Citizens Community Bancorp Inc.
Form 10-Q
February 14, 2011

UNITED STATES
SECURIT1ES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)
xQUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended December 31, 2010

OR

oTRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from __________________________ to__________________________

Commission file number 001-33003

CITIZENS COMMUNITY BANCORP, INC.
(Exact name of registrant as specified in its charter)

Maryland	20-5120010
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification Number)

2174 EastRidge Center, Eau Claire, WI 54701
(Address of principal executive offices)

715-836-9994
(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 and 15(d) of the Securities Exchange Act of 1934 during the past 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 [ ]

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 small reporting company. See the definitions of "large accelerated filer, " "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act (Check one):

Large accelerated filer [ ]	Accelerated filer [ ]	Non-Accelerated filer [ ] (do not check if a smaller reporting company)	Smaller reporting company [X]

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

Yes [ ]　　No [X]

APPLICABLE ONLY TO CORPORATE ISSUERS

Indicate the number of shares outstanding of each of the registrant's classes of common stock, as of the latest practicable date:

At February 14, 2011 there were 5,113,258 shares of the registrant's common stock, par value $0.01 per share, outstanding.

CITIZENS COMMUNITY BANCORP, INC.

FORM 10-Q

DECEMBER 31, 2010

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ITEM 1. FINANCIAL STATEMENTS

CITIZENS COMMUNITY BANCORP, INC.

Consolidated Balance Sheets
December 31, 2010 unaudited and September 30, 2010 derived from audited financial statements
(in thousands, except share data)

	December 31, 2010	September 30, 2010
Assets		
Cash and cash equivalents	$ 67,302	$ 72,438
Securities available-for-sale (at fair value)	40,856	41,708
Federal Home Loan Bank stock	5,787	5,787
Loans receivable	450,718	456,232
Allowance for loan losses	(4,412)	(4,145)
Loans receivable - net	446,306	452,087
Office properties and equipment - net	7,399	7,216
Accrued interest receivable	1,774	1,977
Intangible assets	732	815
Other assets	10,182	12,337
TOTAL ASSETS	$ 580,338	$ 594,365
Liabilities and Stockholders' Equity		
Liabilities:		
Deposits	$ 482,393	$ 476,302
Federal Home Loan Bank advances	42,800	64,200
Other liabilities	3,344	3,986
Total liabilities	528,537	544,488
Stockholders' equity:		
Common stock - 5,113,258 and 5,113,258 shares, respectively	51	51
Additional paid-in capital	53,823	53,823
Retained earnings	891	1,130
Unearned deferred compensation	-	(1)
Accumulated other comprehensive loss	(2,964)	(5,126)
Total stockholders' equity	51,801	49,877
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 580,338	$ 594,365

See accompanying condensed notes to consolidated financial statements.

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CITIZENS COMMUNITY BANCORP, INC.
Consolidated Statements of Operations - Unaudited
Three Months Ended December 31, 2010 and 2009
(in thousands, except per share data)

	Three Months Ended December 31, 2010	December 31, 2009
Interest and Dividend Income:		
Interest and fees on loans	$ 7,269	$ 7,348
Interest on investments	690	824
Total interest and dividend income	7,959	8,172
Interest expense:		
Interest on deposits	1,989	2,272
Interest on borrowed funds	607	921
Total interest expense	2,596	3,193
Net interest income	5,363	4,979
Provision for loan losses	1,600	760
Net interest income after provision for loan losses	3,763	4,219
Noninterest income:		
Total other-than-temporary impairment losses	(1,980)	(606)
Portion of loss recognized in other comprehensive loss (before tax)	1,410	22
Net impairment losses recognized in earnings	(570)	(584)
Service charges on deposit accounts	374	389
Insurance commissions	24	52
Loan fees and service charges	211	160
Other	2	2
Total noninterest income	41	19
Noninterest expense:		
Salaries and related benefits	2,017	1,885
Occupancy - net	643	612
Office	374	349
Data processing	59	98
Amortization of core deposit	83	83
Advertising, marketing and public relations	48	33
FDIC premium assessment	270	243
Professional services	287	305
Other	410	329
Total noninterest expense	4,191	3,937
Income (loss) before provision for income tax	(387)	301
Provision (benefit) for income taxes	(148)	126
Net income (loss) attibutable to common stockholders	$ (239)	$ 175
Per share information:		
Basic earnings	$ (0.05)	$ 0.03

Diluted earnings	$	(0.05)	$	0.03
Dividends paid	$	-	$	-

See accompanying condensed notes to consolidated financial statements.

CITIZENS COMMUNITY BANCORP, INC.
Consolidated Statements of
Changes in Stockholders' Equity and Comprehensive Gain - Unaudited
Three Months Ended December 31, 2010
(in thousands, except Shares)

	Common Stock		Additional Paid-in	Retained	Unearned	Accumulated Other Comprehensive Income	Total
	Shares	Amount	Capital	Earnings	Compensation	(loss)	Equity
Balance, September 30, 2010	5,113,258	$ 51	$ 53,823	$ 1,130	$ (1)	$ (5,126)	$ 49,877
Comprehensive gain (loss):							
Net loss				(239)			(239)
Amortization of unrecognized prior service costs and net gains/losses, net of tax						30	30
Net unrealized gain on available for sale securities, net of tax						1,790	1,790
Change for realized losses on securities available for sale for OTTI write-down, net of tax						342	342
Total comprehensive gain							1,923
Amortization of restricted stock					1		1
Balance, December 31, 2010	5,113,258	$ 51	$ 53,823	$ 891	$ -	$ (2,964)	$ 51,801

See accompanying condensed notes to unaudited, consolidated financial statements.

