Citizens Community Bancorp Inc.
Form 10-Q
August 07, 2017

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

FORM 10-Q

(Mark One)
x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2017
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 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)

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 preceding 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 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
		Emerging growth company	¨

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ¨

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 August 7, 2017 there were 5,276,724 shares of the registrant's common stock, par value $0.01 per share, outstanding.

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PART 1 – FINANCIAL INFORMATION

As disclosed in our Annual Report on Form 10-K for the fiscal year ended September 30, 2016, which was filed on December 29, 2016, we have restated the unaudited interim and audited annual financial statements for the fiscal years ended September 30, 2014 and 2015 and the quarterly periods ended December 31, 2015, March 31, 2016 and June 30, 2016 (the “Restated Periods”) due to errors identified in such financial statements related to the accrual for professional expenses for the Restated Periods. For further discussion of the effects of the 2016 restatements, please refer to the following portions of this Quarterly Report on Form 10-Q: Part 1, Item 1. Financial Statements, Note 1 to Consolidated Financial Statements, Nature of Business and Summary of Significant Accounting Policies and Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations.

ITEM 1. FINANCIAL STATEMENTS

CITIZENS COMMUNITY BANCORP, INC.
Consolidated Balance Sheets
June 30, 2017 (unaudited) and September 30, 2016
(derived from audited financial statements)
(in thousands, except share data)

	June 30, 2017	September 30, 2016
Assets		
Cash and cash equivalents	$33,749	$10,046
Other interest-bearing deposits	995	745
Securities available for sale	78,475	80,123
Securities held to maturity	5,653	6,669
Non-marketable equity securities, at cost	4,498	5,034
Loans receivable	519,403	574,439
Allowance for loan losses	(5,756)	(6,068)
Loans receivable, net	513,647	568,371
Office properties and equipment, net	5,023	5,338
Accrued interest receivable	1,950	2,032
Intangible assets	753	872
Goodwill	4,663	4,663
Foreclosed and repossessed assets, net	622	776
Other assets	15,613	11,196
TOTAL ASSETS	$665,641	$695,865
Liabilities and Stockholders' Equity		
Liabilities:		
Deposits	$519,133	$557,677
Federal Home Loan Bank advances	67,900	59,291
Other borrowings	11,000	11,000
Other liabilities	1,598	3,353
Total liabilities	599,631	631,321
Stockholders' equity:		
Common stock— $0.01 par value, authorized 30,000,000, 5,270,895 and 5,260,098 shares issued and outstanding, respectively	53	53
Additional paid-in capital	55,089	54,963
Retained earnings	11,221	9,107
Unearned deferred compensation	(214)	(193)
Accumulated other comprehensive (loss) income	(139)	614
Total stockholders' equity	66,010	64,544
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$665,641	$695,865

See accompanying condensed notes to unaudited consolidated financial statements.

CITIZENS COMMUNITY BANCORP, INC.
Consolidated Statements of Operations (unaudited)
Three and Nine Months Ended June 30, 2017 and 2016 (As Restated)
(in thousands, except per share data)

	Three Months Ended		Nine Months Ended	
	June 30, 2017	June 30, 2016 (As Restated)	June 30, 2017	June 30, 2016 (As Restated)
Interest and dividend income:				
Interest and fees on loans	$6,030	$ 6,072	$18,632	$ 16,623
Interest on investments	591	402	1,476	1,267
Total interest and dividend income	6,621	6,474	20,108	17,890
Interest expense:				
Interest on deposits	1,035	1,081	3,204	2,988
Interest on FHLB borrowed funds	164	167	500	496
Interest on other borrowed funds	107	47	308	47
Total interest expense	1,306	1,295	4,012	3,531
Net interest income before provision for loan losses	5,315	5,179	16,096	14,359
Provision for loan losses	—	—	—	75
Net interest income after provision for loan losses	5,315	5,179	16,096	14,284
Non-interest income:				
Net gains on sale of available for sale securities	—	43	29	47
Service charges on deposit accounts	325	410	1,065	1,164
Loan fees and service charges	475	302	1,372	886
Settlement proceeds	—	—	283	—
Other	302	258	870	676
Total non-interest income	1,102	1,013	3,619	2,773
Non-interest expense:				
Compensation and benefits	2,506	2,378	7,888	6,784
Occupancy	565	554	2,196	1,835
Office	304	350	897	864
Data processing	476	445	1,402	1,274
Amortization of core deposit intangible	38	31	119	66
Advertising, marketing and public relations	75	174	243	456
FDIC premium assessment	79	86	231	255
Professional services	382	333	1,218	789
Other	305	453	1,034	1,006
Total non-interest expense	4,730	4,804	15,228	13,329
Income before provision for income taxes	1,687	1,388	4,487	3,728
Provision for income taxes	604	513	1,530	1,331
Net income attributable to common stockholders	$1,083	$ 875	$2,957	$ 2,397
Per share information:				
Basic earnings	$0.21	$ 0.16	$0.56	$ 0.45
Diluted earnings	$0.20	$ 0.16	$0.56	$ 0.45
Cash dividends paid	$—	$ —	$0.16	$ 0.12

See accompanying condensed notes to unaudited consolidated financial statements.

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CITIZENS COMMUNITY BANCORP, INC.
Consolidated Statements of Comprehensive Income (unaudited)
Nine months ended June 30, 2017 and 2016 (As Restated)
(in thousands, except per share data)

	Nine Months Ended June 30, 2017	June 30, 2016 (As Restated)
Net income attributable to common stockholders	$2,957	$ 2,397
Other comprehensive income, net of tax:		
Securities available for sale		
Net unrealized (losses) gains arising during period	(770)	1,006
Reclassification adjustment for gains included in net income	17	28
Other comprehensive (loss) income	(753)	1,034
Defined benefit plans:		
Amortization of unrecognized prior service costs and net losses	—	(35)
Total other comprehensive (loss) income, net of tax	(753)	999
Comprehensive income	$2,204	$ 3,396

See accompanying condensed notes to unaudited consolidated financial statements.

