

WILLIAM PENN BANCORP INC  
Form 10-Q  
November 15, 2010

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, DC 20549

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FORM 10-Q

(Mark One)

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

For the Quarterly Period Ended September 30, 2010

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 0-53172

WILLIAM PENN BANCORP, INC.  
(Exact name of registrant as specified in its charter)

United States  
(State or other jurisdiction of  
incorporation or organization)

37-1562563  
(I.R.S. Employer  
Identification No.)

8150 Route 13, Levittown, Pennsylvania  
(Address of principal executive offices)

19057  
(Zip Code)

(215) 945-1200  
(Registrant's telephone number, including area code)

Not applicable  
(Former name, former address and former fiscal year, if changed since last report)

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

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

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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 definition of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act:

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

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

As of November 15, 2010 there were 3,641,018 shares of the issuer’s common stock outstanding.

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WILLIAM PENN BANCORP, INC.  
QUARTERLY REPORT ON FORM 10-Q

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## PART I – FINANCIAL INFORMATION

## Item 1. Financial Statements

William Penn Bancorp, Inc.

Consolidated Balance Sheets

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

	September 30, 2010 (unaudited)		June 30, 2010
<b>ASSETS</b>			
Cash and due from banks	\$ 703	\$	725
Interest bearing deposits with other banks	16,853		18,903
Total cash and cash equivalents	17,556		19,628
Interest bearing time deposits	1,180		779
Securities available for sale	17,695		16,447
Securities held to maturity, fair value of \$33,703 and \$48,689	33,119		48,014
Loans receivable, net of allowance for loan losses of \$2,790 and \$2,645, respectively	238,965		230,367
Premises and equipment, net	2,468		2,208
Federal Home Loan Bank stock, at cost	4,974		4,974
Deferred income taxes	1,676		1,696
Real estate owned	1		233
Accrued interest receivable and other assets	2,338		2,023
<b>TOTAL ASSETS</b>	<b>\$ 319,972</b>	<b>\$</b>	<b>326,369</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>			
<b>LIABILITIES</b>			
Deposits:			
Non-interest bearing	\$ 1,920	\$	2,341
Interest bearing	176,524		178,940
Total deposits	178,444		181,281
Advances from Federal Home Loan Bank	85,500		89,000
Advances from borrowers for taxes and insurance	783		2,107
Accrued interest payable and other liabilities	2,962		2,774
<b>TOTAL LIABILITIES</b>	<b>267,689</b>		<b>275,162</b>
Commitments and contingencies	-		-

## STOCKHOLDERS' EQUITY

Preferred stock, no par value, 1,000,000 shares authorized;			
no shares issued	-		-
Common Stock, \$.10 par value, 49,000,000 shares authorized;			
3,641,018 shares issued and outstanding	364		364
Additional paid-in capital	9,819		9,811
Unallocated common stock held by the Employee Stock Ownership Plan ("ESOP")	(633)		(655)
Retained earnings	41,721		40,891
Accumulated other comprehensive income	1,012		796
TOTAL STOCKHOLDERS' EQUITY	52,283		51,207
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 319,972	\$	326,369

See accompanying notes to the unaudited consolidated financial statements

William Penn Bancorp, Inc.  
 Consolidated Statements of Income  
 (Dollars in thousands, except share and per share data)

	September 30, 2010	Three months ended (unaudited)	2009
<b>INTEREST INCOME</b>			
Loans receivable, including fees	\$ 3,446	\$	3,357
Taxable securities	409		646
Exempt from federal income tax	3		3
Other	13		21
Total Interest Income	3,871		4,027
<b>INTEREST EXPENSE</b>			
Deposits	672		846
Borrowings	810		975
Total Interest Expense	1,482		1,821
Net Interest Income	2,389		2,206
Provision For Loan Losses	145		94
<b>NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES</b>			
	2,244		2,112
<b>OTHER INCOME</b>			
Service fees	32		29
Realized gain on securities	-		70
Gain on sale of loans, net	27		6
Other	34		35
Total Other Income	93		140
<b>OTHER EXPENSES</b>			
Salaries and employee benefits	653		570
Occupancy and equipment	170		161
Professional fees	37		43
FDIC premium	53		57
Other	188		136
Total Other Expenses	1,101		967
Income Before Income Taxes	1,236		1,285
Income Tax Expenses	406		430
NET INCOME	\$ 830	\$	855
	\$ 0.23	\$	0.24