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CITIZENS COMMUNITY BANCORP, INC.

Consolidated Statements of Cash Flows - Unaudited
Three Months Ended December 31, 2010 and 2009
(in thousands, except per share data)

	Three Months Ended December 31, 2010	December 31, 2009
Cash flows from operating activities:		
Net income (loss) attributable to common stockholders	$(239)	$175
Adjustments to reconcile net loss to net cash provided by operating activities:		
Net securities amortization	(97)	(103)
Provision for depreciation	305	277
Provision for loan losses	1,600	760
Impairment on mortgage-backed securities	620	584
Amortization of core deposit intangible	83	83
Amortization of restricted stock	1	13
Provision for stock options	0	9
Provision (benefit) for deferred income taxes	0	143
(Increase) decrease in accrued interest receivable and other assets	903	(3,021)
Increase in other liabilities	(642)	(134)
Total adjustments	2,773	(1,389)
Net cash provided by (used in) operating activities	2,534	(1,214)
Cash flows from investing activities:		
Net decrease in interest-bearing deposits	0	1,213
Proceeds from principal repayments on securities available for sale	3,932	3,501
Net (increase) decrease in loans	4,194	(5,369)
Net capital expenditures	(487)	(82)
Net cash provided by (used in) investing activities	7,639	(737)
Cash flows from financing activities:		
Net (decrease) in borrowings	(21,400)	(5,105)
Net increase (decrease) in deposits	6,091	(3,361)
Net cash used in financing activities	(15,309)	(8,466)
Net decrease in cash and cash equivalents	(5,136)	(10,417)
Cash and cash equivalents at beginning	72,438	43,191
Cash and cash equivalents at end	$67,302	$32,774
Supplemental cash flow information:		
Cash paid during the year for:		
Interest on deposits	$1,992	$2,275
Interest on borrowings	$676	$997

Income taxes	$3	$-
Supplemental noncash disclosure:		
Transfers from loans to foreclosed properties	$192	$-

See accompanying condensed notes to consolidated financial statements.

CITIZENS COMMUNITY BANCORP, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

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

The financial statements of Citizens Community Federal (the “Bank”) included herein have been included by its parent company, Citizens Community Bancorp, Inc. (the “Company”), pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”). Citizens Community Bancorp (“CCB”) was a successor to Citizens Community Federal as a result of a regulatory restructuring into the mutual holding company form, which was effective on March 29, 2004. Originally, Citizens Community Federal was a credit union. In December 2001, Citizens Community Federal converted to a federal mutual savings bank. In 2004, Citizens Community Federal reorganized into the mutual holding company form of organization. In 2006, Citizens Community Bancorp completed its second-step mutual to stock conversion.

The consolidated income (loss) of the Company is principally derived from the Bank’s income (loss). The Bank originates residential and consumer loans and accepts deposits from customers, primarily in Wisconsin, Minnesota and Michigan. The Bank operates 26 full-service offices consisting of 7 stand-alone locations and 19 in-store branch locations.

The Bank is subject to competition from other financial institutions and non-financial institutions providing financial products. Additionally, the Bank is subject to the regulations of certain regulatory agencies and undergoes periodic examination by those regulatory agencies.

In preparing these financial statements, we evaluated the events and transactions that occurred through February 14, 2011, the date on which the financial statements were available to be issued. A subsequent event warranting disclosure is discussed in “Note 6 – Subsequent Event” in the “Condensed Notes to Consolidated Financial Statements”.

The accompanying interim financial statements are unaudited. However, in the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included.

Principles of Consolidation - The accompanying consolidated financial statements include the accounts of the Company and its wholly owned subsidiary, Citizens Community Federal. All significant inter-company accounts and transactions have been eliminated.

Use of Estimates - Preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (U.S. GAAP) requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying disclosures. These estimates are based on management’s knowledge of current events and actions the Company may undertake in the future. Estimates are used in accounting for, among other items, fair value of financial instruments, the allowance for loan losses, valuation of acquired intangible assets, useful lives for depreciation and amortization, future cash flows associated with impairment testing for goodwill, indefinite-lived intangible assets and long-lived assets, deferred tax assets, uncertain income tax positions and contingencies. Actual results may ultimately differ from estimates, although management does not generally believe such differences would materially affect the financial statements in any individual reporting period.

Securities – Securities are classified as available for sale when they might be sold before maturity. Securities available for sale are carried at fair value, with unrealized holding gains and losses and losses deemed other-than-temporarily impaired due to non-credit issues being reported in other comprehensive income, net of tax. Unrealized losses deemed other-than-temporarily impaired due to credit issues are reported in operations.

Interest income includes amortization of purchase premium or accretion of purchase discount. Amortization of premiums and accretion of discounts are recognized in interest income using the interest method over the estimated lives of the securities.

Declines in the fair value of securities below their cost that are other than temporary due to credit issues are reflected as “Net impairment losses recognized in earnings” in the statement of operations. In estimating other-than-temporary impairment, management considers: (1) the length of time and extent that fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, and (3) the Bank’s ability and intent to hold the security for a period sufficient to allow for any anticipated recovery in fair value. The difference between the present values of the cash flows expected to be collected and the amortized cost basis is the credit loss. The credit loss is the portion of the other-than-temporary impairment that is recognized in earnings and is a reduction to the cost basis of the security. The portion of other-than-temporary impairment related to all other factors is included in other comprehensive income (loss), net of the related tax effect.

