SOUTHERN MISSOURI BANCORP INC
Form 10-Q
May 15, 2012

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 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 March 31, 2012

OR

___ 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 0-23406

Southern Missouri Bancorp, Inc.
(Exact name of registrant as specified in its charter)

| | |
|---|---|
| Missouri<br>(State or jurisdiction of incorporation) | 43-1665523<br>(IRS employer id. no.) |
| 531 Vine Street, Poplar Bluff, MO<br>(Address of principal executive offices) | 63901<br>(Zip code) |

(573) 778-1800
Registrant's telephone number, including area code

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been 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 proceeding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes X No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definition of "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 | | Smaller reporting company | X |

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

Yes No X

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

| Class | Outstanding at May 14, 2012 |
|---|---|
| Common Stock, Par Value $.01 | 3,250,476 |

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PART I: Item 1: Condensed Consolidated Financial Statements

SOUTHERN MISSOURI BANCORP, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
MARCH 31, 2012, AND JUNE 30, 2011

| | March 31, 2012 (unaudited) | June 30, 2011 |
|---|---|---|
| Cash and cash equivalents | $86,923,644 | $33,895,706 |
| Interest-bearing time deposits | 1,372,000 | 792,000 |
| Available for sale securities | 73,593,003 | 63,327,201 |
| Stock in FHLB of Des Moines | 2,052,200 | 2,369,200 |
| Stock in Federal Reserve Bank of St. Louis | 1,001,050 | 718,750 |
| Loans receivable, net of allowance for loan losses of $7,258,712 and $6,438,451 at March 31, 2012, and June 30, 2011, respectively | 546,226,461 | 556,576,055 |
| Accrued interest receivable | 2,941,918 | 3,799,935 |
| Premises and equipment, net | 11,322,794 | 8,057,529 |
| Bank owned life insurance – cash surrender value | 15,828,599 | 8,114,469 |
| Intangible assets, net | 1,561,840 | 1,874,689 |
| Prepaid expenses and other assets | 8,354,625 | 8,674,848 |
| Total assets | $751,178,134 | $688,200,382 |
| | | |
| Deposits | $599,298,621 | $560,150,817 |
| Securities sold under agreements to repurchase | 26,516,711 | 25,230,051 |
| Advances from FHLB of Des Moines | 24,500,000 | 33,500,000 |
| Accounts payable and other liabilities | 313,718 | 5,536,062 |
| Accrued interest payable | 702,096 | 834,344 |
| Subordinated debt | 7,217,000 | 7,217,000 |
| Total liabilities | 658,548,146 | 632,468,274 |
| | | |
| Commitments and contingencies | - | - |
| | | |
| Preferred stock, $.01 par value, $1,000 liquidation value; 500,000 shares authorized; 20,000 and 9,550 shares issued and outstanding at March 31, 2012, and June 30, 2011, respectively | 20,000,000 | 9,455,635 |
| Common stock, $.01 par value; 4,000,000 shares authorized; 3,252,706 and 2,957,256 shares issued at March 31, 2012, and June 30, 2011, respectively | 32,527 | 29,572 |
| Warrants to acquire common stock | 176,790 | 176,790 |
| Additional paid-in capital | 22,470,035 | 16,274,545 |
| Retained earnings | 49,408,068 | 43,014,191 |
| Treasury stock of 2,730 and 858,250 shares at March 31, 2012, and June 30, 2011, at cost | (32,215) | (13,754,245) |
| Accumulated other comprehensive income | 574,783 | 535,620 |
| Total stockholders' equity | 92,629,988 | 55,732,108 |
| | | |
| Total liabilities and stockholders' equity | $751,178,134 | $688,200,382 |

See Notes to Condensed Consolidated Financial Statements

SOUTHERN MISSOURI BANCORP, INC
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
FOR THE THREE- AND NINE-MONTH PERIODS ENDED MARCH 31, 2012 AND 2011 (Unaudited)