Basic and diluted earnings per share

(Note 5)

See accompanying notes to the unaudited consolidated financial statements

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William Penn Bancorp, Inc.		Three months ended September 30,	
Consolidated Statements of Cash Flows		2010	2009
(Dollars in thousands)		(unaudited)	
Cash Flows from Operating Activities			
Net income	\$	830	\$ 855
Adjustments to reconcile net income to net cash provided by operating activities:			
Provision for loan losses		145	94
Provision for depreciation		50	43
Net amortization of securities premiums and discounts		46	108
Compensation expense on ESOP		30	30
Deferred income taxes		20	(5)
Origination of loans for sale		(1,199)	(495)
Proceeds from sale of loans		1,226	501
Gain on sale of loans		(27)	(6)
Realized gain on securities		-	(70)
Increase in accrued interest receivable and other assets		(426)	(16)
(Decrease) increase in accrued interest payable and other liabilities		188	(55)
Net Cash Provided by Operating Activities		883	984
Cash Flows from Investing Activities			
Securities available for sale:			
Purchases		(2,017)	(3,991)
Maturities, calls and principal paydowns		1,089	1,563
Securities held to maturity:			
Purchases		(9,227)	(6,829)
Maturities, calls and principal paydowns		24,083	8,738
Net increase in loans receivable		(8,743)	(9,791)
Interest bearing time deposits:			
Purchases		(500)	-
Maturities & principal paydowns		99	610
Proceeds from sale of REO		232	-
Purchases of premises and equipment		(310)	(200)
Net Cash Provided by (Used for) Investing Activities		4,706	(9,900)
Cash Flows from Financing Activities			
Net (decrease) increase in deposits		(2,837)	297
Repayment of advances from Federal Home Loan Bank		(3,500)	(2,000)
Decrease in advances from borrowers for taxes and insurance		(1,324)	(1,311)
Net Cash Used for Financing Activities		(7,661)	(3,014)
Net Decrease in Cash and Cash Equivalents		(2,072)	(11,930)
Cash and Cash Equivalents-Beginning		19,628	15,855
Cash and Cash Equivalents-Ending	\$	17,556	\$ 3,925
Supplementary Cash Flows Information			
Interest paid	\$	1,556	\$ 1,865

Income taxes paid	\$	550	\$	325
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See accompanying notes to the unaudited consolidated financial statements.

WILLIAM PENN BANCORP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(UNAUDITED)

Note 1 - William Penn Bancorp, Inc.

The registrant, William Penn Bancorp, Inc. (the “Company”) is a federally chartered corporation formed for the purpose of becoming the mid-tier holding company for William Penn Bank, FSB (the “Bank”) in connection with its mutual holding company reorganization.

On April 15, 2008, the Bank completed the reorganization and became a wholly owned subsidiary of the Company. As part of the transaction, the Company sold 1,025,283 shares of its common stock, \$.10 par value, to the public at \$10.00 per share (including 87,384 shares purchased by the Bank’s Employee Stock Ownership Plan with funds borrowed from the Company) and issued 2,548,713 shares to William Penn, MHC. In addition, the Company contributed 67,022 shares to the William Penn Bank Community Foundation. Prior to consummation of the reorganization, the Company had no assets or liabilities.

Note 2 - Nature of Operations

The consolidated financial statements include the accounts of William Penn Bancorp, Inc. (the “Company”), and its wholly owned subsidiary, William Penn Bank, FSB (the “Bank”), and the Bank’s wholly owned subsidiary, WPSLA Investment Corporation (“WPSLA”). The primary purpose of the Company is to act as the holding company for the Bank. The Company is subject to regulation and supervision by the Office of Thrift Supervision (the “OTS”). William Penn Bank, FSB is a federally chartered savings bank. The Bank’s primary business consists of the taking of deposits and granting of mortgage loans to the customers generally in the Bucks County, Pennsylvania area. The Bank is supervised and regulated by the OTS. The investment in subsidiary on the parent company’s financial statements is carried at the parent company’s equity in the underlying net assets. WPSLA was incorporated under Delaware law to hold securities for the Bank. All intercompany transactions and balances have been eliminated in consolidation.