Loans – Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are reported at the principal balance outstanding, net of unearned interest, deferred loan fees and costs, and an allowance for loan losses. Interest income is accrued on the unpaid principal balance. Loan origination fees, net of certain direct origination costs, are deferred and recognized in interest income using the level-yield method without anticipating prepayments.

Interest income on mortgage and consumer loans is discontinued at the time the loan is over 91 days delinquent. Past due status is based on the contractual terms of the loan. In all cases, loans are placed on nonaccrual or charged off at an earlier date if collection of principal or interest is considered doubtful. All interest accrued but not received for a loan placed on non-accrual is reversed against interest income. Interest received on such loans is accounted for on the cash basis or cost recovery method until qualifying for return to accrual status. Loans are returned to accrual status when payments are made that bring the loan account due date to less than 92 days delinquent. Interest on impaired loans considered troubled debt restructurings that are not more than 91 days delinquent is recognized as income as it accrues based on the revised terms of the loan.

Real estate loans and open ended consumer loans are charged off to estimated net realizable value less estimated selling costs at the earlier of when (a) the loan is deemed by management to be uncollectible, or (b) the loan becomes greater than 180 days past due. Closed end consumer loans are charged off to net realizable value at the earlier of when (a) the loan is deemed by management to be uncollectible, or (b) the loan becomes greater than 120 days past due.

Allowance for Loan Losses – The allowance for loan losses is a valuation allowance for probable and inherent credit losses. Loan losses are charged against the allowance for loan loss (“ALL”) when management believes that the collectability of a loan balance is unlikely. Subsequent recoveries, if any, are credited to the ALL. Management estimates the allowance balance required using past loan loss experience; the nature, volume and composition of the loan portfolio; known and inherent risks in the portfolio; information about specific borrowers’ ability to repay and estimated collateral values; current economic conditions; and other relevant factors. The ALL consists of specific and general components. The specific component relates to loans that are individually classified as impaired. The general component covers non-impaired loans and is based on historical loss experience adjusted for certain qualitative factors. The entire ALL balance is available for any loan that, in management’s judgment, should be charged off.

A loan is impaired when full payment under the loan terms is not expected. Troubled debt restructurings are individually evaluated for impairment. If a loan is impaired, a specific allowance is established so that the loan is reported, net, at the present value of estimated future cash flows using the loan’s existing rate or at the fair value of collateral if repayment is expected solely from the underlying collateral of the loan. Large groups of smaller balance homogeneous loans, such as non-classified consumer and residential real estate loans are collectively evaluated for impairment, and accordingly, are not separately identified for impairment disclosures.

The Bank manages its loan portfolio in two segments; real estate loans and consumer loans. Real estate loans are secured by single family or 1-4 family real estate, and include first and second mortgage loans along with home equity lines of credit. Consumer loans consist mainly of loans secured by personal property as collateral. Management believes that bifurcation of the Bank's loan portfolio into these two segments for credit quality, impairment and ALL disclosures provides the most meaningful presentation, consistent with how the portfolio is managed.

Income Taxes – The Company accounts for income taxes in accordance with ASC Topic 740, "Income Taxes". Under this guidance, deferred taxes are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates that will apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized as income or expense in the period that includes the enactment date. See Note 14 to the Company's consolidated financial statements included in the Company's Form 10-K/A filed with the Securities and Exchange Commission on January 11, 2011 for details on the Company's income taxes.

The Company regularly reviews the carrying amount of its deferred tax assets to determine if the establishment of a valuation allowance is necessary. If based on the available evidence, it is more likely than not that all or a portion of the Company's deferred tax assets will not be realized in future periods, a deferred tax valuation allowance would be established. Consideration is given to various positive and negative factors that could affect the realization of the deferred tax assets. In evaluating this available evidence, management considers, among other things, historical performance, expectations of future earnings, the ability to carry back losses to recoup taxes previously paid, length of statutory carry forward periods, experience with utilization of operating loss and tax credit carry forwards not expiring, tax planning strategies and timing of reversals of temporary differences. Significant judgment is required in assessing future earnings trends and the timing of reversals of temporary differences. The Company's evaluation is based on current tax laws as well as management's expectations of future performance.

Earnings Per Share – Basic earnings per common share is net income or loss divided by the weighted average number of common shares outstanding during the period. Diluted earnings per common share include the dilutive effect of additional potential common shares issuable during the period, consisting of stock options outstanding under the Company's stock incentive plan.

Reclassifications – Certain items previously reported were reclassified for consistency with the current presentation.

Adoption of New Accounting Standards - In July 2010, the FASB issued ASU 2010-20, "Receivables (Topic 310): Disclosure about Credit Quality of Financing Receivables and the Allowance for Credit Losses". The objective of this guidance is for an entity to provide disclosures that facilitate the evaluation of the nature of credit risk inherent in the entity's portfolio of financing receivables; how that risk is analyzed and assessed in arriving at the allowance for doubtful accounts; and the changes and reasons for those changes in the allowance for credit losses. To achieve those objectives, disclosures on a disaggregated basis shall be provided on two defined levels: (1) portfolio segment; and (2) class of financing receivable. This guidance makes changes to existing disclosure requirements and includes additional disclosure requirements relating to financing receivables. The guidance pertaining to disclosures as of the end of a reporting period became effective for the Company for interim and annual reporting periods ending on or after December 15, 2010. The guidance pertaining to disclosures about activity that occurs during a reporting period are effective for the Company for interim and annual reporting periods beginning on or after December 15, 2010. The provisions of this guidance did not have a material impact on the Company's consolidated financial condition, results of operations or liquidity.