| | Three months ended March 31, | | Nine months ended March 31, | |
|---|---|---|---|---|
| | 2012 | 2011 | 2012 | 2011 |
| INTEREST INCOME: | | | | |
| Loans | $9,077,557 | $9,626,619 | $27,890,260 | $23,017,959 |
| Investment securities | 379,900 | 320,730 | 1,122,083 | 954,957 |
| Mortgage-backed securities | 224,338 | 324,188 | 745,727 | 1,070,907 |
| Other interest-earning assets | 73,414 | 24,525 | 154,336 | 86,398 |
| Total interest income | 9,755,209 | 10,296,062 | 29,912,406 | 25,130,221 |
| INTEREST EXPENSE: | | | | |
| Deposits | 2,011,104 | 2,455,785 | 6,457,288 | 6,874,108 |
| Securities sold under agreements to repurchase | 64,958 | 60,536 | 184,002 | 195,208 |
| Advances from FHLB of Des Moines | 310,193 | 332,012 | 988,975 | 1,218,642 |
| Subordinated debt | 59,593 | 55,085 | 173,360 | 171,150 |
| Total interest expense | 2,445,848 | 2,903,418 | 7,803,625 | 8,459,108 |
| NET INTEREST INCOME | 7,309,361 | 7,392,644 | 22,108,781 | 16,671,113 |
| PROVISION FOR LOAN LOSSES | 215,338 | 1,195,891 | 1,077,454 | 2,112,100 |
| NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES | 7,094,023 | 6,196,753 | 21,031,327 | 14,559,013 |
| NONINTEREST INCOME: | | | | |
| Deposit account charges and related fees | 379,825 | 393,970 | 1,128,017 | 1,182,950 |
| Bank credit transaction fees | 278,595 | 221,990 | 805,977 | 633,485 |
| Loan late charges | 53,560 | 44,567 | 169,993 | 160,518 |
| Other loan fees | 22,593 | 46,246 | 121,901 | 155,125 |
| Net realized gains on sale of loans | 89,834 | 34,527 | 232,866 | 85,693 |
| Bargain purchase gain on acquisitions | - | - | - | 6,996,750 |
| Earnings on Bank owned life insurance | 71,179 | 68,805 | 214,130 | 207,571 |
| Other income | 58,933 | 40,196 | 297,211 | 114,550 |
| Total noninterest income | 954,519 | 850,301 | 2,970,095 | 9,536,642 |
| NONINTEREST EXPENSE: | | | | |
| Compensation and benefits | 2,418,341 | 2,281,737 | 6,944,735 | 5,803,040 |
| Occupancy and equipment, net | 679,075 | 518,884 | 1,880,776 | 1,681,825 |
| Deposit insurance premiums | 94,126 | 164,542 | 277,261 | 467,599 |
| Legal and professional fees | 145,362 | 82,385 | 338,436 | 406,584 |
| Advertising | 89,403 | 74,698 | 256,621 | 174,504 |
| Postage and office supplies | 115,941 | 96,789 | 348,819 | 265,340 |
| Intangible amortization | 104,283 | 104,283 | 312,849 | 250,353 |
| Bank card network fees | 136,041 | 104,309 | 398,859 | 302,410 |
| Other operating expense | 1,083,821 | 640,864 | 1,774,771 | 1,273,453 |
| Total noninterest expense | 4,866,393 | 4,068,491 | 12,533,127 | 10,625,108 |
| INCOME BEFORE INCOME TAXES | 3,182,149 | 2,978,563 | 11,468,295 | 13,470,547 |
| INCOME TAXES | 1,006,107 | 1,000,571 | 3,767,421 | 4,613,809 |
| NET INCOME | $2,176,042 | $1,977,992 | $7,700,874 | $8,856,738 |

| | | | | |
|---|---|---|---|---|
| Less: effective dividend on preferred shares | 50,000 | 128,011 | 402,111 | 383,724 |
| Net income available to common shareholders | $2,126,042 | $1,849,981 | $7,298,763 | $8,473,014 |
| | | | | |
| Basic earnings per common share | $0.65 | $0.88 | $2.76 | $4.06 |
| Diluted earnings per common share | $0.64 | $0.86 | $2.67 | $3.93 |
| Dividends per common share | $0.12 | $0.12 | $0.36 | $0.36 |

See Notes to Condensed Consolidated Financial Statements

SOUTHERN MISSOURI BANCORP, INC
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
FOR THE THREE- AND NINE-MONTH PERIODS ENDED MARCH 31, 2012 AND 2011 (Unaudited)

| | Three months ended March 31, | | Nine months ended March 31, | |
|---|---|---|---|---|
| | 2012 | 2011 | 2012 | 2011 |
| Net income | $2,176,042 | $1,977,992 | $7,700,874 | $8,856,738 |
| Other comprehensive income: | | | | |
| Unrealized gains (losses) on securities available-for-sale | (334,212) | 229,641 | 135,040 | (1,019,506) |
| Unrealized gains (losses) on available-for-sale securities for which a portion of an other-than-temporary impairment has been recognized in income | (33) | (277) | (72,876) | (10) |
| Tax benefit (expense) | 123,671 | (84,865) | (23,001) | 377,221 |
| Total other comprehensive income (loss) | (210,574) | 144,499 | 39,163 | (642,295) |
| Comprehensive income | $1,965,468 | $2,122,491 | $7,740,037 | $8,214,443 |

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SOUTHERN MISSOURI BANCORP, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE NINE-MONTH PERIODS ENDED MARCH 31, 2012 AND 2011 (Unaudited)