CITIZENS COMMUNITY BANCORP, INC.
Consolidated Statement of Changes in Stockholders’ Equity (unaudited)
Nine Months Ended June 30, 2017
(in thousands, except shares and per share data)

	Common Stock		Additional Paid-In Capital	Retained Earnings	Unearned Deferred Compensation	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity
	Shares	Amount					
Balance, October 1, 2016	5,260,098	$ 53	$ 54,963	$ 9,107	$ (193)	$ 614	$ 64,544
Net income				2,957			2,957
Other comprehensive loss, net of tax						(753)	(753)
Surrender of restricted shares of common stock	(1,375)		(17)				(17)
Common stock awarded under the equity incentive plan	5,500		69		(69)		—
Common stock repurchased	(1,428)		(16)				(16)
Common stock options exercised	8,100		67				67
Stock option expense			23				23
Amortization of restricted stock					48		48
Cash dividends ($0.16 per share)				(843)			(843)
Balance, June 30, 2017	5,270,895	$ 53	$ 55,089	$ 11,221	$ (214)	$ (139)	$ 66,010

See accompanying condensed notes to unaudited consolidated financial statements.

CITIZENS COMMUNITY BANCORP, INC.
Consolidated Statements of Cash Flows (unaudited)
Nine Months Ended June 30, 2017 and 2016 (As Restated)
(in thousands, except per share data)

	Nine Months Ended June 30, 2017		June 30, 2016 (As Restated)	
Cash flows from operating activities:				
Net income attributable to common stockholders	$ 2,957		$ 2,397	
Adjustments to reconcile net income to net cash provided by operating activities:				
Net amortization of premium/discount on securities	575		851	
Depreciation	674		583	
Provision for loan losses	—		75	
Net realized gain on sale of securities	(29	)	(47	)
Amortization of core deposit intangible	119		66	
Amortization of restricted stock	48		33	
Stock based compensation expense	23		25	
Loss on sale of office properties	2		—	
Provision for deferred income taxes	456		555	
Net losses from disposals of foreclosed properties	(16	)	(77	)
Increase in accrued interest receivable and other assets	(498	)	(1,218	)
Decrease in other liabilities	(1,755	)	(226	)
Total adjustments	(401	)	620	
Net cash provided by operating activities	2,556		3,017	
Cash flows from investing activities:				
Purchase of investment securities	(16,239	)	(15,062	)
Purchase of bank owned life insurance	(3,500	)	—	
Net increase in interest-bearing deposits	(250	)	7,241	

Proceeds from sale of securities available for sale	10,644		17,665	
Principal payments on investment securities	6,458		11,301	
Proceeds from sale of non-marketable equity securities	953		—	
Purchase of non-marketable equity securities	(417	)	(3	)
Proceeds from sale of foreclosed properties	713		892	
Net decrease (increase) in loans	53,888		(5,723	)
Net capital expenditures	(366	)	(711	)
Net cash received in business combinations	—		20,658	
Net cash received from sale of office properties	7		—	
Net cash provided by investing activities	51,891		36,258	
Cash flows from financing activities:				
Net increase (decrease) in Federal Home Loan Bank advances	8,609		(3,017	)
Increase in other borrowings	—		11,000	
Net decrease in deposits	(38,544	)	(49,225	)
Surrender of restricted shares of common stock	(17	)	(49	)
Exercise of common stock options	67		153	
Termination of director retirement plan/supplemental executive retirement plan	—		(35	)
Repurchase shares of common stock	(16	)	—	
Cash dividends paid	(843	)	(629	)
Net cash used in financing activities	(30,744	)	(41,802	)
Net increase (decrease) in cash and cash equivalents	23,703		(2,527	)
Cash and cash equivalents at beginning of period	10,046		23,872	
Cash and cash equivalents at end of period	$ 33,749		$ 21,345	

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Supplemental cash flow information:		
Cash paid during the period for:		
Interest on deposits	$3,172	$2,859
Interest on borrowings	$584	$495
Income taxes	$979	$1,211
Supplemental noncash disclosure:		
Transfers from loans receivable to foreclosed and repossessed assets	$543	$542
Fair value of assets acquired, net of cash and cash equivalents	$—	$168,129
Fair value of liabilities assumed, net of cash and cash equivalents	$—	$154,250

See accompanying condensed notes to unaudited consolidated financial statements.

CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Dollars in thousands, except share data)
(UNAUDITED)
NOTE 1 – NATURE OF BUSINESS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES
The accompanying consolidated financial statements include the accounts of Citizens Community Bancorp, Inc. (the “Company”) and its wholly owned subsidiary, Citizens Community Federal N.A. (the "Bank"), and have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”) for interim financial statements. As used in this quarterly report, the terms “we”, “us”, “our”, and “Citizens Community Bancorp, Inc.” mean the Company and its wholly owned subsidiary, the Bank, unless the context indicates other meaning.
The Bank is a national banking association (a "National Bank") and operates under the title of Citizens Community Federal National Association ("Citizens Community Federal N.A."). The Company is a bank holding company, supervised by the Federal Reserve Bank of Minneapolis (the "FRB"), and operates under the title of Citizens Community Bancorp, Inc. The U.S. Office of the Comptroller of the Currency (the "OCC"), is the primary federal regulator for the Bank.
The consolidated income of the Company is principally derived from the income of the Bank, the Company’s wholly owned subsidiary. The Bank originates commercial, agricultural, residential, consumer and commercial and industrial (C&I) loans and accepts deposits from customers, primarily in Wisconsin, Minnesota and Michigan. The Bank operates 14 full-service offices, 12 stand-alone locations and 2 branches located inside Walmart Supercenters.
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 consolidated financial statements, we evaluated the events and transactions that occurred subsequent to the balance sheet date as of June 30, 2017 and through the date the financial statements were available to be issued for items that should potentially be recognized or disclosed in these consolidated financial statements.