In January 2010, the FASB issued ASU 2010-06, which provided updated guidance on fair value measurements and disclosures as set forth in ASC 820-10. The guidance requires companies to disclose transfers in and out of levels 1 and 2, and to expand the reconciliation of level 3 fair value measurements by presenting separately information about purchases, sales, issuances and settlements. The updated guidance also clarifies existing disclosure requirements on the level of disaggregation (provide fair value measurement disclosures for each class of assets and liabilities) and inputs and valuation techniques (required disclosure for fair value measurements that fall in either level 2 or level 3). This guidance was effective for interim and annual reporting periods beginning after December 15, 2009, except for disclosures about purchases, sales, issuances and settlements in the reconciliation of level 3 fair value measurements. Those disclosures regarding the reconciliation of level 3 fair value measurements became effective for periods beginning after December 15, 2010. The provisions of this guidance did not have a material impact on the Company's consolidated financial condition, results of operations or liquidity.

NOTE 2 – FAIR VALUE ACCOUNTING

ASC 820-10 establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The statement describes three levels of inputs that may be used to measure fair value:

Level 1- Quoted prices (unadjusted) for identical assets or liabilities in active markets that we have the ability to access as of the measurement date.

Level 2- Significant other observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

Level 3- Significant unobservable inputs that reflect our own assumptions about the assumptions that market participants would use in pricing an asset or liability.

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input within the valuation hierarchy that is significant to the fair value measurement.

The fair value of securities available for sale is determined by obtaining market price quotes from independent third parties wherever such quotes are available. Where such quotes are not available, we utilize independent third party valuation analyses to support our own estimates and judgments in determining fair value.

Assets Measured on a Recurring Basis

	Fair Value	Quoted Prices in Active Markets for Identical Instruments (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
December 31, 2010:				
Securities available for sale:				
U.S. Agency securities	$ 15,580	$ -	$ 15,580	$ -
Non-agency mortgage-backed securities	25,276	-	-	25,276
Total	$ 40,856	$ -	$ 15,580	$ 25,276
September 30, 2010:				
Securities available for sale:				
U.S. Agency securities	$ 16,709	$ -	$ 16,709	$ -
Non-agency mortgage-backed securities	24,999	-	-	24,999
Total	$ 41,708	$ -	$ 16,709	$ 24,999
		`		

Assets Measured on a Nonrecurring Basis

	Fair Value	Quoted Prices in Active Markets for Identical Instruments (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
December 31, 2010:				
Foreclosed assets	$ 519	$ -	$ -	$ 519
Loans restructured in a troubled debt restructuring	5,728	-	-	5,728
Total	$ 6,247	$ -	$ -	$ 6,247
September 30, 2010:				
Foreclosed assets	$ 448	$ -	$ -	$ 448
Loans restructured in a troubled debt restructuring	3,178	-	-	3,178
Total	$ 3,626	$ -	$ -	$ 3,626

Fair value of foreclosed assets is determined, initially, by a third-party appraisal. Subsequent to foreclosure, valuations are periodically performed by management to identify potential changes in fair value.

Level 3 assets measured on a recurring basis are certain investments for which little or no market activity exists or whose value of the underlying collateral is not market observable. Management's valuation uses both observable as well as unobservable inputs to assist in the Level 3 valuation of mortgage backed securities held by the Bank, employing a methodology that considers future cash flows along with risk-adjusted returns. The inputs in this methodology are as follows: ability and intent to hold to maturities, mortgage underwriting rates, market prices/conditions, loan type, loan-to-value, strength of borrower, loan age, delinquencies, prepayment/cash flows, liquidity, expected future cash flows, rating agency actions, and a discount rate, which is assumed to be approximately equal to the coupon rate for each security. We had an independent valuation of all Level 3 securities in the current quarter. Based on this valuation, we recorded pre-tax other than temporary impairment of $620 in the current quarter.

The fair value of foreclosed assets is determined by obtaining market price quotes from independent third parties wherever such quotes are available. Where such quotes are not available, we utilize independent third party appraisals to support our own estimates and judgments in determining fair value.

The following table presents a reconciliation of residential mortgage-backed securities held by the Bank measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the three month periods ended December 31, 2010 and 2009:

	Three Months Ended December 31, 2010	Three Months Ended December 31, 2009
Balance beginning of period	$24,999	$36,517
Total gains or losses (realized/unrealized):		
Included in earnings	(620)	(584)
Included in other comprehensive loss	3,632	(1,517)
Purchases, sales, issuances, and settlements, net	(2,735)	(2,711)
Balance end of period	$25,276	$31,705

Fair Values of Financial Instruments

ASC 825-10 and ASC 270-10, Interim Disclosures about Fair Value Financial Instruments, require disclosures about fair value financial instruments and significant assumptions used to estimate fair value. The estimated fair values of financial instruments not previously disclosed are as follows:

Cash and Cash Equivalents
Due to their short-term nature, the carrying amounts of cash and cash equivalents were considered to be a reasonable estimate of fair value.

Loans
Fair value is estimated for portfolios of loans with similar financial characteristics. Loans are segregated by type such as residential mortgage and consumer. The fair value of loans is calculated by discounting scheduled cash flows through the estimated maturity date using market discount rates reflecting the credit and interest rate risk inherent in the loan. The estimate of maturity is based on the Bank's repayment schedules for each loan classification.