| | Nine months ended March 31, | |
|---|---|---|
| | 2012 | 2011 |
| Cash Flows From Operating Activities: | | |
| Net income | $7,700,874 | $8,856,738 |
| Items not requiring (providing) cash: | | |
| Depreciation | 682,285 | 535,309 |
| MRP and SOP expense | 17,687 | 53,352 |
| (Gain) loss on sale of foreclosed assets | (124,089) | 51,900 |
| Amortization of intangible assets | 312,849 | 250,353 |
| Increase in cash surrender value of bank owned life insurance | (214,130) | (207,571) |
| Provision for loan losses | 1,077,454 | 2,112,100 |
| Net amortization of premiums and discounts on securities | 243,518 | 214,499 |
| Bargain purchase gain on acquisition | - | (6,996,750) |
| Deferred income taxes | (1,146,145) | 3,012,402 |
| Changes in: | | |
| Accrued interest receivable | 858,017 | 585,276 |
| Prepaid expenses and other assets | 565,825 | 488,921 |
| Accounts payable and other liabilities | (4,109,200) | 3,148,316 |
| Accrued interest payable | (132,248) | (29,422) |
| Net cash provided by operating activities | 5,742,697 | 11,915,423 |
| | | |
| Cash flows from investing activities: | | |
| Net decrease (increase) in loans | 9,149,712 | (20,438,842) |
| Net cash received in acquisitions | - | 38,249,088 |
| Net (increase) decrease in interest-bearing deposits | (580,000) | 297,000 |
| Proceeds from maturities of available for sale securities | 29,425,788 | 21,223,397 |
| Net redemptions of Federal Home Loan Bank stock | 317,000 | 444,900 |
| Net purchases of Federal Reserve Bank of St. Louis stock | (282,300) | (135,650) |
| Purchases of available-for-sale securities | (39,872,944) | (18,915,545) |
| Purchases of premises and equipment | (3,947,550) | (853,696) |
| Purchases of bank owned life insurance | (7,500,000) | - |
| Investments in state & federal tax credits | (686,109) | (2,475,412) |
| Proceeds from sale of foreclosed assets | 687,024 | 176,699 |
| Net cash provided by (used in) investing activities | (13,289,379) | 17,571,939 |
| | | |
| Cash flows from financing activities: | | |
| Proceeds from issuance of preferred stock | 19,973,208 | - |
| Redemption of preferred stock | (9,550,000) | - |
| Proceeds from issuance of common stock | 19,914,349 | - |
| Net increase in demand deposits and savings accounts | 58,584,161 | 56,566,359 |
| Net decrease in certificates of deposits | (19,436,357) | (33,829,909) |
| Net increase (decrease) in securities sold under agreements to repurchase | 1,286,660 | (4,385,977) |
| Repayments of Federal Home Loan Bank advances | (9,000,000) | (27,206,803) |

| | | |
|---|---|---|
| Dividends paid on preferred stock | (318,760) | (358,125) |
| Dividends paid on common stock | (893,871) | (752,871) |
| Exercise of stock options | 15,230 | 67,500 |
| Net cash provided by (used in) financing activities | 60,574,620 | (9,899,826) |
| | | |
| Increase in cash and cash equivalents | 53,027,938 | 19,587,536 |
| Cash and cash equivalents at beginning of period | 33,895,706 | 33,383,278 |
| | | |
| Cash and cash equivalents at end of period | $86,923,644 | $52,970,814 |
| | | |
| Supplemental disclosures of Cash flow information: | | |
| | | |
| Noncash investing and financing activities: | | |
| Conversion of loans to foreclosed real estate | $549,502 | $540,332 |
| Conversion of foreclosed real estate to loans | 565,550 | 616,882 |
| Conversion of loans to repossessed assets | 138,476 | 149,715 |
| Cash paid during the period for: | | |
| Interest (net of interest credited) | $2,367,008 | $2,463,519 |
| Income taxes | 5,601,570 | 1,049,101 |

See Notes to Condensed Consolidated Financial Statements

SOUTHERN MISSOURI BANCORP, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

Note 1: Basis of Presentation

The accompanying unaudited interim consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Securities and Exchange Commission (SEC) Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, all material adjustments (consisting only of normal recurring accruals) considered necessary for a fair presentation have been included. The consolidated balance sheet of the Company as of June 30, 2011, has been derived from the audited consolidated balance sheet of the Company as of that date. Operating results for the three- and nine-month periods ended March 31, 2012, are not necessarily indicative of the results that may be expected for the entire fiscal year. For additional information, refer to the audited consolidated financial statements included in the Company's June 30, 2011, Form 10-K, which was filed with the SEC.

The accompanying consolidated financial statements include the accounts of the Company and its wholly owned subsidiary, Southern Bank (Bank). All significant intercompany accounts and transactions have been eliminated in consolidation.

Note 2: Organization and Summary of Significant Accounting Policies

Organization. Southern Missouri Bancorp, Inc., a Missouri corporation (the Company) was organized in 1994 and is the parent company of Southern Bank (the Bank). Substantially all of the Company's consolidated revenues are derived from the operations of the Bank, and the Bank represents substantially all of the Company's consolidated assets and liabilities.

The Bank is primarily engaged in providing a full range of banking and financial services to individuals and corporate customers in its market areas. The Bank and Company are subject to competition from other financial institutions. The Bank and Company are subject to regulation by certain federal and state agencies and undergo periodic examinations by those regulatory authorities.

Basis of Financial Statement Presentation. The financial statements of the Company have been prepared in conformity with accounting principles generally accepted in the United States of America and general practices within the banking industry. In the normal course of business, the Company encounters two significant types of risk: economic and regulatory. Economic risk is comprised of interest rate risk, credit risk, and market risk. The Company is subject to interest rate risk to the degree that its interest-bearing liabilities reprice on a different basis than its interest-earning assets. Credit risk is the risk of default on the Company's investment or loan portfolios resulting from the borrowers' inability or unwillingness to make contractually required payments. Market risk reflects changes in the value of the investment portfolio, collateral underlying loans receivable, and the value of the Company's investments in real estate.

Principles of Consolidation. The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary, the Bank. All significant intercompany accounts and transactions have been eliminated.

Use of Estimates. The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Material estimates that are particularly susceptible to significant change relate to the determination of the allowance for loan losses, estimated fair values of purchased loans, other-than-temporary impairments (OTTI), and fair value of financial instruments.