Effective May 16, 2016, Community Bank of Northern Wisconsin ("CBN") was acquired through merger (“Merger”) by the Bank. The Merger was consummated pursuant to the terms of a Plan and Agreement of Merger (“Merger Agreement”), dated February 10, 2016, as amended by the First Amendment to Agreement and Plan of Merger dated as of May 13, 2016 by and among the Bank, Old Murry Bancorp, Inc. ("Old Murry"), the controlling shareholders of Old Murry, and CBN. In accordance with the terms of the Merger Agreement, the Bank agreed to purchase all of the assets and assume all of the liabilities of CBN. The total purchase price paid in cash by the Bank was $17,447, which represented a $16,762 book value of the CBN as of April 30, 2016, less a capital dividend of $4,342 declared by CBN to Old Murry, plus a $5,000 fixed premium and daily interest through May 16, 2016 in the amount of $27. The purchase price was funded by $11,000 of debt, and the remaining $6,447 of cash.

On March 17, 2017, the Company and Wells Financial Corp., a Minnesota corporation (“Wells”) entered into an Agreement and Plan of Merger (the “Merger Agreement”). Under the Merger Agreement, Wells will merge with and into the Company with the Company surviving the merger (the “Merger”) in a transaction valued at approximately $39,800.

Pursuant to the terms and subject to the conditions of the Merger Agreement, which has been approved by the boards of directors of each of the Company and Wells, the Merger Agreement provides for the payment to Wells stockholders of total
consideration of (i) $41.31 in cash and (ii) .7636 shares of the Company's common stock. The stock consideration is subject to a pricing collar adjustment in certain circumstances based on the Company's common stock price at the time of closing. In the event of a termination of the Merger Agreement,Wells may be required to pay a termination fee of $1,600.

At the closing of the Merger Agreement, Wells Federal Bank ("Wells Bank), a Minnesota state-chartered bank and a wholly-owned subsidiary of Wells and the Bank, will enter into an Agreement and Plan of Merger pursuant to which Wells Bank will merge with and into the Bank, with the Bank surviving the bank merger.

The Merger Agreement contains customary representations, warranties and covenants made by each of Wells and the Company. Completion of the Merger is subject to certain conditions, including, among others, (i) the approval of the Merger Agreement by Wells' stockholders; (ii) the absence of governmental orders prohibiting or actions seeking to prohibit the
Merger; (iii) the receipt of certain governmental and regulatory approvals; (iv) the absence of an event that would have or could

reasonably be expected to have a material adverse effect on Wells or the Company; and (v) the receipt by Wells of certain third-party consents. The Merger is expected to close during the fourth fiscal quarter of 2017.
The accompanying consolidated 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. Unless otherwise stated herein, and except for shares and per share amounts, all amounts are in thousands.
As disclosed in our Annual Report on Form 10-K for the fiscal year ended September 30, 2016, which was filed on December 29, 2016, we have restated the unaudited interim and audited annual financial statements for the fiscal years ended September 30, 2014 and 2015 and the quarterly periods ended December 31, 2015, March 31, 2016 and June 30, 2016 (the “Restated Periods”) due to errors identified in such financial statements related to the accrual for professional expenses for the Restated Periods. The effect of these restatements on the Company's quarterly consolidated statements of operations for the three and nine months ended June 30, 2016 compared to the initially reported results, are as follows: Total non-interest expense increased by $151 for the quarter ended June 30, 2016 and $215 for the nine months ended June 30, 2016. Net income decreased by $92 for the quarter ended June 30, 2016 and $131 for the nine months ended June 30, 2016. The effects of the restatements on the Company's consolidated balance sheets, consolidated statements of cash flows and earnings per share for the restated three and nine months ended June 30, 2016 were not material. For additional details on the effects of the restatement on certain line items within our previously reported financial statements during the Restated Periods, please refer to the following portions of this Quarterly Report on Form 10-Q: Part 1, Item 1. Financial Statements, and Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations, as well as the following portions of our Annual Report on Form 10-K: Explanatory Note Regarding Restatement; Part II, Item 7 Management’s Discussion and Analysis of Financial Condition and Results of Operations, Item 8 Financial Statements and Supplementary Data, Note 2, Restatement of Previously Issued Financial Statements, and Item 9A Controls and Procedures.
Principles of Consolidation – The accompanying consolidated financial statements include the accounts of the Company and the Bank. All significant intercompany accounts and transactions have been eliminated.
Use of Estimates – Preparation of consolidated 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 best 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, indefinite-lived intangible assets and long-lived assets, deferred tax assets, uncertain income tax positions and contingencies. Management does not anticipate any material changes to estimates made herein in the near term. Factors that may cause sensitivity to the aforementioned estimates include, but are not limited to, external market factors such as market interest rates and unemployment rates, changes to operating policies and procedures, and changes in applicable banking regulations. Actual results may ultimately differ from estimates, although management does not generally believe such differences would materially affect the consolidated financial statements in any individual reporting period.
Investment Securities; Held to Maturity and Available for Sale – Management determines the appropriate classification of investment securities at the time of purchase and reevaluates such designation as of the date of each balance sheet. Securities are classified as held to maturity when the Company has the positive intent and ability to hold the securities to maturity. Held to maturity securities are stated at amortized cost. Investment securities not classified as held to maturity are classified as available for sale. Available for sale securities are stated at fair value, with unrealized holding gains and losses deemed other than temporarily impaired due to non-credit issues being reported in other comprehensive income (loss), net of tax. Unrealized losses deemed other-than-temporary due to credit issues are reported in the Company’s net income in the period in which the losses arise. 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 underlying securities.
The Company evaluates 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 issuer is assessed. Significant inputs used to measure the amount of other-than-temporary impairment related to credit loss include, but are not limited to, default and delinquency rates of the underlying collateral, remaining credit support, and historical loss severities. Adjustments to market value of available for sale securities that are considered temporary are recorded as separate components of equity, net of tax. If the unrealized loss of a security is identified as other-than-temporary based on information available, such as the decline in the creditworthiness 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 Company's consolidated statement of operations. Unrealized losses on available for sale securities, other than credit, will continue to be recognized in other comprehensive income (loss), net of tax.