Federal Home Loan Bank (FHLB) Stock
Federal Home Loan Bank Stock is carried at cost, which is its redeemable fair value since the market for the stock is restricted (See Note 8 to the Company's consolidated financial statements included in the Company's Form 10-K/A filed with the Securities and Exchange Commission on January 11, 2011).

Accrued Interest Receivable and Payable
Due to their short-term nature, the carrying amounts of accrued interest receivable, and payable, respectively, were considered to be a reasonable estimate of fair value.

Deposits
The fair value of deposits with no stated maturity, such as demand deposits, savings accounts, and money market accounts, is the amount payable on demand at the reporting date. The fair value of certificate accounts is calculated by

using discounted cash flows applying interest rates currently being offered on similar certificates.

Borrowed Funds
The fair value of long-term borrowed funds is estimated using discounted cash flows based on the Bank's current incremental borrowing rates for similar borrowing arrangements. The carrying value of short-term borrowing approximates its fair value.

Off-Balance-Sheet Instruments
The fair value of off-balance sheet commitments would be estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements, the current interest rates, and the present creditworthiness of the customers. Since this amount is immaterial to the Company, no amounts for fair value are presented.

The carrying amount and estimated fair value of financial instruments were as follows (000's):

	December 31, 2010		September 30, 2010	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Financial assets:				
Cash and cash equivalents	$67,302	$67,302	$72,438	$72,438
Interest-bearing deposits	-	-	-	-
Securities available for sale	40,856	40,856	41,708	41,708
Loans receivable	446,306	464,135	452,087	477,039
FHLB stock	5,787	5,787	5,787	5,787
Accrued interest receivable	1,774	1,774	1,977	1,977
Financial liabilities:				
Deposits	482,393	488,986	476,302	482,337
Borrowed funds	42,800	45,623	64,200	68,290
Accrued interest payable	$160	$160	$232	$232

NOTE 3 –LOANS, ALLOWANCE FOR LOAN LOSSES AND IMPAIRED LOANS

The Allowance for Loan Losses ("ALL") represents management's estimate of probable and inherent credit losses in the Bank's loan portfolio. Estimating the amount of the ALL requires the exercise of significant judgment and the use of estimates related to the amount and timing of expected future cash flows on impaired loans, estimated losses on pools of homogeneous loans based on historical loss experience, and consideration of other qualitative factors such as current economic trends and conditions, all of which may be susceptible to significant change. The loan portfolio also represents the largest asset on our consolidated balance sheet. Loan losses are charged off against the ALL, while recoveries of amounts previously charged off are credited to the ALL. A provision for loan losses is charged to operations based on management's periodic evaluation of the aforementioned specific factors as well as any other pertinent factors.

The ALL consists of a specific component on impaired loans and a general component for non-impaired loans. The components of the ALL represent estimations pursuant to either ASC 450-10, Accounting for contingencies, or ASC 310-10, Accounting by Creditors for Impairment of a Loan. The specific component of the ALL reflects estimated losses from analyses developed through review of individual loans deemed impaired. These analyses involve a high degree of judgment in estimating the amount of potential loss associated with specific loans, including estimating the amount and timing of future cash flows and collateral values. The general component of ALL is based on the Company’s historical loss experience which is updated quarterly. The general component of ALL also includes consideration for concentrations, changes in portfolio mix and volume and other qualitative factors.

There are many factors affecting the ALL; some are quantitative, while others require qualitative judgment. The process for determining the ALL (which management believes adequately considers potential factors which result in probable credit losses), includes subjective elements and, therefore, may be susceptible to significant change. To the extent actual outcomes differ from management estimates, additional provision for credit losses could be required that could adversely affect our earnings or financial position in future periods. Allocations of the ALL may be made for specific loans but the entire ALL is available for any loan that, in management’s judgment, should be charged-off or for which an actual loss is realized.

Changes in the ALL for the periods presented below were as follows (dollar amounts in thousands):

	Real Estate	Consumer	Total
December 31, 2010 and Three Months then Ended:			
Allowance for Loan Losses:			
Beginning balance	$ 1,562	$ 2,583	$ 4,145
Charge-offs	(423)	(983)	(1,406)
Recoveries	22	51	73
Provision (1)	481	1,119	1,600
Ending balance	$ 1,642	$ 2,770	$ 4,412
Ending balance: individually evaluated for impairment	$ 313	$ 322	$ 635
Ending balance: collectively evaluated for impairment	$ 1,329	$ 2,448	$ 3,777
Loans Receivable:			
Ending balance	$ 264,482	$ 186,236	$ 450,718
Ending balance: individually evaluated for impairment	$ 10,008	$ 3,534	$ 13,542
Ending balance: collectively evaluated for impairment	$ 254,474	$ 182,702	$ 437,176
September 30, 2010 and Twelve Months then Ended:			
Allowance for Loan Losses:			
Beginning balance	$ 846	$ 1,079	$ 1,925
Charge-offs	(1,331)	(3,445)	(4,776)
Recoveries	44	51	95
Provision (1)	2,003	4,898	6,901
Ending balance	$ 1,562	$ 2,583	$ 4,145
Ending balance: individually evaluated for impairment	$ 211	$ 522	$ 733
Ending balance: collectively evaluated for impairment	$ 1,351	$ 2,061	$ 3,412
Loans Receivable:			
Ending balance	$ 261,357	$ 194,875	$ 456,232
Ending balance: individually evaluated for impairment	$ 4,092	$ 4,560	$ 8,652
Ending balance: collectively evaluated for impairment	$ 257,265	$ 190,315	$ 447,580

(1) The Bank does not have historical data disaggregating provision for loan Losses between real estate and consumer loans. Therefore, provision for loan losses has been allocated between real estate and consumer loans for each period presented based on the ratio of real estate and consumer net loan charge-offs for that period.