Note 3 – Basis of Consolidated Financial Statement Presentation

The accompanying unaudited consolidated financial statements were prepared in accordance with instructions for Form 10-Q and Regulation S-X and do not include information or footnotes necessary for a complete presentation of financial condition, results of operations and cash flows in conformity with generally accepted accounting principles (“GAAP”). However, in the opinion of management, all adjustments (consisting of normal recurring adjustments) necessary for a fair presentation of the consolidated financial statements have been included. The results of operations for the three months ended September 30, 2010, are not necessarily indicative of the results that may be expected for the entire fiscal year or any other period.

The data in the consolidated balance sheet for June 30, 2010 was derived from the Company’s audited consolidated financial statements. That data, along with the interim financial information presented in the consolidated balance sheets, statements of income and statements of cash flows should be read in conjunction with the 2010 consolidated financial statements of William Penn Bancorp, Inc. including the notes thereto included in the Annual Report on Form 10-K for the year ended June 30, 2010. William Penn Bancorp, Inc. is a “smaller reporting company” as defined by Item 10 of Regulation S-K and the financial statements were prepared in accordance with instructions applicable for such companies.



## Note 4 - Comprehensive Income

The components of comprehensive income include unrealized gains and losses on available for sale securities. Comprehensive income for the three months ended September 30, 2010 and 2009 was \$1,046,000 and \$1,080,000, respectively.

	Three months ended September 30,	
	2010	2009
	(in thousands)	
Unrealized holding gains on available for sale securities	\$ 327	\$ 411
Reclassification adjustment for gains included in net income	-	(70)
Net Unrealized Gains	327	341
Income tax effect	111	116
Net of Tax Amount	\$ 216	\$ 225

## Note 5 – Earnings Per Share

There are no convertible securities which would affect the numerator in calculating basic and diluted earnings per share; therefore, the net income for the three months ended September 30, 2010 and 2009, respectively as presented on the Consolidated Statements of Income (unaudited), is used as the numerator.

The following table sets forth the composition of the weighted-average common shares (denominator) used in the basic and diluted earnings per share computation.

	Three months ended September 30,	
	2010	2009
Weighted-average common shares outstanding	3,641,018	3,641,018
Average unearned ESOP shares	(64,114)	(72,852)
Weighted-average common shares and common stock equivalents used to calculate basic and diluted earnings per share	3,576,904	3,568,166
Net Income	\$ 830,000	\$ 855,000
Basic and diluted earnings per share	\$ 0.23	\$ 0.24



## Note 6 – Securities

The amortized cost and approximate fair value of securities are summarized as follows (in thousands):

	September 30, 2010			
	Amortized	Gross	Gross	Fair
	Cost	Unrealized	Unrealized	Value
		Gains	Losses	
<b>Available For Sale:</b>				
Mutual funds	\$ 14	\$ -	\$ -	\$ 14
Private label collateralized mortgage obligations	16,148	1,558	(25)	17,681
Total available for sale	\$ 16,162	\$ 1,558	(25)	\$ 17,695
<b>Held to Maturity:</b>				
U.S. Government corporations and agencies securities	\$ 24,170	\$ 314	(9)	\$ 24,475
Mortgage-backed securities	4,744	196	-	4,940
U.S. agency collateralized mortgage obligations	3,806	70	-	3,876
Municipal bonds	299	12	-	311
Corporate bonds	100	1	-	101
Total held to maturity	\$ 33,119	\$ 593	(9)	\$ 33,703
	June 30, 2010			
	Amortized	Gross	Gross	Fair
	Cost	Unrealized	Unrealized	Value
		Gains	Losses	
<b>Available For Sale:</b>				
Mutual funds	\$ 13	\$ -	\$ -	\$ 13
Private label collateralized mortgage obligations	15,228	1,263	(57)	16,434
Total available for sale	\$ 15,241	\$ 1,263	(57)	\$ 16,447
<b>Held to Maturity:</b>				
U.S. Government corporations and agencies securities	\$ 37,971	\$ 387	(3)	\$ 38,355
Mortgage-backed securities	4,977	210	-	5,187
U.S. agency collateralized mortgage obligations	4,767	75	-	4,842
Municipal bonds	299	6	-	305
Total held to maturity	\$ 48,014	\$ 678	(3)	\$ 48,689

At three months ended September 30, 2009, the Company recognized proceeds from sale of investment securities classified as available for sale and related gross gains of \$638,000 and \$70,000, respectively. The Company did not have any sale of available-for-sale securities for the same period in 2010.



