UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended December 31, 2012

Commission File Number: 1-14588

Northeast Bancorp

(Exact name of registrant as specified in its charter)

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

(207) 786-3245

Registrant s telephone number, including area code

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subjected to such filing requirements for the past 90 days. Yes x No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definition of accelerated filer , large accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (check one):

Large accelerated filer o	Accelerated filer o
Non-accelerated filer o	Smaller Reporting Company x

Indicate by check mark whether the registrant is a shell company (as defined by Rule 12b-2 of the Exchange Act). Yes o No x

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date. As of January 31, 2013, the registrant had outstanding 9,467,372 shares of voting common stock, $1.00 par value per share and 916,069 shares of non-voting common stock, $1.00 par value per share.

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PART 1- FINANCIAL INFORMATION

Item 1. Financial Statements (Unaudited)

NORTHEAST BANCORP AND SUBSIDIARY

CONSOLIDATED BALANCE SHEETS

(Unaudited)

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

	December 31, 2012	June 30, 2012
Assets		
Cash and due from banks	$ 3,284	$ 2,538
Short-term investments	124,328	125,736
Total cash and cash equivalents	127,612	128,274
Available-for-sale securities, at fair value	133,363	133,264
Loans held for sale	8,262	9,882
Loans	392,583	356,254
Less: Allowance for loan losses	875	824
Loans, net	391,708	355,430
Premises and equipment, net	10,434	9,205
Repossessed collateral, net	2,633	834
Accrued interest receivable	2,068	1,840
Federal Home Loan Bank stock, at cost	4,602	4,602
Federal Reserve Bank stock, at cost	871	871
Intangible assets, net	3,957	4,487
Bank owned life insurance	14,148	14,295
Other assets	5,052	6,212
Total assets	$ 704,710	$ 669,196
Liabilities and Stockholders Equity		
Liabilities		
Deposits		
Demand	$ 48,136	$ 45,323
Savings and interest checking	86,231	90,204
Money market	58,351	45,024
Time deposits	308,800	241,637
Total deposits	501,518	422,188
Federal Home Loan Bank advances	43,213	43,450
Structured repurchase agreements	25,637	66,183
Short-term borrowings	1,570	1,209
Junior subordinated debentures issued to affiliated trusts	8,186	8,106

Capital lease obligation		1,827		1,911
Other liabilities		7,828		7,010
Total liabilities		589,779		550,057
Commitments and contingencies				
Stockholders equity				
Preferred stock, $1.00 par value, 1,000,000 shares authorized; no shares issued and outstanding at December 31, 2012; 4,227 shares issued and outstanding at June 30, 2012; liquidation preference of $1,000 per share		0		4
Voting common stock, $1.00 par value, 25,000,000 and 13,500,000 shares authorized at December 31, 2012 and June 30, 2012, respectively; 9,467,372 and 9,307,127 issued and outstanding at December 31, 2012 and June 30, 2012, respectively		9,467		9,307
Non-voting common stock, $1.00 par value, 3,000,000 and 1,500,000 shares authorized at December 31, 2012 and June 30, 2012, respectively; 916,069 and 1,076,314 issued and outstanding at December 31, 2012 and June 30, 2012, respectively		916		1,076
Warrants to purchase common stock		0		406
Additional paid-in capital		92,570		96,080
Unearned restricted stock		(109)		(127)
Retained earnings		12,534		12,235
Accumulated other comprehensive (loss) income		(447)		158
Total stockholders equity		114,931		119,139
Total liabilities and stockholders equity	$	704,710	$	669,196

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

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NORTHEAST BANCORP AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