The Bank has originated all loans currently recorded on its balance sheet. The Bank has not acquired any loans.

As an integral part of their examination process, various regulatory agencies review the ALL. Such agencies may require that changes in the ALL be recognized when such regulators' credit evaluations differ from those of management based on information available to the regulators at the time of their examinations.

Loans receivable as of the end of the periods shown below are as follows (dollar amounts in thousands):

	Real Estate Loans		Consumer Loans	
	December 31, 2010	September 30, 2010	December 31, 2010	September 30, 2010
Performing loans				
Performing TDR loans	$ 3,204	$ 2,714	$ 1,191	$ 559
Performing loans, other	254,475	255,110	182,702	192,765
Total performing loans	257,679	257,824	183,893	193,324
Nonperforming loans (1)				
Nonperforming TDR loans	1,748	-	179	-
Nonperforming loans, other	5,055	3,533	2,164	1,551
Total nonperforming loans	6,803	3,533	2,343	1,551
Total loans	$ 264,482	$ 261,357	$ 186,236	$ 194,875

(1) Nonperforming loans are defined as loans that (a) are 91+ days past due and nonaccruing, or (b) TDR loans restructured at a 0% interest rate that were 91+ days past due and nonaccruing at the time of restructuring.

Impaired loans with a valuation allowance based upon the fair value of the underlying collateral had a carrying amount of $2,759 at December 31, 2010 compared to $2,581 at September 30, 2010. The valuation allowance on impaired loans was $635 at December 31, 2010, compared to $733 at September 30, 2010.

An aging analysis of the Bank's real estate and consumer loans as of December 31, and September 30, 2010 is as follows:

	31-60 Days Past Due	61-90 Days Past Due	Greater Than 90 Days	Total Past Due	Current	Total Loans	Recorded Investment > 90 Days and Accruing
December 31, 2010:							
Real estate loans	$ 4,257	$ 425	$ 5,047	$ 9,729	$ 254,753	$ 264,482	$ -
Consumer loans	7,985	1,904	2,186	12,075	174,161	186,236	-
Total	$ 12,242	$ 2,329	$ 7,233	$ 21,804	$ 428,914	$ 450,718	$ -
September 30, 2010:							

Real estate loans	$ 5,144	$ 1,054	$ 3,322	$ 9,520	$ 251,837	$ 261,357	$ -
Consumer loans	9,064	2,550	3,535	15,149	179,726	194,875	-
Total	$ 14,208	$ 3,604	$ 6,857	$ 24,669	$ 431,563	$ 456,232	$ -

A summary of the Bank's impaired loans as of December 31, and September 30, 2010 is as follows:

	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
December 31, 2010 and Three Months then Ended:					
With no related allowance recorded:					
Real estate loans	$3,296	$3,296	$-	$1,648	$22
Consumer loans	309	309	-	$155	3
With an allowance recorded:					
Real estate loans	1,656	1,656	282	$828	4
Consumer loans	1,062	1,062	312	$531	7
Total:					
Real estate loans	$4,952	$4,952	$282	$2,476	$26
Consumer loans	$1,371	$1,371	$312	$686	$10
September 30, 2010 and Twelve Months then Ended:					
With no related allowance recorded:					
Real estate loans	$907	$907	$-	$937	$4
Consumer loans	211	211	-	$869	5
With an allowance recorded:					
Real estate loans	1,297	1,297	271	$1,884	3
Consumer loans	958	958	294	$2,418	18
Total:					
Real estate loans	$2,204	$2,204	$271	$2,820	$7
Consumer loans	$1,169	$1,169	$294	$3,286	$23

A summary of loans modified in a troubled debt restructuring as of December 31, 2010 and the three months then ended is as follows:

	December 31, 2010		
	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Troubled Debt Restructurings:			
Real estate loans	10	$ 945,504	$ 945,504
Consumer loans	9	171,365	171,365
Total	19	$ 1,116,869	$ 1,116,869

	Number of Contracts	Recorded Investment
Troubled Debt Restructurings That Subsequently Defaulted:		
Real estate loans	2	$ 233,199
Consumer loans	4	111,006
Total	6	$ 344,205

NOTE 4 – INVESTMENT SECURITIES

The amortized cost, estimated fair value and related unrealized gains and losses of securities available for sale as of December 31 and September 30, 2010, respectively, are as follows:

Description of Securities	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
December 31, 2010				
U.S. Agency securities	$ 15,140	$ 440	$ -	$ 15,580
Non-agency mortgage-backed securities	30,417	-	5,141	25,276
Total investment securities	$ 45,557	$ 440	$ 5,141	$ 40,856
September 30, 2010				
U.S. Agency securities	$ 16,240	$ 469	$ -	$ 16,709
Non-agency mortgage-backed securities	33,772	-	8,773	24,999
Total investment securities	$ 50,012	$ 469	$ 8,773	$ 41,708

We evaluate securities for other-than-temporary impairment at least on a quarterly basis, and more frequently when economic or market concerns warrant such evaluation. As part of such monitoring, the credit quality of individual securities and their issuers are assessed. Adjustments to market value that are considered temporary are recorded as separate components of equity, net of tax. If an impairment of a security is identified as other-than-temporary based on information available, such as the decline in the credit worthiness of the issuer, external market ratings, or the anticipated or realized elimination of associated dividends, such impairments are further analyzed to determine if credit loss exists. If there is a credit loss, it will be recorded in the Consolidated Statement of Operations. Losses other than credit will continue to be recognized in other comprehensive income (loss). Unrealized losses reflected in the preceding tables have not been included in results of operations because the unrealized loss was not deemed other-than-temporary. Management has determined that more likely than not, the Bank will not be required to sell the debt security before its anticipated recovery and therefore, there is no other-than-temporary impairment. The non-agency mortgage backed securities with continuous unrealized losses for twelve months or more consist of 14 specific securities.