Loans – Loans that management has the intent and ability to hold for the foreseeable future, until maturity or payoff are reported at the principal balance outstanding, net of unearned interest, and net of deferred loan fees and costs. Interest income is accrued on the unpaid principal balance of these loans. Loan origination fees, net of certain direct origination costs, are deferred and recognized in interest income using the interest method without anticipating prepayments. Delinquency fees are recognized into income when chargeable, assuming collection is reasonably insured.

Interest income on commercial, mortgage and consumer loans is discontinued according to the following schedules:

•Commercial/agricultural real estate loans past due 90 days or more;

•Commercial/agricultural non-real estate loans past due 90 days or more;

•Closed end consumer non-real estate loans past due 120 days or more; and

•Residential real estate loans and open ended consumer non-real estate loans past due 180 days or more.

Past due status is based on the contractual terms of the loan. In all cases, loans are placed on nonaccrual status 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 nonaccrual status is reversed against interest income. Interest received on such loans is accounted for on the cash basis or cost recovery method, and is generally applied against principal, until qualifying for return to accrual status. Loans are returned to accrual status when payments are made that bring the loan account current with the contractual term of the loan and a 6 month payment history has been established. Interest on impaired loans considered troubled debt restructurings (“TDRs”) or substandard, less than 90 days delinquent, is recognized as income as it accrues based on the revised terms of the loan over an established period of continued payment. Substandard loans, as defined by the OCC, our primary banking regulator, are loans that are inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any.

Residential 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 past due 180 days or more. 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 past due 120 days or more. Commercial loans, including agricultural and C&I 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 past due 180 days or more for open ended loans or loans secured by real estate collateral, or the loan becomes 120 days past due or more for loans secured by non-real estate collateral.

The Company defines Acquired Loans as all loans acquired in a business combination accounted for under Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") Topic 805, "Business Combinations". These loans include, but are not limited to loans accounted for under FASB ASC 310-30, "Loans and Debt Securities Acquired with Deteriorated Credit Quality" as discussed below. All other loans are defined as Originated Loans.

Allowance for Loan Losses – The allowance for loan losses (“ALL”) is a valuation allowance for probable and inherent credit losses in our loan portfolio. Loan losses are charged against the 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 required ALL balance taking into account the following factors: past loan loss experience; the nature, volume and composition of our loan portfolio; known and inherent risks in our loan portfolio; information about specific borrowers’ ability to repay; estimated collateral values; current economic conditions; and other relevant factors determined by management. 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 our management’s judgment, should be charged off.

A loan is impaired when full payment under the loan terms is not expected. Impaired loans consist of all TDRs, as well as individual substandard loans not considered a TDR when full payment under the loan terms is not expected.

All TDRs are individually evaluated for impairment. See Note 3, “Loans, Allowance for Loan Losses and Impaired Loans” for more information on what we consider to be a TDR. If a TDR or substandard loan is deemed to be impaired, a specific ALL allocation may be established so that the loan is reported, net, at the lower of (a) outstanding principal balance, (b) the present value of estimated future cash flows using the loan’s existing rate; or (c) at the fair value of any collateral, less estimated disposal costs, if repayment is expected solely from the underlying collateral of the loan. For TDRs less than 90 days past due, and certain substandard loans that are less than 90 days delinquent, the likelihood of the loan migrating to over 90 days past due is also taken into account when determining the specific ALL allocation for these particular loans. Large groups of smaller balance homogeneous loans, such as consumer and residential real estate loans, as well as non-TDR commercial loans, are collectively evaluated for impairment, and accordingly, are not separately identified for impairment disclosures.

Loans Acquired through Business Combination with Deteriorated Credit Quality - ASC Topic 310-30, "Loan and Debt Securities Acquired with Deteriorated Credit Quality", applies to loans acquired in a business combination that have evidence of deterioration of credit quality since origination and for which it is probable, at acquisition, that we will be unable to collect all contractually required payments receivable. In accordance with this guidance, these loans are initially recorded at fair value (as determined by the present value of expected future cash flows) with no valuation allowance. The difference between the undiscounted cash flows expected at acquisition and the investment in the loan, or the “accretable yield”, is recognized as interest income over the life of the loans using a method that approximates the level-yield method. Contractually required payments for interest and principal that exceed the undiscounted cash flows expected at acquisition, or the “nonaccretable difference”, are not recognized as a yield adjustment, a loss accrual, or a valuation allowance, Increases in expected cash flows subsequent to the initial investment are recognized prospectively through adjustment of the yield on the loan over its remaining life. Decreases in expected cash flows are recognized as impairments. Valuation allowances on these impaired loans reflect only losses incurred after the acquisition.

Foreclosed and Repossessed Assets, net – Assets acquired through foreclosure or repossession are initially recorded at fair value, less estimated costs to sell, which establishes a new cost basis. If the fair value declines subsequent to foreclosure or repossession, a valuation allowance is recorded through expense. Costs incurred after acquisition are expensed and are included in non-interest expense, other on our Consolidated Statements of Operations.

Goodwill - Goodwill resulting from the acquisition by merger of CBN was determined as the excess of the fair value of the consideration transferred, over the fair value of the net assets acquired, less liabilities assumed in the acquisition by merger, as of the acquisition date. Goodwill resulting from the selective purchase of loans and deposits from Central Bank in February 2016 was determined as the excess of the Premium Deposit less the Core Deposit Intangible as of the acquisition date. Goodwill is determined to have an indefinite useful life, and is not amortized. Goodwill is tested for impairment at least annually or more frequently if events and circumstances exist that indicate that a goodwill impairment test should be performed.

Income Taxes – The Company accounts for income taxes in accordance with the FASB 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 6, "Income Taxes" for details on the Company’s income taxes.

The Company regularly reviews the carrying amount of its net 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 net 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, the length of statutory carryforward periods, any experience with utilization of operating loss and tax credit carryforwards 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. Accordingly, 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 includes the dilutive effect of additional potential common shares issuable during the period, consisting of stock options outstanding under the Company’s stock incentive plans that have an exercise price that is less than the Company's stock price on the reporting date.

