10-Q should be read in conjunction with Company's 2011 Annual Report on Form 10-K ("2011 Form 10-K") as filed with the SEC. Interim results are not necessarily indicative of results for a full year.

Loans receivable – When a borrower defaults on a loan, the Company attempts to cure the deficiency by working with the borrower. In most cases, deficiencies are cured promptly, sometimes as a result of a negotiated modification of terms. If the delinquency is not promptly cured, and negotiations do not lead to a modification of terms, the Company may institute appropriate legal action to collect the loan, which may include foreclosure of collateral. If foreclosed, the collateral is liquidated in a reasonable time frame at prices available in the market place.

The Company will consider modifying the interest rates and terms of a loan if it determines that a modification is a better alternative to foreclosure.

Loans are placed on nonaccrual status when, in the judgment of management, the probability of collection of interest is deemed to be insufficient to warrant further accrual. When a loan is placed on nonaccrual status, previously accrued but unpaid interest is deducted from interest income. The Company does not accrue interest on loans 90 days past due or more. If payment is made on a loan so that the loan becomes less than 90 days past due, and the Company expects full collection of principal and interest, the loan is returned to full accrual status. Any interest ultimately collected is credited to income in the period of recovery. A loan is charged-off when the loss is estimable and it is confirmed that the borrower will not be able to meet its contractual obligations.

The Company maintains an allowance for loan losses to absorb losses inherent in the loan portfolio. The allowance is based on ongoing, quarterly assessments of the probable and estimable losses inherent in the loan portfolio. The Company's methodology for assessing the appropriateness of the allowance consists of two components, which include the general allowance and specific allowances.

The general loan loss allowance is established by applying a loss percentage factor to the different loan types. Management believes loan types are the most relevant factor to group loans for the allowance calculation as the risk characteristics in these groups are similar. The loss percentage factor is made up of 2 parts – the historical loss factor ("HLF") and the qualitative loss factor ("QLF"). The HLF takes into account historical charge-offs, while the QLF is determined by loan type and allows management to augment reserve levels to reflect the current environment and portfolio performance trends including recent charge-off trends. The allowances are provided based on Management's continuing evaluation of the pertinent factors underlying the quality of the loan portfolio, including changes in the size and composition of the loan portfolio, actual loan loss experience, current economic conditions, collateral values, geographic concentrations, seasoning of the loan portfolio, specific industry conditions, and the duration of the current business cycle. The recovery of the carrying value of loans is susceptible to future market conditions beyond the Company's control, which may result in losses or recoveries differing from those provided.

Specific allowances are established for loans which are individually evaluated, in cases where Management has identified weaknesses that it believes indicate the probability that a loss has been incurred.

Impaired loans consist of loans receivable that are not expected to have their principal and interest repaid in accordance with their contractual terms. Collateral dependent impaired loans are measured using the fair value of the collateral, less selling costs. Non-collateral dependent loans are measured at the present value of expected future cash flows.

The Company receives fees for originating loans in addition to various fees and charges related to existing loans, which may include prepayment charges, late charges and assumption fees. Deferred loan fees and costs are recognized over the life of the loans using the effective interest method.

Off-Balance-Sheet Credit Exposures – The only material off-balance-sheet credit exposure is loans in process ("LIP"), which had a balance at June 30, 2012, excluding covered loans, of $155,051,000. The Company estimates losses on LIP by including LIP

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with the related principal balance outstanding and then applying its general reserve methodology to the gross amount. Certain reclassifications have been made to the financial statements to conform prior periods to current classifications.

NOTE B - Acquisitions

Western National Bank
Effective December 16, 2011, Washington Federal, acquired certain assets and liabilities, including most of the loans and deposits, of Western National Bank, headquartered in Phoenix, Arizona (“WNB”) from the Federal Deposit Insurance Corporation (“FDIC”) in an FDIC assisted transaction. Under the terms of the Purchase and Assumption Agreement, the Company and the FDIC agreed to a discount of $53 million on net assets and no loss sharing provision or premium on deposits.

WNB operated three full-service offices in Arizona. The Company acquired certain assets with a book value of $177 million, including $143 million in loans and $7 million in foreclosed real estate, and selected liabilities with a book value of $153 million, including $136 million in deposits. Pursuant to the purchase and assumption agreement with the FDIC, the Company received a cash payment from the FDIC for $30 million.