Cash and Cash Equivalents. For purposes of reporting cash flows, cash and cash equivalents includes cash, due from depository institutions and interest-bearing deposits in other depository institutions with original maturities of three months or less. Interest-bearing deposits in other depository institutions were $84,237,000 and $30,690,000 at March 31, 2012, and June 30, 2011, respectively. The deposits are held in various commercial banks in amounts not exceeding the FDIC's deposit insurance limits, as well as at the Federal Reserve, the Federal Home Loan Bank of Des Moines, and the Federal Home Loan Bank of Dallas.

Available for Sale Securities. Available for sale securities, which include any security for which the Company has no immediate plan to sell but which may be sold in the future, are carried at fair value. Unrealized gains and losses, net of tax, are reported in accumulated other comprehensive income, a component of stockholders' equity. All securities have been classified as available for sale.

Premiums and discounts on debt securities are amortized or accreted as adjustments to income over the estimated life of the security using the level yield method. Realized gains or losses on the sale of securities is based on the specific identification method. The fair value of securities is based on quoted market prices or dealer quotes. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities.

The Company does not invest in collateralized mortgage obligations that are considered high risk.

When the Company does not intend to sell a debt security, and it is more likely than not the Company will not have to sell the security before recovery of its cost basis, it recognizes the credit component of an other-than-temporary impairment of a debt security in earnings and the remaining portion in other comprehensive income. As a result, the Company's balance sheet as of the dates presented reflects the full impairment (that is, the difference between the security's amortized cost basis and fair value) on debt securities that the Company intends to sell or would more likely than not be required to sell before the expected recovery of the amortized cost basis. For available-for-sale debt securities that management has no intent to sell and believes that it more likely than not will not be required to sell prior to recovery, only the credit loss component of the impairment is recognized in earnings, while the noncredit loss is recognized in accumulated other comprehensive income. The credit loss component recognized in earnings is identified as the amount of principal cash flows not expected to be received over the remaining term of the security as projected based on cash flow projections.

Federal Reserve Bank and Federal Home Loan Bank Stock. The Bank is a member of the Federal Reserve and the Federal Home Loan Bank (FHLB) systems. Capital stock of the Federal Reserve and the FHLB is a required investment based upon a predetermined formula and is carried at cost.

Loans. Loans are generally stated at unpaid principal balances, less the allowance for loan losses and net deferred loan origination fees.

Interest on loans is accrued based upon the principal amount outstanding. The accrual of interest on loans is discontinued when, in management's judgment, the collectibility of interest or principal in the normal course of business is doubtful. The Company complies with regulatory guidance which indicates that loans should be placed in nonaccrual status when 90 days past due, unless the loan is both well-secured and in the process of collection. A loan that is "in the process of collection" may be subject to legal action or, in appropriate circumstances, through other collection efforts reasonably expected to result in repayment or restoration to current status in the near future. A loan is considered delinquent when a payment has not been made by the contractual due date. Interest income previously accrued but not collected at the date a loan is placed on nonaccrual status is reversed against interest income. Cash receipts on a nonaccrual loan are applied to principal and interest in accordance with its contractual terms unless full payment of principal is not expected, in which case cash receipts, whether designated as principal or interest, are applied as a reduction of the carrying value of the loan. A nonaccrual loan is generally returned to accrual status when principal and interest payments are current, full collectability of principal and interest is reasonably assured, and a consistent record of performance has been demonstrated.

The allowance for losses on loans represents management's best estimate of losses probable in the existing loan portfolio. The allowance for losses on loans is increased by the provision for losses on loans charged to expense and reduced by loans charged off, net of recoveries. Loans are charged off in the period deemed uncollectible, based on management's analysis of expected cash flow (for non-collateral dependent loans) or collateral value (for collateral-dependent loans). Subsequent recoveries of loans previously charged off, if any, are credited to the allowance when received. The provision for losses on loans is determined based on management's assessment of several factors: reviews and evaluations of specific loans, changes in the nature and volume of the loan portfolio, current economic conditions and the related impact on specific borrowers and industry groups, historical loan loss experience, the level of classified and nonperforming loans and the results of regulatory examinations.

Loans are considered impaired if, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Depending on a particular loan's circumstances, we measure impairment of a loan based upon either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's observable market price, or the fair value of the collateral less estimated costs to sell if the loan is collateral dependent. Valuation allowances are established for collateral-dependent impaired loans for the difference between the loan amount and fair value of collateral less estimated selling costs. For impaired loans that are not collateral dependent, a valuation allowance is established for the difference between the loan amount and the present value of expected future cash flows discounted at the historical effective interest rate or the observable market price of the loan. Impairment losses are recognized through an increase in the required allowance for loan losses. Cash receipts on loans deemed impaired are recorded based on the loan's separate status as a nonaccrual loan or an accrual loan.