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

	Three Months Ended December 31, 2012	Three Months Ended December 31, 2011	Six Months Ended December 31, 2012	Six Months Ended December 31, 2011
Interest and dividend income:				
Interest on loans	$ 8,267	$ 5,874	$ 15,608	$ 11,011
Interest on available-for-sale securities	348	541	695	1,180
Other interest and dividend income	109	57	198	116
Total interest and dividend income	8,724	6,472	16,501	12,307
Interest expense:				
Deposits	1,028	836	2,006	1,673
Federal Home Loan Bank advances	259	258	518	516
Structured repurchase agreements	161	249	380	497
Short-term borrowings	5	3	11	8
Junior subordinated debentures issued to affiliated trusts	191	185	384	368
Obligation under capital lease agreements	23	25	47	51
Total interest expense	1,667	1,556	3,346	3,113
Net interest and dividend income before provision for loan losses	7,057	4,916	13,155	9,194
Provision for loan losses	247	134	475	534
Net interest and dividend income after provision for loan losses	6,810	4,782	12,680	8,660
Noninterest income:				
Fees for other services to customers	462	370	772	710
Net securities gains	0	433	792	380
Gain on sales of loans held for sale	914	770	1,670	1,426
Gain on sales of portfolio loans	998	203	998	203
Gain recognized on repossessed collateral, net	0	73	451	50
Investment commissions	799	704	1,474	1,391
Bank-owned life insurance income	358	126	481	253
Other noninterest income	13	13	56	57
Total noninterest income	3,544	2,692	6,694	4,470
Noninterest expense:				
Salaries and employee benefits	4,413	3,729	8,470	7,446
Occupancy and equipment expense	1,147	916	2,225	1,765
Professional fees	399	277	822	692
Data processing fees	284	289	552	563
Marketing expense	252	254	439	345
Loan acquisition and collection expense	479	288	933	570
FDIC insurance premiums	122	122	239	239
Intangible asset amortization	265	337	530	673
Other noninterest expense	771	665	1,425	1,237

Total noninterest expense		8,132		6,877		15,635		13,530
Income (loss) from continuing operations before income tax expense (benefit)		2,222		597		3,739		(400)
Income tax expense (benefit)		705		179		1,189		(224)
Net income (loss) from continuing operations	$	1,517	$	418	$	2,550	$	(176)
Discontinued operations:								
Income from discontinued operations	$	0	$	0	$	0	$	186
Gain on sale of discontinued operations		0		0		0		1,529
Income tax expense		0		0		0		592
Net income from discontinued operations	$	0	$	0	$	0	$	1,123
Net income	$	1,517	$	418	$	2,550	$	947
Net income available to common stockholders	$	1,259	$	320	$	2,195	$	751
Weighted-average shares outstanding:								
Basic		10,383,441		3,494,498		10,383,441		3,494,498
Diluted		10,383,441		3,511,994		10,383,441		3,494,498
Earnings per common share:								
Basic:								
Income (loss) from continuing operations	$	0.12	$	0.09	$	0.21	$	(0.11)
Income from discontinued operations		0.00		0.00		0.00		0.32
Net income	$	0.12	$	0.09	$	0.21	$	0.21
Diluted:								
Income (loss) from continuing operations	$	0.12	$	0.09	$	0.21	$	(0.11)
Income from discontinued operations		0.00		0.00		0.00		0.32
Net income	$	0.12	$	0.09	$	0.21	$	0.21
Cash dividends declared per common share	$	0.09	$	0.09	$	0.18	$	0.18

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

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NORTHEAST BANCORP AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited)

(Dollars in thousands)

	Three Months Ended December 31,		Six Months Ended December 31,	
	2012	**2011**	**2012**	**2011**
Net income	$ 1,517	$ 418	$ 2,550	$ 947
Other comprehensive (loss) income, before tax:				
Available-for-sale securities:				
Change in net unrealized gain or loss on available-for-sale securities	(311)	(273)	(154)	1,363
Reclassification adjustment for net gains included in net income	0	(433)	(792)	(380)
Total available-for-sale securities	(311)	(706)	(946)	983
Derivatives and hedging activities:				
Change in accumulated loss on effective cash flow hedges	59	55	65	(143)
Reclassification adjustments for net gains included in net income	(19)	(21)	(37)	(43)
Total derivatives and hedging activities	40	34	28	(186)
Total other comprehensive (loss) income , before tax	(271)	(672)	(918)	797
Income tax (benefit) expense related to other comprehensive (loss) income	(93)	(229)	(313)	271
Other comprehensive (loss) income, net of tax	(178)	(443)	(605)	526
Comprehensive income (loss)	$ 1,339	$ (25)	$ 1,945	$ 1,473