The acquisition was accounted for under the acquisition method of accounting. The purchased assets and assumed liabilities were recorded at their respective acquisition date estimated fair values. The purchase accounting for acquired assets and liabilities were provisionally recorded at their estimated fair values as of the December 16, 2011 acquisition date. The initial accounting for acquired loans, real estate held for sale and deposits was incomplete as of December 31, 2011. The amounts recognized at December 31, 2011 were determined provisionally as the fair value analysis of those assets was incomplete as of December 31, 2011. These amounts have been retrospectively adjusted to reflect the completion of the fair value analysis during the quarter ended June 30, 2012. The adjustments recorded in the quarter ended June 30, 2012 were a decrease in acquired loans of $716,000, a decrease in real estate held for sale of $252,000 and an increase in other assets of $836,000 to reflect the core deposit intangible.

The operating results of the Company include the operating results produced by the acquired assets and assumed liabilities for the period December 16, 2011 to June 30, 2012.

The table below displays the amounts recognized as of the acquisition date for each major class of assets acquired and liabilities assumed:

	Received from FDIC	Fair Value Adjustments	Recorded by WAFD
	(In thousands)		
Assets:			
Cash and cash equivalents	$20,677	$—	$20,677
Available-for-sale securities	3,500	—	3,500
FHLB & FRB stock	1,744	4	1,748
Loans receivable, net	143,328	(49,637)	93,691
Interest receivable	251	—	251
Property and equipment, net	—	—	—
Real estate held for sale	7,149	(3,462)	3,687
Other assets	79	961	1,040
Total Assets	176,728	(52,134)	124,594
Liabilities:			
Customer accounts	135,783	—	135,783
FHLB advances	17,666	9	17,675
Other liabilities	40	995	1,035
Total Liabilities	153,489	1,004	154,493
Net assets (liabilities) acquired	$23,239	$(53,138)	$(29,899)
Aggregate fair value adjustments		$(53,138)	
Net liabilities acquired			$(29,899)
Cash received from the FDIC			29,899

South Valley Bancorp, Inc.

On April 4, 2012, the Company and South Valley Bancorp, Inc. (“South Valley”) announced the signing of a definitive merger agreement. The merger agreement calls for the merger of South Valley with and into the Company, followed by the merger of South Valley's wholly owned subsidiary, South Valley Bank & Trust, into the Company's wholly owned subsidiary, Washington Federal. Under the terms of the definitive merger agreement, each outstanding share of South Valley common stock will be converted into the right to receive: (i) 0.2962 of a share of the Company's common stock, (ii) a contingent cash payment equal to the pro rata portion of an earn-out from the net proceeds collected from a pool of specified assets of South Valley with a value of approximately $39 million as of March 31, 2012, and (iii) a contingent cash payment equal to the pro rata portion of the net proceeds, if any, received by South Valley from the sale of its trust business and/or wealth management business prior to the closing of the merger. Assuming a per share price of $16.88 for the Company's common stock, the aggregate value of the stock portion of the merger consideration is approximately $33.7 million. After consummation of the merger, the combined company will have 190 offices in eight western states with total assets of approximately $14.4 billion and total deposits of approximately $9.6 billion, based on financial results as of December 31, 2011. The merger is expected to close in the third calendar quarter of 2012, pending the receipt of all requisite regulatory approvals and the satisfaction of other customary closing conditions. On June 28, 2012, the shareholders of South Valley approved the merger transaction, with over 82% of the outstanding shares of South Valley common stock voting in favor of the merger.

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NOTE C – Dividends

On July 19, 2012, the Company paid its 118th consecutive quarterly cash dividend on common stock. Dividends per share were $.08 and $.06 for the quarters ended June 30, 2012 and 2011, respectively.