There were no sales of available for sale securities during the three-month period ended December 31, 2010.

A summary of the amount of other-than-temporary impairment related to credit losses on available-for-sale securities that have been recognized in earnings follows:

	Three Months Ended December 31, 2010	Twelve Months Ended September 30, 2010
Beginning balance of the amount of OTTI related to credit losses	$ 9,497	$ 7,236
Credit portion of OTTI on securities for which OTTI was not previously recognized	620	2,276
Cash payments received on a security in excess of the security's book value adjusted for previously recognized credit portion of OTTI	(50)	(15)
Ending balance of the amount of OTTI related to credit losses	$ 10,067	$ 9,497

The Bank has pledged certain of its U.S. Agency securities as collateral against a borrowing line with the Federal Reserve Bank. However, as of December 31, 2010, there are no borrowings outstanding on the Federal Reserve line of credit.

NOTE 5 – STOCK-BASED COMPENSATION

In February 2005, our stockholders approved the Company's Recognition and Retention Plan. This plan provides for the grant of up to 113,910 shares of the Company's common stock to eligible participants under this plan. As of December 31, 2010, 70,615 restricted shares were issued and outstanding under this plan. During the quarter ended December 31, 2010 no shares were granted to eligible participants under this plan; and 9,338 of previously awarded shares were forfeited. Restricted shares are awarded at no cost to the employee and have a five-year vesting period. The fair value of the restricted shares on the date of award was $7.04 per share for 63,783 shares and $6.18 for 6,832 shares. Compensation expense related to these awards was $1 and $13 for the three months ended December 31, 2010 and 2009, respectively.

In February 2005, our stockholders also approved the Company's 2004 Stock Option and Incentive Plan. This plan provides for the grant of nonqualified and incentive stock options and stock appreciation rights to eligible participants under this plan. The plan provides for the grant of awards for up to 284,778 shares of the Company's common stock. At December 31, 2010, 202,197 options had been granted under this plan to eligible participants at a weighted-average exercise price of $7.04 per share. Options granted vest over a five-year period. Unexercised, nonqualified stock options expire within 15 years of the grant date and unexercised incentive stock options expire within 10 years of the grant date. Through December 31, 2010, since the plan’s inception, options for 113,915 shares of the Company's common stock were vested, options for 83,724 shares were forfeited and options for 4,558 shares were exercised. Of the 202,197 options granted, 113,915 remained outstanding as of December 31, 2010.

We account for stock-based employee compensation related to our 2004 Stock Option and Incentive Plan using the fair-value-based method. Accordingly, we record compensation expense based on the value of the award as measured on the grant date and recognize that cost over the vesting period for the award. The compensation cost recognized for stock-based employee compensation for the three month periods ended December 31, 2010 and 2009 were $0 and $10, respectively.

In February 2008, our stockholders approved the Company's 2008 Equity Incentive Plan. The aggregate number of shares of common stock reserved and available for issuance under the 2008 Equity Incentive Plan is 597,605 shares. Under the Plan, the Compensation Committee may grant stock options and stock appreciation rights that, upon exercise, result in the issuance of 426,860 shares of the Company's common stock. The Committee may grant restricted stock and restricted stock units for an aggregate of 170,745 shares of Company common stock under this plan. In October 2008, the Compensation Committee suspended consideration of distributions or awards under this plan, and as of December 31, 2010, no grants or awards have been made to eligible participants under the 2008 Equity Incentive Plan.

NOTE 6 – SUBSEQUENT EVENT

On February 2, 2011, the Bank sold four agency and 10 non-agency mortgage-backed securities (“MBS”) with an aggregate book value of approximately $25,000, resulting in a net realized gain of approximately $150. The sale was executed in order to (a) take advantage of current favorable market prices to minimize realized losses on certain non-agency MBS, (b) reduce the Bank’s exposure to credit risk within its non-agency MBS portfolio, and (c) improve the Bank’s risk-based capital position by eliminating certain MBS securities which represented higher risk-weighted assets for regulatory capital computation purposes.