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

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NORTHEAST BANCORP AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS EQUITY

(Unaudited)

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

	Preferred Stock Shares	Preferred Stock Amount	Voting Common Stock Shares	Voting Common Stock Amount	Non-voting Common Stock Shares	Non-voting Common Stock Amount	Warrants to Purchase Common Stock	Additional Paid-in Capital	Unearned Restricted Stock	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Stockholders Equity
Balance at June 30, 2011	4,227	$ 4	3,312,173	$ 3,312	195,351	$ 195	$ 406	$ 49,700	$ (163)	$ 11,726	$ (226)	$ 64,954
Net income	0	0	0	0	0	0	0	0	0	947	0	947
Other comprehensive income, net of tax	0	0	0	0	0	0	0	0	0	0	526	526
Dividends on preferred stock	0	0	0	0	0	0	0	0	0	(106)	0	(106)
Dividends on common stock at $0.18 per share	0	0	0	0	0	0	0	0	0	(631)	0	(631)
Stock-based compensation	0	0	0	0	0	0	0	192	18	0	0	210
Accretion of preferred stock	0	0	0	0	0	0	0	90	0	(90)	0	0
Balance at December 31, 2011	4,227	$ 4	3,312,173	$ 3,312	195,351	$ 195	$ 406	$ 49,982	$ (145)	$ 11,846	$ 300	$ 65,900
Balance at June 30, 2012	4,227	$ 4	9,307,127	$ 9,307	1,076,314	$ 1,076	$ 406	$ 96,080	$ (127)	$ 12,235	$ 158	$ 119,139
Net income	0	0	0	0	0	0	0	0	0	2,550	0	2,550
Other comprehensive loss, net of tax	0	0	0	0	0	0	0	0	0	0	(605)	(605)
Conversion of non-voting common stock to voting common stock	0	0	160,245	160	(160,245)	(160)	0	0	0	0	0	0
Dividends on preferred stock	0	0	0	0	0	0	0	0	0	(113)	0	(113)
Dividends on common stock at $0.18 per share	0	0	0	0	0	0	0	0	0	(1,870)	0	(1,870)
Offering costs	0	0	0	0	0	0	0	(60)	0	0	0	(60)
Stock-based compensation	0	0	0	0	0	0	0	194	18	0	0	212
Redemption of preferred stock and warrants	(4,227)	(4)	0	0	0	0	(406)	(3,912)	0	0	0	(4,322)
Accretion of preferred stock	0	0	0	0	0	0	0	268	0	(268)	0	0
	0	$ 0	9,467,372	$ 9,467	916,069	$ 916	0	$ 92,570	$ (109)	$ 12,534	$ (447)	$ 114,931

Balance at
December 31, 2012

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

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NORTHEAST BANCORP AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(Dollars in thousands)

	Six Months Ended December 31, 2012	2011
Operating activities:		
Net income	$ 2,550	$ 947
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Provision for loan losses	475	534
Gain on sale or impairment of repossessed collateral, net	(451)	(50)
Accretion of fair value adjustments on loans, net	(3,505)	(1,124)
Accretion of fair value adjustments on deposits, net	(537)	(716)
Accretion of fair value adjustments on borrowings, net	(703)	(1,088)
Originations of loans held for sale	(73,982)	(72,454)
Net proceeds from sales of loans held for sale	77,272	70,867
Gain on sales of loans held for sale	(1,670)	(1,426)
Gain on sales of portfolio loans	(998)	(203)
Amortization of intangible assets	530	742
Bank-owned life insurance income, net	(481)	(253)
Depreciation of premises and equipment	842	604
Loss on sale of premises and equipment	0	2
Net gain on sale of available-for-sale securities	(792)	(380)
Stock-based compensation	212	210
Gain on sale of assets of insurance division	0	(1,529)
Amortization of securities, net	794	843
Changes in other assets and liabilities:		
Interest receivable	(228)	(517)
Decrease in prepaid FDIC assessment	220	323
Other assets and liabilities	2,099	372
Net cash provided by (used in) operating activities	1,647	(4,296)
Investing activities:		
Proceeds from sales of available-for-sale securities	159,579	49,053
Purchases of available-for-sale securities	(167,294)	(51,274)
Proceeds from maturities and principal payments on available-for-sale securities	6,668	12,223
Loan purchases	(63,887)	(51,662)
Loan originations and principal collections, net	24,193	14,141
Purchases of premises and equipment	(2,071)	(1,754)
Proceeds from sales of portfolio loans	5,189	711
Proceeds from sales of repossessed collateral	907	660
Proceeds from life insurance benefits	628	0
Proceeds from sale of assets of insurance division	0	9,726
Net cash used in investing activities	(36,088)	(18,176)
Financing activities:		
Net increase in deposits	79,867	622
Net increase (decrease) in short-term borrowings	361	(771)
Dividends paid on preferred stock	(113)	(106)