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NOTE D – Loans Receivable (excluding Covered Loans)

	June 30, 2012 (In thousands)			September 30, 2011		
Non-acquired loans						
Single-family residential	$5,904,805	74.0	%	$6,218,878	74.9	%
Construction - speculative	130,741	1.6		140,459	1.7	
Construction - custom	210,488	2.6		279,851	3.4	
Land - acquisition & development	135,392	1.7		200,692	2.4	
Land - consumer lot loans	145,129	1.8		163,146	2.0	
Multi-family	692,763	8.7		700,673	8.4	
Commercial real estate	310,588	3.9		303,442	3.7	
Commercial & industrial	148,577	1.9		109,332	1.3	
HELOC	113,559	1.4		115,092	1.4	
Consumer	68,202	0.9		67,509	0.8	
Total non-acquired loans	7,860,244	98.5		8,299,074	100	
Credit-impaired acquired loans						
Single-family residential	343	—		—	—	
Construction - speculative	1,889	—		—	—	
Construction - custom	—	—		—	—	
Land - acquisition & development	4,211	0.1		—	—	
Land - consumer lot loans	—	—		—	—	
Multi-family	1,074	—		—	—	
Commercial real estate	91,006	1.1		—	—	
Commercial & industrial	5,100	0.1		—	—	
HELOC	15,037	0.2		—	—	
Consumer	115	—		—	—	
Total credit-impaired acquired loans	118,775	1.5		—	—	
Total loans						
Single-family residential	5,905,148	74.0		6,218,878	74.9	
Construction - speculative	132,630	1.7		140,459	1.7	
Construction - custom	210,488	2.6		279,851	3.4	
Land - acquisition & development	139,603	1.7		200,692	2.4	
Land - consumer lot loans	145,129	1.8		163,146	2	
Multi-family	693,837	8.7		700,673	8.4	
Commercial real estate	401,594	5.1		303,442	3.7	
Commercial & industrial	153,677	1.9		109,332	1.3	
HELOC	128,596	1.6		115,092	1.4	
Consumer	68,317	0.9		67,509	0.8	
Total loans	7,979,019	100	%	8,299,074	100	%
Less:						
Allowance for probable losses	137,951			157,160		
Loans in process	155,051			170,229		
Discount on acquired loans	35,200			—		

Deferred net origination fees	34,612	35,808
	362,814	363,197
	$7,616,205	$7,935,877

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The following table presents the changes in the accretable yield for credit impaired acquired loans as of June 30, 2012:

	Credit impaired acquired loans	
	Accretable Yield	Carrying Amount of Loans
	(In thousands)	
Balance as of October 1, 2011	$—	$—
Additions	21,606	92,981
Accretion	(3,278)	3,278
Transfers to REO	—	—
Payments received, net	—	(12,714)
Balance as of June 30, 2012	$18,328	$83,545

The following table sets forth information regarding non-accrual loans held by the Company as of the dates indicated:

	June 30, 2012		September 30, 2011	
	(In thousands)			
Non-accrual loans:				
Single-family residential	$129,295	75.6%	$126,624	60.3%
Construction - speculative	12,424	7.3	15,383	7.3
Construction - custom	539	0.3	635	0.3
Land - acquisition & development	12,514	7.3	37,339	17.7
Land - consumer lot loans	5,844	3.4	8,843	4.2
Multi-family	3,405	2.0	7,664	3.6
Commercial real estate	6,285	3.7	11,380	5.4
Commercial & industrial	—	—	1,679	0.8
HELOC	388	0.2	481	0.2
Consumer	339	0.2	437	0.2
Total non-accrual loans	$171,033	100%	$210,465	100%

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The following tables provide an analysis of the age of loans in past due status as of June 30, 2012 and September 30, 2011, respectively.