ITEM 2. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

FORWARD-LOOKING STATEMENTS

Certain statements contained in this report are considered “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. These statements may be identified by the use of forward-looking words or phrases such as “anticipate,” “believe,” “could,” “expect,” “intend,” “may,” “planned,” “potential,” “should,” “will,” “would.” Such forward-looking statements in this report are inherently subject to many uncertainties in the Company’s operations and business environment. These uncertainties include general economic conditions, in particular, relating to consumer demand for the Bank’s products and services; the Bank’s ability to maintain current deposit and loan levels at current interest rates; competitive and technological developments; deteriorating credit quality, including changes in the interest rate environment reducing interest margins; prepayment speeds, loan origination and sale volumes, charge-offs and loan loss provisions; the Bank’s ability to maintain required capital levels and adequate sources of funding and liquidity; maintaining capital requirements may limit the Bank’s operations and potential growth; changes and trends in capital markets; competitive pressures among depository institutions; effects of critical accounting policies and judgments; changes in accounting policies or procedures as may be required by the Financial Accounting Standards Board (FASB) or other regulatory agencies; further write-downs in the Bank’s mortgage-backed securities portfolio; the Bank’s ability to implement its cost-savings and revenue enhancement initiatives; legislative or regulatory changes or actions, or significant litigation, adversely affecting the Bank; fluctuation of the Company’s stock price; ability to attract and retain key personnel; ability to secure confidential information through the use of computer systems and telecommunications networks; and the impact of reputational risk created by these developments on such matters as business generation and retention, funding and liquidity. Shareholders, potential investors and other readers are urged to consider these factors carefully in evaluating the forward-looking statements and are cautioned not to place undue reliance on such forward-looking statements. Such uncertainties and other risks that may affect the Company's performance are discussed further in Part I, Item 1A, "Risk Factors," in the Company's Form 10-K, as amended, for the year ended September 30, 2010 originally filed with the Securities and Exchange Commission on December 23, 2010. The Company undertakes no obligation to make any revisions to the forward-looking statements contained in this report or to update them to reflect events or circumstances occurring after the date of this report.

GENERAL

The following discussion sets forth management's discussion and analysis of our consolidated financial condition as of December 31, 2010, and the consolidated results of operations for the three months ended December 31, 2010, compared to the same period in the fiscal year ended September 30, 2010. This discussion should be read in conjunction with the interim consolidated financial statements and the condensed notes thereto included with this report and with Management's Discussion and Analysis of Financial Condition and Results of Operations and the financial statements and notes related thereto included in the Company's annual report on Form 10-K/A filed with the Securities and Exchange Commission on January 11, 2011 and originally filed on December 23, 2010.

PERFORMANCE SUMMARY

The following table sets forth our results of operations and related summary information for the three month periods ended December 31, 2010 and 2009:

SUMMARY RESULTS OF OPERATIONS
(Dollar amounts in thousands, except for per share data)

	Three Months Ended December 31,	
	2010	2009
Net income (loss), as reported	$(239)	$175
EPS - basic, as reported	$(0.05)	$0.03
EBS - diluted, as reported	$(0.05)	$0.03
Cash dividends paid	$-	$-
Return on average assets (annualized)	(0.16%)	0.12%
Reteurn on average equity (annualized)	(1.87%)	1.26%
Efficiency ratio, as reported (1)	70.15%	70.53%

(1) Non-interest expense divided by the sum of net interest income plus non-interest income, excluding net impairment losses recognized in earnings. A lower ratio indicates greater efficiency.

The following is a brief summary of some of the factors that affected our operating results in the three months ended December 31, 2010. See the remainder of this section for a more thorough discussion. Unless otherwise stated, all monetary amounts in this Management's Discussion and Analysis of Financial Condition and Results of Operations, other than share and per share amounts, are stated in thousands. We reported a net loss of $239 for the three months ended December 31, 2010, compared to net income of $175 for the three months ended December 31, 2009. Both basic and diluted losses per share were ($0.05) for the three months ended December 31, 2010, compared to basic and diluted earnings per share of $0.03 for the three months ended December 31, 2009. The return on average assets for the three months ended December 31, 2010 and 2009 was (0.16%) and 0.12%, respectively. The return on average equity for the three months ended December 31, 2010 and 2009 was (1.87%) and 1.26%, respectively. No cash dividends were declared or paid in either of the three month periods ended December 31, 2010 and 2009, respectively.

Key factors behind these results were:

Net interest income and net interest margin improved from the comparable period last year as rates paid on interest bearing liabilities decreased at a greater rate than the decrease in rates on our interest earning assets, thereby increasing our interest rate spread.
Net interest income was $5,363 for the three month period ended December 31, 2010, an increase of $384 or 7.71% from the three month period ended December 31, 2009. Interest income decreased $213, from $8,172 to $7,959, and interest expense decreased $597 from $3,193 to $2,596 over the same periods.
The net interest margin of 3.73% for the three months ended December 31, 2010 compares to 3.62% for the three months ended December 31, 2009. The 11 basis point ("bp") increase largely resulted from a 14 bp increase in interest rate spread caused by a 41 bp decrease in the return on interest bearing assets, which was more than offset by a 55 bp decrease in the cost of interest bearing liabilities. We continue to see larger decreases in rates paid on deposits compared to the decreases in our lending interest rates. We also have reduced our balance of FHLB borrowings, which represents our higher interest rate source of funds.
Total loans were $450,718 at December 31, 2010, a decrease of $5,514, or 1.21% from September 30, 2010.
Total deposits were $482,393 at December 31, 2010, an increase of $6,091 or 1.28% from September 30, 2010.
Net loan charge-offs increased from $398 for the three months ended December 31, 2009 to $1,333 for the three months ended December 31, 2010. Increased net loan charge-offs, along with increases in delinquency rates and non-performing loans led to significantly increased provision for loan losses of $1,600 for the three months ended December 31, 2010 compared to $760 for the three months ended December 31, 2009. Net loan charge-offs represented 0.98% of total loans for the three months ended December 31, 2010, compared to 0.51% for the three months ended December 31, 2009. Our new credit policy and more proactive charge-off and collection practices have contributed to increased loan charge-offs. Our customers' ability to repay their loans has also been adversely affected by sustained higher unemployment rates. Further, depressed home prices and other collateral values have increased incidences of collateral shortfalls and have contributed to an increase in impaired loans, charge-offs and the need for higher levels of allowance for loan loss.
Non-interest income (loss