Operating Segments—While our chief decision makers monitor the revenue streams of the various banking products and services, operations are managed and financial performance is evaluated on a Company-wide basis. Accordingly, all of the
Company’s banking operations are considered by management to be aggregated in one reportable operating segment.

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

Recent Accounting Pronouncements - In May 2017, the FASB issued Accounting Standards Update ("ASU") 2017-09, "Compensation--Stock Compensation (Topic 718): Scope of Modification Accounting." ASU 2017-09 provides specific guidance as to which changes to terms and conditions of share-based payment awards require an entity to apply modification accounting in Topic 718. For public entities, ASU 2017-09 is effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. Early adoption is permitted. The Company expects the adoption of ASU 2017-09 will have no material effect on the Company's consolidated results of operations, financial position or cash flows.
In March 2017, the FASB issued ASU 2017-08, "Receivables--Nonrefundable fees and Other Costs (Subtopic 310-20): Premium Amortization on Purchased Callable Debt Securities." ASU 2017-08 amends the amortization period for certain purchased callable debt securities held at a premium. For public entities, ASU 2017-08 is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. The Company expects the adoption of ASU 2017-08 will have no material effect on the Company's consolidated results of operations, financial position or cash flows.
In February 2017, the FASB issued ASU 2017-05, "Other Income--Gains and Losses from the Derecognition of Non-financial Assets (Subtopic 610-20): Clarifying the Scope of Asset Derecognition Guidance and Accounting for Partial Sales of Non-financial Assets." ASU 2017-05 clarifies previously issued ASU 2014-09, primarily with respect to (a) derecognition of an in substance non-financial asset, and (b) partial sales of non-financial assets. For public entities, ASU 2017-05 is effective at the same time of adoption of ASU 2014-09, "Revenue from Contracts with Customers (Topic 606)," which is for annual reporting periods beginning after December 15, 2017 and related interim periods. Early adoption is not permitted. The Company expects the adoption of ASU 2017-05 will have no material effect on the Company's consolidated results of operations, financial position or cash flows.
In January, 2017, the FASB issued ASU 2017-04, "Intangibles--Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment." ASU 2017-04 intends to simplify how an entity is required to test goodwill impairment. For public entities, ASU 2017-04 is effective for fiscal years beginning after December 15, 2019, and any related interim annual goodwill impairment tests thereon. The Company expects the adoption of ASU 2017-04 will have no material effect on the Company's consolidated results of operations, financial position or cash flows.
In January, 2017, the FASB issued ASU 2017-01, "Business Combinations (Topic 805): Clarifying the Definition of a Business." ASU 2017-01 narrows the definition of a "business" with respect to accounting for business combinations. For public entities, ASU 2017-01 is effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. The Company expects the adoption of ASU 2017-01 will have no material effect on the Company's consolidated results of operations, financial position or cash flows.
In June, 2016 the FASB issued ASU 2016-13, “Financial Instruments-Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments.” ASU 2016-13 is intended to provide financial statement users with more decision-useful information about the excepted credit losses on financial instruments and other commitments to extend credit. For public entities, ASU 2016-13 is effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. The Company has not yet evaluated the potential effects of adopting ASU 2016-13 on the Company’s consolidated results of operations, financial position or cash flows. We are currently assessing the impact of the standard and evaluating credit loss models. We expect a significant effort to develop new or modified credit loss models and that the timing of the recognition of credit losses will accelerate under the new standard.
In May 2016, the FASB issued ASU 2016-12, “Revenue from Contracts with Customers (Topic 606); Narrow-Scope Improvements and Practical Expedients.” ASU 2016-12 is intended to address certain specific issues identified by the FASB-IASB Joint Transition Resource Group for Revenue Recognition with respect to ASU 2014-09, “Revenue from Contracts with Customers (Topic 606).” For public entities, ASU 2016-12 is effective on a retrospective basis for the annual periods, and interim periods within those annual periods, beginning after December 15, 2017. Early adoption is not permitted. The Company expects the adoption of ASU 2016-12 will have no material effect on the Company's consolidated results of operations, financial position or cash flows. This guidance does not apply to revenue associated with financial instruments, including loans, securities and derivatives that are accounted for under other U.S. GAAP guidance. For that reason, we do not expect it to have a material impact on our consolidated results of operations for

the elements of the statement of operations associated with financial instruments, including securities gains, interest income, and interest expense. However, we do believe that the new standard will result in new disclosure requirements. We are currently in the process of reviewing contracts to assess the impact of the new guidance on our service offerings that are within the scope of the guidance included in non-interest income; such as service charges, payment processing fees, and other service fees. The Company is continuing to evaluate the effect of the new guidance on revenue sources other than financial instruments on our financial position and consolidated results of operations.
In March 2016, the FASB issued ASU 2016-09, "Compensation-Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting." ASU 2016-09 is intended to simplify certain areas of share-based payment

transaction accounting, including the income tax consequences, equity or liability classification of certain share awards, and classification on the statement of cash flows. ASU 2016-09 is effective for the annual periods, and interim periods within those annual periods, beginning after December 15, 2016. Early adoption is permitted. The Company is currently evaluating the effect on the consolidated results of operations, financial position and cash flows.

In February 2016, the FASB issued ASU 2016-02, "Leases (Topic 842)". ASU 2016-02 is intended to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. ASU 2016-02 is effective for the annual periods, and interim periods within those annual periods, beginning after December 15, 2018. Early adoption is permitted. The Company is currently evaluating the provisions of ASU 2016-02, but expects to report increased assets and liabilities as a result of reporting additional leases on the Company's consolidated balance sheet.