June 30, 2012 Type of Loan	Amount of Loans Net of LIP & Chg.-Offs (In thousands)	Days Delinquent Based on $ Amount of Loans Current	30	60	90	Total	% based on $	
Non-acquired loans								
Single-Family Residential	$5,902,633	$5,736,969	$33,571	$19,127	$112,966	$165,664	2.81	%
Construction - Speculative	94,930	87,134	899	509	6,388	7,796	8.21	
Construction - Custom	123,965	123,382	1	43	539	583	0.47	
Land - Acquisition & Development	127,953	114,563	234	3,226	9,930	13,390	10.46	
Land - Consumer Lot Loans	145,037	136,545	1,753	895	5,844	8,492	5.86	
Multi-Family	675,334	670,859	569	594	3,312	4,475	0.66	
Commercial Real Estate	305,046	300,668	334	—	4,044	4,378	1.44	
Commercial & Industrial	148,565	148,546	9	10	—	19	0.01	
HELOC	113,559	112,824	29	318	388	735	0.65	
Consumer	68,202	66,222	1,117	524	339	1,980	2.90	
Total non-acquired loans	7,705,224	7,497,712	38,516	25,246	143,750	207,512	2.69	
Credit-impaired acquired loans								
Single-Family Residential	343	—	—	343	—	343	100.00	
Construction - Speculative	1,889	1,889	—	—	—	—	—	
Construction - Custom	—	—	—	—	—	—	—	
Land - Acquisition & Development	4,210	3,685	—	—	525	525	12.47	
Land - Consumer Lot Loans	—	—	—	—	—	—	—	
Multi-Family	1,074	1,074	—	—	—	—	—	
Commercial Real Estate	90,977	80,860	2,072	1,698	6,347	10,117	11.12	
Commercial & Industrial	5,099	4,244	125	730	—	855	16.77	
HELOC	15,037	13,912	1,125	—	—	1,125	7.48	
Consumer	115	69	5	40	1	46	40.00	
Total credit-impaired acquired loans	118,744	105,733	3,327	2,811	6,873	13,011	10.96	

Total loans	$7,823,968		$7,603,445	$41,843	$28,057	$150,623	$220,523	2.82

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September 30, 2011	Amount of Loans	Days Delinquent Based on $ Amount of Loans					% based
Type of Loan	Net of LIP & Chg.-Offs	Current	30	60	90	Total	on $
	(In thousands)						
Single-Family Residential	$6,217,670	$6,015,464	$54,140	$21,985	$126,082	$202,207	3.25 %
Construction - Speculative	115,409	106,843	330	—	8,236	8,566	7.42
Construction - Custom	147,764	147,129	—	—	635	635	0.43
Land - Acquisition & Development	193,613	159,357	679	—	33,577	34,256	17.69
Land - Consumer Lot Loans	163,146	151,849	1,163	1,291	8,843	11,297	6.92
Multi-Family	699,340	690,765	—	1,202	7,373	8,575	1.23
Commercial Real Estate	300,307	292,015	1,016	—	7,276	8,292	2.76
Commercial & Industrial	108,995	106,708	55	553	1,679	2,287	2.10
HELOC	115,092	114,059	452	100	481	1,033	0.90
Consumer	67,509	65,434	1,191	446	437	2,074	3.07
	$8,128,845	$7,849,623	$59,026	$25,577	$194,619	$279,222	3.43

Most loans restructured in troubled debt restructurings ("TDRs") are accruing and performing loans where the borrower has proactively approached the Company about modification due to temporary financial difficulties. Each request is individually evaluated for merit and likelihood of success. The concession for these loans is typically a payment reduction through a rate reduction of between 100 to 200 basis points for a specific term, usually six to twelve months. Interest-only payments may also be approved during the modification period. Principal forgiveness is not an available option for restructured loans. As of June 30, 2012, single-family residential loans comprised 83.2% of TDRs.

The Company reserves for restructured loans within its allowance for loan loss methodology by taking into account the following performance indicators: 1) time since modification, 2) current payment status and 3) geographic area.

The following tables provide information related to loans that were restructured during the periods indicated:

	Quarter Ended June 30,					
	2012			2011		
	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
		(In thousands)			(In thousands)	
Troubled Debt Restructurings:						
Single-Family Residential	199	$43,104	$ 43,104	155	$39,362	$ 39,362

Construction - Speculative	—	—	—	1	337	337
Construction - Custom	1	1,196	1,196	—	—	—
Land - Acquisition & Development	—	—	—	3	4,427	4,427
Land - Consumer Lot Loans	8	965	965	9	1,335	1,335
Multi-Family	1	389	389	1	985	985
Commercial Real Estate	2	5,572	5,572	—	—	—
Commercial & Industrial	—	—	—	—	—	—
HELOC	2	113	113	—	—	—
Consumer	—	—	—	—	—	—
	213	$51,339	$ 51,339	169	$46,446	$ 46,446