Dividends paid on common stock		(1,870)		(631)
Stock offering costs		(60)		0
Repayment of structured repurchase agreements		(40,000)		0
Repayment of other borrowings		0		(2,129)
Redemption of preferred stock and warrants		(4,322)		0
Repayment of capital lease obligation		(84)		(81)
Net cash provided by (used in) financing activities		33,779		(3,096)
Net decrease in cash and cash equivalents		(662)		(25,568)
Cash and cash equivalents, beginning of period		128,274		83,931
Cash and cash equivalents, end of period	$	127,612	$	58,363
Supplemental schedule of noncash investing and financing activities:				
Transfers from loans to repossessed collateral	$	3,310	$	757
Transfers from repossessed collateral to loans		1,055		0

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

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NORTHEAST BANCORP AND SUBSIDIARY

Notes to Unaudited Consolidated Financial Statements

December 31, 2012

1. Basis of Presentation

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

These financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and notes required by GAAP for complete financial statements. In the opinion of management, the accompanying consolidated financial statements contain all adjustments (consisting principally of normal recurring accruals) considered necessary for a fair presentation of the Company s financial position at December 31, 2012, the results of operations for the three and six months ended December 31, 2012 and 2011, comprehensive income for the three and six months ended December 31, 2012 and 2011, the changes in stockholders equity for the six months ended December 31, 2012 and 2011, and the cash flows for the six months ended December 31, 2012 and 2011. Operating results for the six months ended December 31, 2012 are not necessarily indicative of the results that may be expected for the fiscal year ending June 30, 2013 (Fiscal 2013). For further information, refer to the audited consolidated financial statements and notes thereto for the fiscal year ended June 30, 2012 (Fiscal 2012) included in the Company s Annual Report on Form 10-K filed with the Securities and Exchange Commission.

2. Recent Accounting Pronouncements

In December 2011, the Financial Accounting Standards Board (FASB) issued ASU No. 2011-11, *Balance Sheet (Topic 210): Disclosures about Offsetting Assets and Liabilities* (ASU 2011-11). The update requires entities to disclose information about offsetting and related arrangements of financial instruments and derivative instruments. The amendments require enhanced disclosures by requiring improved information about financial instruments and derivative instruments that are either (i) offset in accordance with current literature or (ii) subject to an enforceable master netting arrangement or similar agreement, irrespective of whether they are offset in accordance with current literature. ASU 2011-11 is effective for fiscal years, and interim periods within those years, beginning on or after January 1, 2013. The Company does not anticipate that the adoption of this guidance will have a material impact on the consolidated financial statements.

In June 2011, the FASB issued ASU No. 2011-05, *Comprehensive Income (Topic 220): Presentation of Comprehensive Income* (ASU 2011-05). The objective of this update is to improve the comparability, consistency, and transparency of financial reporting and to increase the prominence of items reported in other comprehensive income. The amendments in this update require that all non-owner changes in stockholders equity be presented either in as single continuous statement of comprehensive income or in two separate but consecutive statements. The amendments are effective for interim and annual periods beginning after December 15, 2011. The adoption of this guidance did not have a material impact on the consolidated financial statements.

In December 2011, the FASB issued ASU No. 2011-12, *Comprehensive Income (Topic 220): Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05.* The amendments in this update defer those changes in ASU 2011-05 that relate to the presentation of reclassifications out of accumulated other comprehensive income on the components of net income and other comprehensive income for all periods presented. All other requirements in ASU 2011-05 are not affected by this update. The amendments are effective for interim and annual periods beginning after December 15, 2011. The adoption of this guidance did not have a material impact on the consolidated financial statements.