In January 2016, the FASB issued ASU 2016-01, "Financial Instruments-overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities”. ASU 2016-01 is intended to address certain aspects of recognition, measurement, presentation and disclosure of financial instruments. For public entities, ASU 2016-01 is effective for the annual periods, and interim periods within those annual periods, beginning after December 15, 2017. Early adoption is not permitted, except for certain provisions of ASU 2016-01, which are not applicable to the Company. The Company expects the adoption of ASU 2016-01 to have no material effect on the Company's consolidated results of operations, financial position or cash flows.

NOTE 2 – FAIR VALUE ACCOUNTING

ASC Topic 820-10, “Fair Value Measurements and Disclosures” 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 the Company has 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 the Company’s assumptions about the factors 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 (Level 1 inputs); or matrix pricing, which is a mathematical technique widely used in the industry to value debt securities without relying exclusively on quoted prices for the specific securities but rather by relying on the securities’ relationship to other benchmark quoted securities (Level 2 inputs). Where such quotes are not available, the Company utilizes independent third party valuation analysis to support the Company’s estimates and judgments in determining fair value (Level 3 inputs).

Assets Measured on a Recurring Basis

The following tables present the financial instruments measured at fair value on a recurring basis as of June 30, 2017 and September 30, 2016:

	Fair Value	Quoted Prices in Active Markets for Identical Instruments (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
June 30, 2017				
Investment securities:				
U.S. government agency obligations	$14,522	$ —	$ 14,522	$ —
Obligations of states and political subdivisions	32,887	—	32,887	—
Mortgage-backed securities	30,930	—	30,930	—
Federal Agricultural Mortgage Corporation	136	—	136	—
Total	$78,475	$ —	$ 78,475	$ —
September 30, 2016				
Investment securities:				
U.S. government agency obligations	$16,407	$ —	$ 16,407	$ —
Obligations of states and political subdivisions	34,012	—	34,012	—
Mortgage-backed securities	29,247	—	29,247	—
Federal Agricultural Mortgage Corporation	81	—	81	—
Trust preferred securities	376	—	—	376
Total	$80,123	$ —	$ 79,747	$ 376

The following table presents additional information about the security available for sale measured at fair value on a recurring basis and for which the Company utilized significant unobservable inputs (Level 3 inputs) to determine fair value for the nine months ended June 30, 2017 and year ended September 30, 2016:

	Fair value measurements using significant unobservable inputs (Level 3)	
Securities available for sale	Nine months ended June 30, 2017	Year ended September 30, 2016
Balance, beginning of period	$ 376	$ —
Payments received	(500)	—
Total gains or losses (realized/unrealized)		
Included in earnings	124	—
Included in other comprehensive income	—	—
Transfers in and/or out of Level 3	—	376
Balance, end of period	$ —	$ 376

Assets Measured on a Nonrecurring Basis

The following tables present the financial instruments measured at fair value on a nonrecurring basis as of June 30, 2017 and September 30, 2016:

	Fair Value	Quoted Prices in Active Markets for Identical Instruments (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
June 30, 2017				
Foreclosed and repossessed assets, net	$622	$ —	$ —	$ 622
Impaired loans with allocated allowances	1,328	—	—	1,328
Total	$1,950	$ —	$ —	$ 1,950
September 30, 2016				
Foreclosed and repossessed assets, net	$776	$ —	$ —	$ 776
Impaired loans with allocated allowances	2,412	—	—	2,412
Total	$3,188	$ —	$ —	$ 3,188

The fair value of impaired loans referenced above was determined by obtaining independent third party appraisals and/or internally developed collateral valuations to support the Company's estimates and judgments in determining the fair value of the underlying collateral supporting impaired loans.

The fair value of foreclosed and repossessed assets was determined by obtaining market price valuations from independent third parties wherever such quotes were available for other collateral owned. The Company utilized independent third party appraisals to support the Company's estimates and judgments in determining fair value for other real estate owned.

The following table represents additional quantitative information about assets measured at fair value on a recurring and nonrecurring basis and for which we have utilized Level 3 inputs to determine their fair value at June 30, 2017.

	Fair Value	Valuation Techniques (1)	Significant Unobservable Inputs (2)	Range
June 30, 2017				
Foreclosed and repossessed assets, net	$622	Appraisal value	Estimated costs to sell	10 - 15%
Impaired loans with allocated allowances	$1,328	Appraisal value	Estimated costs to sell	10 - 15%
September 30, 2016				
Foreclosed and repossessed assets, net	$776	Appraisal value	Estimated costs to sell	10 - 15%
Impaired loans with allocated allowances	$2,412	Appraisal value	Estimated costs to sell	10 - 15%

(1) Fair value is generally determined through independent third-party appraisals of the underlying collateral, which generally includes various level 3 inputs which are not observable.

(2) The fair value basis of impaired loans and real estate owned may be adjusted to reflect management estimates of disposal costs including, but not limited to, real estate brokerage commissions, legal fees, and delinquent property taxes.

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 determined as follows:

Cash and Cash Equivalents
Due to their short-term nature, the carrying amounts of cash and cash equivalents are considered to be a reasonable estimate of fair value and represents a level 1 measurement.
Other Interest-Bearing Deposits
Fair value of interest bearing deposits is estimated using a discounted cash flow analysis based on current interest rates being offered by instruments with similar terms and represents a level 3 measurement.
Non-marketable Equity Securities, at cost
Non-marketable equity securities are comprised of Federal Home Loan Bank stock and Federal Reserve Bank stock carried at cost, which are their redeemable fair values since the market for each category of this stock is restricted and represents a level 1 measurement.
Loans Receivable, net
Fair value is estimated for portfolios of loans with similar financial characteristics. Loans are segregated by type such as real estate, C&I 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. The fair value of variable rate loans approximates carrying value. The net carrying value of the loans acquired through the CBN acquisition approximates the fair value of the loans at June 30, 2017. The fair value of loans is considered to be a level 3 measurement.
Impaired Loans (carried at fair value)
Impaired loans are loans in which the Company has measured impairment, generally based on the fair value of the loan's collateral. Fair value is generally determined based upon independent third-party appraisals of the properties, or discounted cash flows based upon the expected proceeds. These assets are included as Level 3 fair values, based upon the lowest level of input that is significant to the fair value measurements.