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	Nine Months Ended June 30, 2012			2011		
	Number of Contracts	Pre-Modification Outstanding Recorded Investment (In thousands)	Post-Modification Outstanding Recorded Investment	Number of Contracts	Pre-Modification Outstanding Recorded Investment (In thousands)	Post-Modification Outstanding Recorded Investment
Troubled Debt Restructurings:						
Single-Family Residential	681	$159,651	$ 159,651	481	$131,018	$ 131,018
Construction - Speculative	22	6,253	6,253	2	529	529
Construction - Custom	1	1,196	1,196	—	—	—
Land - Acquisition & Development	26	5,565	5,565	3	4,427	4,427
Land - Consumer Lot Loans	30	3,906	3,906	34	5,175	5,175
Multi-Family	3	2,257	2,257	7	9,146	9,146
Commercial Real Estate	3	5,881	5,881	—	—	—
Commercial & Industrial	1	2	2	—	—	—
HELOC	2	113	113	—	—	—
Consumer	—	—	—	—	—	—
	769	$184,824	$ 184,824	527	$150,295	$ 150,295

The following tables provide information on restructured loans for which a payment default occurred during the periods indicated and that had been modified as a TDR within 12 months or less of the payment default:

	Quarter Ended June 30, 2012		2011	
	Number of Contracts	Recorded Investment (In thousands)	Number of Contracts	Recorded Investment (In thousands)
Troubled Debt Restructurings That Subsequently Defaulted:				
Single-Family Residential	30	$8,225	10	$3,295
Construction - Speculative	—	—	—	—
Construction - Custom	—	—	—	—
Land - Acquisition & Development	—	—	—	—
Land - Consumer Lot Loans	—	—	3	404

Multi-Family	—	—	1	3,589
Commercial Real Estate	—	—	—	—
Commercial & Industrial	—	—	—	—
HELOC	—	—	—	—
Consumer	—	—	—	—
	30	$8,225	14	$7,288

	Nine Months Ended June 30,			
	2012		2011	
	Number of Contracts	Recorded Investment (In thousands)	Number of Contracts	Recorded Investment (In thousands)
Troubled Debt Restructurings That Subsequently Defaulted:				
Single-Family Residential	97	$21,687	29	$7,783
Construction - Speculative	—	—	—	—
Construction - Custom	—	—	—	—
Land - Acquisition & Development	—	—	—	—
Land - Consumer Lot Loans	4	603	3	404
Multi-Family	—	—	1	3,589
Commercial Real Estate	—	—	—	—
Commercial & Industrial	—	—	—	—
HELOC	—	—	—	—
Consumer	—	—	—	—
	101	$22,290	33	$11,776

NOTE E – Allowance for Losses on Loans

The Company has an asset quality review function that analyzes its loan portfolios and reports the results of the review to the Board of Directors on a quarterly basis. The single-family residential, HELOC and consumer portfolios are evaluated based on their performance as a pool of loans, since no single loan is individually significant or judged by its risk rating, size or potential risk of loss. The construction, land, multi-family, commercial real estate and commercial and industrial loans are risk rated on a loan by loan basis to determine the relative risk inherent in specific borrowers or loans. Based on that risk rating, the loans are assigned a grade and classified as follows:

- Pass – the credit does not meet one of the definitions below.
- Special mention – A special mention credit is considered to be currently protected from loss but is potentially weak. No loss of principal or interest is foreseen; however, proper supervision and Management attention is required to deter further deterioration in the credit. Assets in this category constitute some undue and unwarranted credit risk but not to the point of justifying a risk rating of substandard. The credit risk may be relatively minor yet constitutes an unwarranted risk in light of the circumstances surrounding a specific asset.
- Substandard – A substandard credit is an unacceptable credit. Additionally, repayment in the normal course is in jeopardy due to the existence of one or more well defined weaknesses. In these situations, loss of principal is likely if the weakness is not corrected. A substandard asset is inadequately protected by the current sound worth and paying capacity of the borrower or of the collateral pledged, if any. Assets so classified will have a well defined weakness or weaknesses that jeopardize the liquidation of the debt. Loss potential, while existing in the aggregate amount of substandard assets, does not have to exist in individual assets risk rated substandard.
- Doubtful – A credit classified doubtful has all the weaknesses inherent in one classified substandard with the added characteristic that the weakness makes collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable and improbable. The probability of loss is high, but because of certain important and reasonably specific pending factors that may work to the advantage and strengthening of the asset, its classification as an estimated loss is deferred until its more exact status may be determined. Pending factors include proposed merger, acquisition, or liquidation procedures, capital injection, perfecting liens on additional collateral, and

refinancing plans.