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3. Securities Available-for-Sale

Securities available-for-sale at amortized cost and approximate fair values are summarized below:

	December 31, 2012		June 30, 2012	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
	(Dollars in thousands)			
U.S. Government agency securities	$ 45,556	$ 45,618	$ 45,824	$ 45,808
Agency mortgage-backed securities	88,128	87,745	86,816	87,456
	$ 133,684	$ 133,363	$ 132,640	$ 133,264

The gross unrealized gains and unrealized losses on available-for-sale securities are as follows:

	December 31, 2012		June 30, 2012	
	Gross Unrealized Gains	Gross Unrealized Losses	Gross Unrealized Gains	Gross Unrealized Losses
	(Dollars in thousands)			
U.S. Government agency securities	$ 62	$ 0	$ 5	$ 21
Agency mortgage-backed securities	95	478	640	0
	$ 157	$ 478	$ 645	$ 21

When securities are sold, the adjusted cost of the specific security sold is used to compute the gain or loss on sale. The following table summarizes realized gains and losses on available-for-sale securities.

	Three Months Ended December 31,		Six Months Ended December 31,	
	2012	2011	2012	2011
	(Dollars in thousands)			
Gross realized gains	$ 0	$ 433	$ 831	$ 447
Gross realized losses	0	0	(39)	(67)
Net security gains	$ 0	$ 433	$ 792	$ 380

At December 31, 2012, investment securities with a fair value of approximately $43.1 million were pledged as collateral to secure outstanding borrowings.

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

	December 31, 2012					
	Less than 12 Months		More than 12 Months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	(Dollars in thousands)					
U.S. Government agency securities	$ 0	$ 0	$ 0	$ 0	$ 0	$ 0
Agency mortgage-backed securities	68,560	478	0	0	68,560	478
	$ 68,560	$ 478	$ 0	$ 0	$ 68,560	$ 478

	June 30, 2012					
	Less than 12 Months		More than 12 Months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	(Dollars in thousands)					
U.S. Government agency securities	$ 36,585	$ 21	$ 0	$ 0	$ 36,585	$ 21
Agency mortgage-backed securities	0	0	0	0	0	0
	$ 36,585	$ 21	$ 0	$ 0	$ 36,585	$ 21

There were no other-than-temporary impairment losses on securities during the three and six months ended December 31, 2012 or 2011.

At December 31, 2012, the Company did not have any securities in a continuous loss position for greater than twelve months. At December 31, 2012, all of the Company s available-for-sale securities were issued or guaranteed by either government agencies or

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government-sponsored enterprises. The decline in fair value of the Company s available-for-sale securities at December 31, 2012 is attributable to changes in interest rates.

Management of the Company, in addition to considering current trends and economic conditions that may affect the quality of individual securities within the Company s investment portfolio, also considers the Company s ability and intent to hold such securities to maturity or recovery of cost. Management does not believe any of the Company s available-for-sale securities are other-than-temporarily impaired at December 31, 2012.

The amortized cost and fair values of available-for-sale debt securities by contractual maturity are shown below as of December 31, 2012. Actual maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Amortized Cost	Fair Value
	(Dollars in thousands)	
Due within one year	$ 12,080	$ 12,096
Due after one year through five years	33,476	33,522
Due after five years through ten years	47,276	47,135
Due after ten years	40,852	40,610
	$ 133,684	$ 133,363

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4. Loans, Allowance for Loan Losses and Credit Quality

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

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

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

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

The composition of the Company s loan portfolio follows.