Foreclosed Assets (carried at fair value)
Foreclosed assets are the only non-financial assets valued on a non-recurring basis which are held by the Company at fair value, less cost to sell. At foreclosure or repossession, if the fair value, less estimated costs to sell, of the collateral acquired (real estate, vehicles, equipment) is less than the Company's recorded investment in the related loan, a write-down is recognized through a charge to the allowance for loan losses. Additionally, valuations are periodically performed by management and any subsequent reduction in value is recognized by a charge to income. The fair value of foreclosed assets held-for-sale is estimated using Level 3 inputs based on observable market data.
Accrued Interest Receivable and Payable
Due to their short-term nature, the carrying amounts of accrued interest receivable and payable are considered to be a reasonable estimate of fair value and represents a level 1 measurement.
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 and represents a level 1 measurement. The fair value of fixed rate certificate accounts is calculated by using discounted cash flows applying interest rates currently being offered on similar certificates and represents a level 3 measurement. The net carrying value of fixed rate certificate accounts acquired through the CBN acquisition approximates the fair value of the certificates at June 30, 2017 and represents a level 3 measurement.
Federal Home Loan Bank ("FHLB") Advances
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 borrowed funds approximates their fair value and represents a level 2 measurement.

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’s consolidated financial statements, no amount for fair value is presented. The table below represents what we would receive to sell an asset or what we would have to pay to transfer a liability in an orderly transaction between market participants at the measurement date. The carrying amount and estimated fair value of the Company's financial instruments as of the dates indicated below were as follows:

		June 30, 2017		September 30, 2016	
	Valuation Method Used	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Financial assets:					
Cash and cash equivalents	(Level 1)	$33,749	$33,749	$10,046	$10,046
Other interest-bearing deposits	(Level 1)	995	999	745	760
Securities available for sale	See above	78,475	78,475	80,123	80,123
Securities held to maturity	(Level II)	5,653	5,810	6,669	6,944
Non-marketable equity securities, at cost	(Level II)	4,498	4,498	5,034	5,034
Loans receivable, net	(Level III)	513,647	524,644	568,371	585,679
Accrued interest receivable	(Level 1)	1,950	1,950	2,032	2,032
Financial liabilities:					
Deposits	(Level III)	$519,133	$522,470	$557,677	$561,919
FHLB advances	(Level III)	67,900	67,896	59,291	59,557
Other borrowings	(Level 1)	11,000	11,000	11,000	11,000
Other liabilities	(Level 1)	1,439	1,439	3,231	3,231
Accrued interest payable	(Level 1)	159	159	122	122

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

Portfolio Segments:

Residential real estate loans are collateralized by primary and secondary positions on real estate and are underwritten primarily based on borrower's documented income, credit scores, and collateral values. Under consumer home equity loan guidelines, the borrower will be approved for a loan based on a percentage of their home's appraised value less the balance owed on the existing first mortgage. Credit risk is minimized within the residential real estate portfolio as relatively small loan amounts are spread across many individual borrowers. Management evaluates trends in past due loans and current economic factors such as the housing price index on a regular basis.

Commercial and agricultural real estate loans are underwritten after evaluating and understanding the borrower's ability to operate profitably and prudently expand its business. Management examines current and projected cash flows to determine the ability of the borrower to repay its obligations as agreed. These loans are viewed primarily as cash flow loans and secondarily as loans secured by real estate. Commercial real estate lending typically involves higher loan principal amounts and the repayment of these loans is generally largely dependent on the successful operation of the property or the business conducted on the property securing the loan. Commercial real estate loans may be more adversely affected by conditions in the real estate markets or in the general economy. The level of owner-occupied property versus non-owner-occupied property are tracked and monitored on a regular basis. Local commercial real estate municipal loans are based on unrestricted assets, tax base and overall borrowing capacity. Agricultural real estate loans are primarily comprised of loans for the purchase of farmland. Loan-to-value ratios on loans secured by farmland generally do not exceed 75%. Land development loans are underwritten using feasibility studies, independent appraisal reviews and financial analysis of the developers or property owners. Commercial construction loans are based upon estimates of cost and value of the completed project. Commercial construction loans often involve the disbursement of substantial funds with the repayment dependent on the success of the ultimate project. Sources of repayment for these loans may be the sale of the developed property or increased cash flow as a result of business expansion.

Consumer non-real estate loans are comprised of originated indirect paper loans secured primarily by boats and recreational vehicles, purchased indirect paper loans secured primarily by household goods and other consumer loans secured primarily by automobiles and other personal assets. Consumer loans underwriting terms often depend on the collateral type, debt to income ratio and the borrower's creditworthiness as evidenced by their credit score. Collateral value alone may not provide an adequate source of repayment of the outstanding loan balance in the event of a consumer non-real estate default. This shortage is a result of the greater likelihood of damage, loss and depreciation for consumer based collateral.

Commercial and agricultural non-real estate loans are primarily made based on the identified cash flows of the borrower and secondarily on the underlying collateral provided by the borrower. These cash flows, however, may not be as expected and the value of collateral securing the loans may fluctuate. Most commercial loans are secured by the assets being financed or other business assets such as accounts receivable or inventory and may incorporate a personal guarantee. Commercial non-real estate municipal loans may be granted based on the unrestricted assets, tax base and overall borrowing capacity of local governments. Agricultural non-real estate loans are generally comprised of term loans to fund the purchase of equipment, livestock and seasonal operating lines. Operating lines are typically written for one year and secured by the crop and other farm assets as considered necessary. Agricultural loans carry significant credit risks as they may involve larger balances concentrated with single borrowers or groups of related borrowers. In addition, repayment of such loans depends on the successful operation or management of the farm property securing the loan or for which an operating loan is utilized. Farming operations may be affected by adverse weather conditions such as, but not limited to, drought, hail or floods that can severely limit crop yields.