As a result of the acquisition of the former First Southern Bank, Batesville, Arkansas, the Company acquired certain loans with an outstanding principal balance of $14.2 million for which it was deemed probable that we would be unable to collect all contractually required payments. These loans are accounted for in accordance with ASC 310-30, Loans and Debt Securities Acquired with Deteriorated Credit Quality. The Company recorded a fair value discount of $3.9 million related to these loans acquired with deteriorated credit quality ("purchased credit impaired loans"), and began carrying them at a value of $10.3 million. For these loans, we determined the contractual amount and timing of undiscounted principal and interest payments (the "undiscounted contractual cash flows"), and estimated the amount and timing of undiscounted expected principal and interest payments, including expected prepayments (the "undiscounted expected cash flows"). Under acquired impaired loan accounting, the difference between the undiscounted contractual cash flows and the undiscounted expected cash flows is the nonaccretable difference. The nonaccretable difference is an estimate of the loss exposure of principal and interest related to the purchased credit impaired loans, and the amount is subject to change over time based on the performance of the loans. The carrying value of purchased credit impaired loans is initially determined as the discounted expected cash flows. The excess of expected cash flows at acquisition over the initial fair value of the purchased credit impaired loans is referred to as the "accretable yield" and is recorded as interest income over the estimated life of the acquired loans using the level-yield method, if the timing and amount of the future cash flows is reasonably estimable. The carrying value of purchased credit impaired loans is reduced by payments received, both principal and interest, and increased by the portion of the accretable yield recognized as interest income. Subsequent to acquisition, the Company evaluates the purchased credit impaired loans on a quarterly basis. Increases in expected cash flows compared to those previously estimated increase the accretable yield and are recognized as interest income prospectively. Decreases in expected cash flows compared to those previously estimated decrease the accretable yield and may result in the establishment of an allowance for loan losses and a provision for loan losses. Purchased credit impaired loans are generally considered accruing and performing loans, as the loans accrete interest income over the estimated life of the loan when expected cash flows are reasonably estimable. Accordingly, purchased credit impaired loans that are contractually past due are still considered to be accruing and performing as long as there is an expectation that the estimated cash flows will be received. If the timing and amount of cash flows is not reasonably estimable, the loans may be classified as nonaccrual loans.

Loan fees and certain direct loan origination costs are deferred, and the net fee or cost is recognized as an adjustment to interest income using the interest method over the contractual life of the loans.

Foreclosed Real Estate. Real estate acquired by foreclosure or by deed in lieu of foreclosure is initially recorded at fair value less estimated selling costs. Costs for development and improvement of the property are capitalized.

Valuations are periodically performed by management, and an allowance for losses is established by a charge to operations if the carrying value of a property exceeds its estimated fair value, less estimated selling costs.

Loans to facilitate the sale of real estate acquired in foreclosure are discounted if made at less than market rates. Discounts are amortized over the fixed interest period of each loan using the interest method.

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Premises and Equipment. Premises and equipment are stated at cost less accumulated depreciation and include expenditures for major betterments and renewals. Maintenance, repairs, and minor renewals are expensed as incurred. When property is retired or sold, the retired asset and related accumulated depreciation are removed from the accounts and the resulting gain or loss taken into income. The Company reviews property and equipment for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If such assets are considered to be impaired, the impairment loss recognized is measured by the amount by which the carrying amount exceeds the fair value of the assets.

Depreciation is computed by use of straight-line and accelerated methods over the estimated useful lives of the assets. Estimated lives are generally 10 to 40 years for premises, and five to seven years for equipment.

Intangible Assets. The Company's gross amount of intangible assets was $4.8 million at both March 31, 2012, and June 30, 2011, with accumulated amortization of $3.2 million and $2.9 million, respectively. The Company's intangible assets are being amortized over periods ranging from five to fifteen years, with amortization expense expected to be approximately $417,000 per year over the next three fiscal years.

Income Taxes. The Company accounts for income taxes in accordance with income tax accounting guidance (ASC 740, Income Taxes). The income tax accounting guidance results in two components of income tax expense: current and deferred. Current income tax expense reflects taxes to be paid or refunded for the current period by applying the provisions of the enacted tax law to the taxable income or excess of deductions over revenues. The Company determines deferred income taxes using the liability (or balance sheet) method. Under this method, the net deferred tax asset or liability is based on the tax effects of the differences between the book and tax bases of assets and liabilities, and enacted changes in tax rates and laws are recognized in the period in which they occur.

Deferred income tax expense results from changes in deferred tax assets and liabilities between periods. Deferred tax assets are recognized if it is more likely than not, based on the technical merits, that the tax position will be realized or sustained upon examination. The term more likely than not means a likelihood of more than 50 percent; the terms examined and upon examination also include resolution of the related appeals or litigation processes, if any. A tax position that meets the more-likely-than-not recognition threshold is initially and subsequently measured as the largest amount of tax benefit that has a greater than 50 percent likelihood of being realized upon settlement with a taxing authority that has full knowledge of all relevant information. The determination of whether or not a tax position has met the more-likely-than-not recognition threshold considers the facts, circumstances, and information available at the reporting date and is subject to management's judgment. Deferred tax assets are reduced by a valuation allowance if, based on the weight of evidence available, it is more likely than not that some portion or all of a deferred tax asset will not be realized.

The Company recognizes interest and penalties on income taxes as a component of income tax expense.

The Company files consolidated income tax returns with its subsidiary.

Incentive Plan. The Company accounts for its management recognition plan (MRP) in accordance with ASC 718, "Share-Based Payment." The aggregate purchase price of all shares owned by the incentive plan is reflected as a reduction of stockholders' equity. Compensation expense is based on the market price of the Company's stock on the date the shares are granted and is recorded over the vesting period. The difference between the aggregate purchase price and the fair value on the date the shares are considered earned is recorded as an adjustment to additional paid in capital.