- Loss – Credits classified loss are considered uncollectible and of such little value that their continuance as a bankable asset is not warranted. This classification does not mean that the asset has absolutely no recovery or salvage value, but rather it is not practical or desirable to defer writing off this asset even though partial recovery may be affected in the future. Losses should be taken in the period in which they are identified as uncollectible. Partial charge-off versus full charge-off may be taken if the collateral offers some identifiable protection.

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The following table summarizes the activity in the allowance for loan losses for the quarter ended June 30, 2012 and fiscal year ended September 30, 2011:

Quarter Ended June 30, 2012	Beginning Allowance	Charge-offs	Recoveries	Provision & Transfers	Ending Allowance
	(In thousands)				
Single-family residential	$83,875	$(14,134)	$2,240	$9,363	$81,344
Construction - speculative	15,943	(2,288)	86	(888)	12,853
Construction - custom	384	—	—	(40)	344
Land - acquisition & development	19,929	(1,519)	533	(1,549)	17,394
Land - consumer lot loans	7,712	(670)	—	295	7,337
Multi-family	4,837	—	279	(278)	4,838
Commercial real estate	2,869	(206)	148	337	3,148
Commercial & industrial	4,427	(69)	70	2,535	6,963
HELOC	969	(147)	6	144	972
Consumer	2,874	(955)	391	448	2,758
	$143,819	$(19,988)	$3,753	$10,367	$137,951
Fiscal Year Ended September 30, 2011	**Beginning Allowance**	**Charge-offs**	**Recoveries**	**Provision & Transfers**	**Ending Allowance**
	(In thousands)				
Single-family residential	$47,160	$(38,465)	$3,072	$71,540	$83,307
Construction - speculative	26,346	(13,197)	2,143	(1,464)	13,828
Construction - custom	770	(237)	—	90	623
Land - acquisition & development	61,637	(39,797)	2,271	8,608	32,719
Land - consumer lot loans	4,793	(4,196)	—	4,923	5,520
Multi-family	5,050	(1,950)	71	4,452	7,623
Commercial real estate	3,165	(1,593)	328	2,431	4,331
Commercial & industrial	6,193	(4,733)	1,925	1,714	5,099
HELOC	586	(939)	185	1,307	1,139
Consumer	7,394	(4,602)	1,429	(1,250)	2,971
	$163,094	$(109,709)	$11,424	$92,351	$157,160

The Company recorded a $10,367,000 provision for loan losses during the quarter ended June 30, 2012, while a $21,000,000 provision was recorded for the same quarter one year ago. Non-performing assets (“NPAs”) amounted to $278,490,000, or 2.07%, of total assets at June 30, 2012, compared to $394,679,000, or 2.96%, of total assets one year ago. Acquired loans, including covered loans, are not classified as non-performing loans because, at acquisition, the carrying value of these loans was adjusted to reflect fair value. There was no additional provision for loan losses recorded on acquired or covered loans during the quarter ended June 30, 2012. Non-accrual loans decreased from $232,752,000 at June 30, 2011, to $171,033,000 at June 30, 2012, a 26.5% decrease. The Company had net charge-offs of $16,235,000 for the quarter ended June 30, 2012, compared with $23,519,000 of net charge-offs for the same quarter one year ago. A loan is charged-off when the loss is estimable and it is confirmed that the borrower will not be able to meet its contractual obligations. The percentage of loans 30 days or more delinquent decreased from 3.66% at June 30, 2011, to 2.69% at June 30, 2012. Delinquencies in the single-family residential portfolio, the largest portion of the loan portfolio, decreased from 3.43% at June 30, 2011, to 2.81% at June 30, 2012. In addition to these improving asset quality trends, real estate values are beginning to increase in most of the Company's primary markets. As a result, the Company recorded a smaller provision for loan losses in the current quarter as compared to the same quarter one year ago. $116,164,000 of the allowance was calculated under the formulas contained in our general allowance methodology and the remaining $21,787,000 was made up of specific reserves on loans that were deemed to be impaired at June 30, 2012. For the period ending June 30, 2011,