	December 31, 2012			June 30, 2012		
	Originated	Purchased	Total	Originated	Purchased	Total
	(Dollars in thousands)					
Residential real estate	$ 84,678	$ 4,254	$ 88,932	$ 90,944	$ 3,931	$ 94,875

Home equity	39,041	0	39,041	42,696	0	42,696
Commercial real estate	103,071	129,470	232,541	100,196	80,539	180,735
Construction	42	0	42	1,187	0	1,187
Commercial business	17,134	0	17,134	19,612	0	19,612
Consumer	14,893	0	14,893	17,149	0	17,149
Total loans	$ 258,859	$ 133,724	$ 392,583	$ 271,784	$ 84,470	$ 356,254

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Purchased credit impaired (PCI) loans include those loans acquired with specific evidence of deterioration of credit quality since origination and for which it is probable, at acquisition, that the Company will be unable to collect all contractually required payments receivable. The Company does not characterize purchased loans with no or insignificant credit impairment as PCI loans. The following table presents a summary of PCI loans purchased by the LASG during the six months ended December 31, 2012 and 2011.

	PCI Loans Acquired Six Months Ended December 31, 2012	2011
	(Dollars in thousands)	
Contractually required payments receivable	$ 44,575	$ 10,064
Nonaccretable difference	(10,814)	(2,958)
Cash flows expected to be collected	33,761	7,106
Accretable yield	(14,214)	(3,122)
Fair value of loans acquired	$ 19,547	$ 3,984

	PCI Loans: Activity in Accretable Yield Six Months Ended December 31, 2012	2011
	(Dollars in thousands)	
Beginning balance	$ 7,169	$ 0
Accretion	(2,052)	(564)
Acquisitions	14,214	3,122
Reclassifications from nonaccretable difference	894	210
Disposals and transfers	(2,951)	(614)
Other changes	23	0
End balance	$ 17,297	$ 2,154

The following table provides information related to the unpaid principal balance and carrying amounts of PCI loans.

	December 31, 2012	June 30, 2012
	(Dollars in thousands)	
Unpaid principal balance	$ 49,768	$ 21,359
Carrying amount	$ 30,104	$ 13,866

Allowance for Loan Losses

The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

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

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

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

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

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

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

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

- Levels and trends in delinquencies
- Trends in the volume and nature of loans
- Trends in credit terms and policies, including underwriting standards, procedures and practices, and the experience and ability of lending management and staff
- Trends in portfolio concentration
- National and local economic trends and conditions.
- Effects of changes or trends in internal risk ratings
- Other effects resulting from trends in the valuation of underlying collateral

There were no changes in the Company s policies or methodology pertaining to the general component of the allowance for loan losses during the three and six months ended December 31, 2012.

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

For all portfolio segments, except the purchased loan segment, a loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower s prior payment record, and the amount of the shortfall in relation to the principal and interest owed. For the purchased loan segment, a loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to realize cash flows as estimated at acquisition. Loan impairment of purchased loans is measured based on the decrease in expected cash flows from those estimated at acquisition, excluding changes due to decreases in interest rate indices, discounted at the loan s effective rate assumed at acquisition. Factors considered by management in determining impairment include payment status, collateral value, and the probability of the collecting scheduled principal and interest payments when due.

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

	Three months ended December 31, 2012					
	Residential Real Estate	Commercial Real Estate	Commercial Business	Consumer	Purchased (1)	Total
	(Dollars in thousands)					
Beginning balance	$ 301	$ 71	$ 53	$ 243	$ 0	$ 668
Provision (benefit)	199	32	(6)	22	0	247
Recoveries	0	0	0	5	0	5
Charge-offs	(8)	(1)	0	(36)	0	(45)
Ending balance	$ 492	$ 102	$ 47	$ 234	$ 0	$ 875

	Three months ended December 31, 2011					
	Residential Real Estate	Commercial Real Estate	Commercial Business	Consumer	Purchased (1)	Total
	(Dollars in thousands)					
Beginning balance	$ 124	$ 114	$ 418	$ 54	$ 0	$ 710
Provision (benefit)	33	33	(191)	259	0	134
Recoveries	1	0	12	13	0	26
Charge-offs	(33)	0	(8)	(92)	0	(133)
Ending balance	$ 125	$ 147	$ 231	$ 234	$ 0	$ 737

(1) Purchased loans include commercial real estate, commercial business, and commercial loans secured by residential real estate loans. The Company separately analyzes all loans purchased by the LASG from other segments in determining the allowance for loan losses under ASC 310-30.

	Six months ended December 31, 2012		
	Residential Real Estate	Commercial Real Estate	Commercial Business