Outside Directors' Retirement. The Bank adopted a directors' retirement plan in April 1994 for outside directors. The directors' retirement plan provides that each non-employee director (participant) shall receive, upon termination of service on the Board on or after age 60, other than termination for cause, a benefit in equal annual installments over a five year period. The benefit will be based upon the product of the participant's vesting percentage and the total Board fees paid to the participant during the calendar year preceding termination of service on the Board. The vesting percentage shall be determined based upon the participant's years of service on the Board.

In the event that the participant dies before collecting any or all of the benefits, the Bank shall pay the participant's beneficiary. No benefits shall be payable to anyone other than the beneficiary, and shall terminate on the death of the beneficiary.

Stock Options. With limited exceptions, the amount of compensation cost is measured based on the grant-date fair value of the equity instruments issued. Compensation cost is recognized over the vesting period during which an employee provides service in exchange for the award. Stock-based compensation has been recognized for all stock options granted or modified after July 1, 2005. In addition, stock options not vested on July 1, 2005, were recognized in expense over their remaining vesting period.

Earnings Per Share. Basic earnings per share available to common stockholders is computed using the weighted-average number of common shares outstanding. Diluted earnings per share available to common stockholders includes the effect of all weighted-average dilutive potential common shares (stock options and warrants) outstanding during each period.

Comprehensive Income. Comprehensive income consists of net income and other comprehensive income, net of applicable income taxes. Other comprehensive income includes unrealized appreciation (depreciation) on available-for-sale securities, unrealized appreciation (depreciation) on available-for-sale securities for which a portion of an other-than-temporary impairment has been recognized in income, and changes in the funded status of defined benefit pension plans.

Treasury Stock. Treasury stock is stated at cost. Cost is determined by the first-in, first-out method.

Reclassification. Certain amounts included in the consolidated financial statements have been reclassified to conform to the 2012 presentation. These reclassifications had no effect on net income.

The following paragraphs summarize the impact of new accounting pronouncements:

In December 2011, the FASB issued ASU No. 2011-11, “Disclosures About Offsetting Assets and Liabilities.” The ASU requires entities to disclose both gross and net information about instruments and transactions eligible for offset in the balance sheet, as well as instruments and transactions subject to an agreement similar to a master netting agreement. The scope of the ASU includes derivatives, sale and repurchase agreements, reverse sale and repurchase agreements, and securities borrowing and lending arrangements. The ASU is effective for annual and interim reporting periods beginning January 1, 2013. The Company is evaluating the ASU, but does not anticipate that it will have a material impact on the Company’s financial position or results of operations.

In September 2011, the FASB issued ASU No. 2011-08 to amend FASB ASC Topic 350, Intangibles – Goodwill and Other, to simplify how entities test goodwill for impairment. The amendment permits an entity to first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount as a basis for determining whether it is necessary to further perform the two-step goodwill impairment test described in Topic 350. The amendments are effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011. The Company is evaluating the ASU, but does not anticipate that it will have a material impact on the Company’s financial position or results of operations.

In June 2011, the FASB issued ASU No. 2011-05 to amend FASB ASC Topic 220, Comprehensive Income: Presentation of Comprehensive Income. The purpose of the update is to improve the comparability, consistency and transparency of financial reporting related to other comprehensive income. It eliminates the option to present the components of other comprehensive income as part of the statement of changes in stockholders’ equity. Instead, the components of other comprehensive income must either be presented with net income in a single continuous statement of comprehensive income or as a separate but consecutive statement following the statement of operations. Regardless of which method is used, adjustments for items that are reclassified from other comprehensive income to net income must be presented on the face of the financial statements. The Update is effective on a retrospective basis for interim and annual reporting periods beginning after December 15, 2011. The Company adopted the ASU in the third quarter ended March 31, 2012, by including a Condensed Consolidated Statement of Comprehensive Income.

In May 2011, the FASB issued ASU No. 2011-04 to amend FASB ASC Topic 820, Fair Value Measurement: Amendments to Achieve Common Fair Value Measurements and Disclosure Requirements in U.S. GAAP and IFRSs. The update amends the GAAP requirements for measuring fair value and for disclosures about fair value measurements to improve consistency between GAAP and IFRSs by changing some of the wording used to describe the requirements, clarifying the intended application of certain requirements and changing certain principles. The update was effective on a prospective basis for interim and annual reporting periods beginning after December 15, 2011. The adoption of the ASU included enhanced disclosure in Note 3 to the Condensed Consolidated Financial Statements, and did not have an impact on the Company's financial position or results of operations.

In April 2011, the FASB issued ASU No. 2011-03 to amend FASB ASC Topic 860, Transfers and Servicing. ASC 860 outlines when the transfer of financial assets under a repurchase agreement may or may not be accounted for as a sale. Whether the transferring entity maintains effective control over the transferred financial assets provides the basis for such a determination. The previous requirement that the transferor must have the ability to repurchase or redeem the financial assets before the maturity of the agreement is removed from the assessment of effective control by this Update. The Update was effective on a prospective basis for interim and annual reporting periods beginning on or after December 15, 2011, and did not have a material impact on the Company's financial position or results of operations.