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$114,159,000 of the allowance was calculated under the formulas contained in our general allowance methodology and the remaining $46,940,000 was made up of specific reserves on loans that were deemed to be impaired. The primary reasons for the shift in total allowance allocation from specific reserves to general reserves is due to the Company having already addressed many of the problem loans focused in the speculative construction and land A&D portfolios, combined with a still weak macro economic environment which may negatively impact the single-family residential portfolio.

The following tables shows a summary of loans collectively and individually evaluated for impairment and the related allocation of general and specific reserves as of June 30, 2012 and September 30, 2011:

June 30, 2012	Loans Collectively Evaluated for Impairment			Loans Individually Evaluated for Impairment		
	General Reserve Allocation	Gross Loans Subject to General Reserve (1)	Ratio	Specific Reserve Allocation	Gross Loans Subject to Specific Reserve (1)	Ratio
	(In thousands)			(In thousands)		
Single-family residential	$80,437	$ 5,823,964	1.4 %	$907	$ 80,842	1.1 %
Construction - speculative	8,615	98,980	8.7	4,238	31,760	13.3
Construction - custom	344	210,488	0.2	—	—	—
Land - acquisition & development	5,777	40,803	14.2	11,617	94,589	12.3
Land - consumer lot loans	6,447	142,712	4.5	890	2,417	36.8
Multi-family	2,728	671,837	0.4	2,110	20,927	10.1
Commercial real estate	1,136	286,779	0.4	2,012	23,808	8.5
Commercial & industrial	6,950	147,394	4.7	13	1,183	1.1
HELOC	972	113,559	0.9	—	—	—
Consumer	2,758	68,202	4.0	—	—	—
	$116,164	$ 7,604,718	1.5	$21,787	$ 255,526	8.5

(1) Excludes acquired and covered loans

September 30, 2011	Loans Collectively Evaluated for Impairment			Loans Individually Evaluated for Impairment		
	General Reserve Allocation	Gross Loans Subject to General Reserve (1)	Ratio	Specific Reserve Allocation	Gross Loans Subject to Specific Reserve (1)	Ratio
	(In thousands)			(In thousands)		
Single-family residential	$77,441	$ 6,186,322	1.3 %	$5,866	$ 32,556	18.0 %
Construction - speculative	6,969	89,986	7.7	6,859	50,473	13.6
Construction - custom	623	279,851	0.2	—	—	—
Land - acquisition & development	10,489	61,277	17.1	22,230	139,415	15.9
Land - consumer lot loans	4,385	160,906	2.7	1,135	2,240	50.7
Multi-family	3,443	679,823	0.5	4,180	20,850	20.0
Commercial real estate	2,730	268,906	1.0	1,601	34,536	4.6
Commercial & industrial	5,058	106,406	4.8	41	2,926	1.4

HELOC	1,139	115,092	1.0	—	—	—
Consumer	2,971	67,509	4.4	—	—	—
	$115,248	$ 8,016,078	1.4	$41,912	$ 282,996	14.8

(1) Excludes covered loans

The following tables provide information on loans based on credit quality indicators (defined in Note A) as of June 30, 2012 and

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September 30, 2011:
Credit Risk Profile by Internally Assigned Grade (excludes covered loans):

June 30, 2012	Internally Assigned Grade					Total
	Pass	Special mention	Substandard	Doubtful	Loss	Gross Loans
	(In thousands)					
Non-acquired loans						
Single-family residential	$5,714,905	$ 299	$189,601	$—	$—	$5,904,805
Construction - speculative	80,542	6,695	43,504	—	—	130,741
Construction - custom	210,488	—	—	—	—	210,488
Land - acquisition & development	42,907	21,935	70,550	—	—	135,392
Land - consumer lot loans	144,658	356	115	—	—	145,129
Multi-family	660,948	7,574	24,241	—	—	692,763
Commercial real estate	271,050	4,608	34,930			