Credit Quality/Risk Ratings:
Management utilizes a numeric risk rating system to identify and quantify the Bank’s risk of loss within its loan portfolio. Ratings are initially assigned prior to funding the loan, and may be changed at any time as circumstances warrant.
Ratings range from the highest to lowest quality based on factors that include measurements of ability to pay, collateral type and value, borrower stability and management experience. The Bank’s loan portfolio is presented below in accordance with the risk rating framework that has been commonly adopted by the federal banking agencies. The definitions of the various risk rating categories are as follows:
1 through 4 - Pass. A "Pass" loan means that the condition of the borrower and the performance of the loan is satisfactory or better.
5 - Watch. A "Watch" loan has clearly identifiable developing weaknesses that deserve additional attention from management. Weaknesses that are not corrected or mitigated, may jeopardize the ability of the borrower to repay the loan in the future.
6 - Special Mention. A "Special Mention" loan has one or more potential weakness that deserve management’s close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or in the institution’s credit position in the future.
7 - Substandard. A "Substandard" loan is inadequately protected by the current net worth and paying capacity of the obligor or the collateral pledged, if any. Assets classified as substandard must have a well-defined weakness, or weaknesses, that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the Bank will sustain some loss if the deficiencies are not corrected.
8 - Doubtful. A "Doubtful" loan has all the weaknesses inherent in a Substandard loan with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable and improbable.
9 - Loss. Loans classified as "Loss" are considered uncollectible, and their continuance as bankable assets is not warranted. This classification does not mean that the loan has absolutely no recovery or salvage value, and a partial recovery may occur in the future.

Below is a summary of originated and acquired loans by type and risk rating as of June 30, 2017:

	1 to 5	6	7	8	9	TOTAL
Originated Loans:						
Residential real estate:						
One to four family	$134,754	$—	$1,773	$—	$—	$136,527
Commercial/Agricultural real estate:						
Commercial real estate	79,332	50	68	—	—	79,450
Agricultural real estate	8,428	—	—	—	—	8,428
Multi-family real estate	23,206	—	148	—	—	23,354
Construction and land development	11,951	—	—	—	—	11,951
Consumer non-real estate:						
Originated indirect paper	93,649	8	230	—	—	93,887
Purchased indirect paper	33,660	—	—	—	—	33,660
Other Consumer	14,648	—	123	—	—	14,771
Commercial/Agricultural non-real estate:						
Commercial non-real estate	22,156	—	152	—	—	22,308
Agricultural non-real estate	11,706	416	91	—	—	12,213
Total originated loans	$433,490	$474	$2,585	$—	$—	$436,549
Acquired Loans:						
Residential real estate:						
One to four family	$19,550	$470	$188	$—	$—	$20,208
Commercial/Agricultural real estate:						
Commercial real estate	24,378	32	417	—	—	24,827
Agricultural real estate	16,882	278	4,100	—	—	21,260
Multi-family real estate	—	—	—	—	—	—
Construction and land development	1,920	—	116	—	—	2,036
Consumer non-real estate:						
Other Consumer	408	—	7	—	—	415
Commercial/Agricultural non-real estate:						
Commercial non-real estate	8,881	—	1,368	—	—	10,249
Agricultural non-real estate	4,067	28	98	—	—	4,193
Total acquired loans	$76,086	$808	$6,294	$—	$—	$83,188
Total Loans:						
Residential real estate:						
One to four family	$154,304	$470	$1,961	$—	$—	$156,735
Commercial/Agricultural real estate:						
Commercial real estate	103,710	82	485	—	—	104,277
Agricultural real estate	25,310	278	4,100	—	—	29,688
Multi-family real estate	23,206	—	148	—	—	23,354
Construction and land development	13,871	—	116	—	—	13,987
Consumer non-real estate:						
Originated indirect paper	93,649	8	230	—	—	93,887
Purchased indirect paper	33,660	—	—	—	—	33,660
Other Consumer	15,056	—	130	—	—	15,186
Commercial/Agricultural non-real estate:						
Commercial non-real estate	31,037	—	1,520	—	—	32,557
Agricultural non-real estate	15,773	444	189	—	—	16,406
Gross loans	$509,576	$1,282	$8,879	$—	$—	$519,737
Less:						

Net deferred loan costs (fees)	(334)
Allowance for loan losses	(5,756)
Loans receivable, net	$513,647

Below is a summary of originated loans by type and risk rating as of September 30, 2016:

	1 to 5	6	7	8	9	TOTAL
Originated Loans:						
Residential real estate:						
One to four family	$159,244	$—	$1,632	$—	$85	$160,961
Commercial/Agricultural real estate:						
Commercial real estate	58,768	—	—	—	—	58,768
Agricultural real estate	3,418	—	—	—	—	3,418
Multi-family real estate	18,935	—	—	—	—	18,935
Construction and land development	12,977	—	—	—	—	12,977
Consumer non-real estate:						
Originated indirect paper	118,809	10	254	—	—	119,073
Purchased indirect paper	49,221	—	—	—	—	49,221
Other Consumer	18,889	—	37	—	—	18,926
Commercial/Agricultural non-real estate:						
Commercial non-real estate	17,790	—	179	—	—	17,969
Agricultural non-real estate	9,994	—	—	—	—	9,994
Total originated loans	$468,045	$10	$2,102	$—	$85	$470,242
Acquired Loans:						
Residential real estate:						
One to four family	$25,613	$603	$561	$—	$—	$26,777
Commercial/Agricultural real estate:						
Commercial real estate	29,607	167	398	—	—	30,172
Agricultural real estate	21,922	11	2,847	—	—	24,780
Multi-family real estate	200	—	—	—	—	200
Construction and land development	3,487	—	116	—	—	3,603
Consumer non-real estate:						
Other Consumer	746	11	32	—	—	789
Commercial/Agricultural non-real estate:						
Commercial non-real estate	13,010	11	11	—	—	13,032
Agricultural non-real estate	4,546	7	100	—	—	4,653
Total acquired loans	$99,131	$810	$4,065	$—	$—	$104,006
Total Loans:						
Residential real estate:						
One to four family	$184,857					