Note 3: Fair Value Measurements

ASC Topic 820, Fair Value Measurements, defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Topic 820 also 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 standard describes three levels of inputs that may be used to measure fair value:

Level 1 Quoted prices in active markets for identical assets or liabilities

Level 2 Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in active markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities

Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities

Recurring Measurements. The following table presents the fair value measurements of assets recognized in the accompanying balance sheets measured at fair value on a recurring basis and the level within the fair value hierarchy in which the fair value measurements fall at March 31, 2012 and June 30, 2011:

| | | Fair Value Measurements at March 31, 2012, Using: | | |
|---|---|---|---|---|
| | Fair Value | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| U.S. government sponsored enterprises (GSEs) | $19,011,074 | $- | $19,011,074 | $- |
| State and political subdivisions | 32,774,387 | - | 32,774,387 | - |

| | | | | |
|---|---|---|---|---|
| Other securities | 558,214 | - | 513,414 | 44,800 |
| Mortgage-backed GSE residential | 21,249,328 | - | 21,249,328 | - |

| | Fair Value Measurements at June 30, 2011, Using: | | | |
|---|---|---|---|---|
| | Fair Value | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| U.S. government sponsored enterprises (GSEs) | $12,976,070 | $- | $12,976,070 | $- |
| State and political subdivisions | 24,981,454 | - | 24,981,454 | - |
| Other securities | 834,141 | - | 763,137 | 71,004 |
| Mortgage-backed GSE residential | 24,535,537 | - | 24,535,537 | - |

Following is a description of the valuation methodologies and inputs used for assets measured at fair value on a recurring basis and recognized in the accompanying consolidated balance sheets, as well as the general classification of such assets pursuant to the valuation hierarch. There have been no significant changes in the valuation techniques during the period ended March 31, 2012.

Available-for-sale Securities. When quoted market prices are available in an active market, securities are classified within Level 1. The Company does not have Level 1 securities. If quoted market prices are not available, then fair values are estimated using pricing models, or quoted prices of securities with similar characteristics. For these securities, our Company obtains fair value measurements from an independent pricing service. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information and the bond's terms and conditions, among other things. Level 2 securities include U.S. Government-sponsored enterprises, state and political subdivisions, other securities and mortgage-backed GSE residential securities. In certain cases where Level 1 or Level 2 inputs are not available, securities are classified within Level 3 of the hierarchy.

The following table presents a reconciliation of activity for available for sale securities measured at fair value based on significant unobservable (Level 3) information for the nine-month periods ended March 31, 2012 and 2011:

| | Three months ended March 31, | | Nine months ended March 31, | |
|---|---|---|---|---|
| | 2012 | 2011 | 2012 | 2011 |
| Available-for-sale securities, beginning of year | $29,000 | $- | $71,004 | $- |
| Total unrealized gain (loss) included in comprehensive income | 15,800 | - | (26,204) | - |
| Transfer from Level 2 to Level 3 | - | - | - | - |
| Available-for-sale securities, end of period | $44,800 | $- | $44,800 | $- |

Nonrecurring Measurements. The following tables present the fair value measurement of assets measured at fair value on a nonrecurring basis and the level within the ASC 820 fair value hierarchy in which the fair value measurements fell at March 31, 2012, and June 30, 2011:

| | Fair Value Measurements at March 31, 2012, Using: | | | |
|---|---|---|---|---|
| | Fair Value at March 31, 2012 | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| Impaired loans (collateral dependent) | $1,352,000 | $- | $- | $1,352,000 |
| Foreclosed and repossessed assets held for sale | 1,082,000 | - | - | 1,082,000 |

| | Fair Value Measurements at June 30, 2011, Using: | | | |
|---|---|---|---|---|
| | Fair Value at June 30, 2011 | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| Impaired loans (collateral dependent) | $543,000 | $- | $- | $543,000 |
| Foreclosed and repossessed assets held for sale | 1,150,000 | - | - | 1,150,000 |

The following table presents gains and (losses) recognized on assets measured on a non-recurring basis for the nine-month periods ended March 31, 2012 and 2011:

| | For the nine months ended | |
|---|---|---|
| | March 31, 2012 | March 31, 2011 |
| Impaired loans | $ (354,000) | $ - |
| Foreclosed and repossessed assets held for sale | (121,000) | (183,000) |
| Total gain (loss) recognized on a nonrecurring basis | $ (475,000) | (183,000) |

The following is a description of valuation methodologies and inputs used for assets measured at fair value on a nonrecurring basis and recognized in the accompanying consolidated balance sheets, as well as the general classification of such assets and liabilities pursuant to the valuation hierarch. For assets classified within Level 3 of fair value hierarchy, the process used to develop the reported fair value process is described below.

Impaired Loans (Collateral Dependent). A collateral dependent loan is considered to be impaired when it is probable that all of the principal and interest due may not be collected according to its contractual terms. Generally, when a collateral dependent loan is considered impaired, the amount of reserve required is measured based on the fair value of the underlying collateral. The Company makes such measurements on all material collateral dependent loans deemed impaired using the fair value of the collateral for collateral dependent loans. The fair value of collateral used by the Company is determined by obtaining an observable market price or by obtaining an appraised value from an independent, licensed or certified appraiser, using observable market data. This data includes information such as selling price of similar properties and capitalization rates of similar properties sold within the market, expected future cash flows or earnings of the subject property based on current market expectations, and other relevant factors. In addition, management applies selling and other discounts to the underlying collateral value to determine the fair value. If an appraised value is not available, the fair value of the collateral dependent impaired loan is determined by an adjusted appraised value including unobservable cash flows.

On a quarterly basis, loans classified as special mention, substandard, doubtful, or loss are evaluated including the loan officer's review of the collateral and its current condition, the Company's knowledge of the current economic environment in the market where the collateral is located, and the Company's recent experience with real estate in the area. The date of the appraisal is also considered in conjunction with the economic environment and any decline in the real estate market since the appraisal was obtained. For all loan types, updated appraisals are obtained if considered necessary. Of the Company's $6.7 million (carrying value) in impaired loans (collateral-dependent and purchased credit-impaired) at March 31, 2012, the Company utilized a real estate appraisal performed in the past 12 months to serve as the primary basis of our valuation for approximately $2.3 million. Older real estate appraisals were available for impaired loans with an outstanding balance of approximately $2.9 million. For impaired loans totaling $22,000, an observable market price within the last 12 months was utilized. The remaining $1.5 million was secured by collateral such as closely-held stock, an assignment of notes receivable, accounts receivable, or inventory. In instances where the economic environment has worsened and/or the real estate market declined since the last appraisal, a higher distressed sale discount would be applied to the appraised value.

The Company records collateral dependent impaired loans based on nonrecurring Level 3 inputs. If a collateral dependent loan's fair value, as estimated by the Company, is less than its carrying value, the Company either records a charge-off of the portion of the loan that exceeds the fair value or establishes a specific reserve as part of the allowance for loan losses.

Foreclosed and Repossessed Assets Held for Sale. Foreclosed and repossessed assets held for sale are valued at the time the loan is foreclosed upon or collateral is repossessed and the asset is transferred to foreclosed or repossessed assets held for sale. The value of the asset is based on third party or internal appraisals, less estimated costs to sell and appropriate discounts, if any. The appraisals are generally discounted based on current and expected market conditions that may impact the sale or value of the asset and management's knowledge and experience with similar assets. Such discounts typically may be significant and result in a Level 3 classification of the inputs for determining fair value of these assets. Foreclosed and repossessed assets held for sale are continually evaluated for additional impairment and are adjusted accordingly if impairment is identified.

Unobservable (Level 3) Inputs. The following table presents quantitative information about unobservable inputs used in recurring and nonrecurring Level 3 fair value measurements.

| | Fair value at March 31, 2012 | Valuation Technique | Unobservable Inputs | Range of Discounts Applied | Weighted-average Discount Applied |
|---|---|---|---|---|---|
| Available-for-sale Securities | $ 44,800 | Discounted cash flow | Discount rate | n/a | 8.32% |
| | | | Prepayment rate | n/a | 5% every 5 years(1) |
| | | | Projected defaults (% of pool balance) | n/a | 37.4% |
| | | | Anticipated recoveries (% of pool balance) | n/a | 8.0% |
| Impaired loans (collateral dependent) | 1,352,000 | Internal or third party appraisals | Discount to reflect realizable value | 0.5% - 100% | 8.2% |
| Foreclosed and repossessed assets | 1,082,000 | Third party appraisal | Marketability discount | 0.0% - 100% | 22.7% |

(1) The Level 3 fair value measurement also assumes that 11.9% of the pooled trust preferred security will prepay in 2013 due to unfavorable regulatory treatment by the issuer under the Dodd-Frank regulatory reform bill.

Fair Value of Financial Instruments. The following table presents estimated fair values of the Company's financial instruments and the level within the fair value hierarchy in which the fair value measurements fell at March 31, 2012, and June 30, 2011.

| | March 31, 2012 | | | |
|---|---|---|---|---|
| | Carrying Amount | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| Financial assets | | | | |
| Cash and cash equivalents | $86,924 | $86,924 | $- | $- |
| Interest-bearing time deposits | 1,372 | - | 1,372 | |
| Stock in FHLB | 2,052 | - | 2,052 | - |
| Stock in Federal Reserve Bank of St. Louis | 1,001 | - | 1,001 | - |
| Loans receivable, net | 546,226 | - | - | 550,537 |
| Accrued interest receivable | 2,942 | - | 2,942 | - |
| Financial liabilities | | | | |
| Deposits | 599,299 | 353,950 | - | 246,514 |
| Securities sold under agreements to repurchase | 26,517 | - | 26,517 | - |
| Advances from FHLB | 24,500 | - | 27,689 | - |
| Accrued interest payable | 702 | - | 702 | - |
| Subordinated debt | 7,217 | - | - | 5,158 |
| Unrecognized financial instruments (net of contract amount) | | | | |
| Commitments to originate loans | - | - | - | - |
| Letters of credit | - | - | - | - |
| Lines of credit | - | - | - | - |

| | June 30, 2011 | |
|---|---|---|
| | Carrying Amount | Fair Value |
| Financial assets | | |
| Cash and cash equivalents | $ 33,896 | $ 33,896 |
| Interest-bearing time deposits | 792 | 792 |
| Stock in FHLB | 2,369 | 2,369 |
| Stock in Federal Reserve Bank of St. Louis | 719 | 719 |
| Loans receivable, net | 556,576 | 558,083 |
| Accrued interest receivable | 3,800 | 3,800 |
| Financial liabilities | | |