## Note 6 – Securities (Continued)

The following table shows the Company's investments' gross unrealized losses and fair value, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position (in thousands):

		September 30, 2010					
		Less than 12 Months		12 Months or More		Total	Total
		Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Available For Sale:							
Private labeled collateralized mortgage obligations							
\$	2,982	\$ (25)	\$ -	\$ -	\$ 2,982	\$ (25)	
	2,982	(25)	-	-	2,982	(25)	
Held to Maturity:							
U.S. Government corporations and agencies securities							
	3,753	(9)	-	-	3,753	(9)	
	3,753	(9)	-	-	3,753	(9)	
Total Temporarily Impaired securities	\$ 6,735	\$ (34)	\$ -	\$ -	\$ 6,735	\$ (34)	
		June 30, 2010					
		Less than 12 Months		12 Months or More		Total	Total
		Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Available For Sale:							
Private labeled collateralized mortgage obligations							
\$	1,517	\$ (37)	\$ 552	(20)	\$ 2,069	\$ (57)	
	1,517	(37)	552	(20)	2,069	(57)	
Held to Maturity:							
U.S. Government corporations and agencies securities							
	3,997	(3)	-	-	3,997	(3)	
	3,997	(3)	-	-	3,997	(3)	
Total Temporarily Impaired securities	\$ 5,514	\$ (40)	\$ 552	(20)	\$ 6,066	\$ (60)	

The Company evaluates its investment securities holdings for other-than-temporary impairment (“OTTI”) on at least a quarterly basis. As part of this process, management considers its intent to sell each debt security and whether it is

more likely than not the Company will be required to sell the security before its anticipated recovery. If either of these conditions is met, OTTI is recognized in earnings equal to the entire difference between the security's amortized cost basis and its fair value at the balance sheet date. For securities that meet neither of these conditions, management performs analysis to determine whether any of these securities are at risk for OTTI. To determine which individual securities are at risk for OTTI and should be quantitatively evaluated utilizing a detailed analysis, management uses indicators which consider various characteristics of each security including, but not limited to, the following: the credit rating; the duration and level of the unrealized loss; prepayment assumptions; and certain other collateral-related characteristics such as delinquency rates, the security's performance, and the severity of expected collateral losses.

There are 11 securities that are impaired at September 30, 2010, including 6 positions in private-label collateralized mortgage obligations. Based on its analysis, management has concluded that the securities portfolio has experienced unrealized losses and a decrease in fair value due to interest rate volatility, illiquidity in the marketplace, and credit deterioration in the U.S. mortgage markets. At this time,

management believes that the Company will fully recover the cost of these securities, and the Company does not intend to sell these securities nor would the Company be required to sell the security before its anticipated recovery. Therefore, the decline is considered temporary.

#### Note 7 – Loans Receivable

The composition of net loans receivable is as follows (dollars in thousands):

	September 30, 2010		June 30, 2010	
	Amount	Percent	Amount	Percent
Mortgage loans on real estate:				
Residential 1-4 family	\$ 147,080	59.98 %	\$ 145,231	61.25%
Residential multi-family (five or more)	11,111	4.53	10,068	4.25
Commercial-non-residential	44,071	17.97	44,209	18.65
Construction	5,797	2.36	5,580	2.35
Land	4,483	1.83	4,600	1.94
Home equity and second mortgages	6,574	2.68	5,835	2.46
Equity lines of credit	23,428	9.55	18,676	7.88
Total Mortgage Loans on Real Estate	242,544		234,199	
Consumer Loans	2,125	0.87	2,352	0.99
Loans on savings accounts	544	0.22	549	0.23
Total Loans	245,213	100.00%	237,100	100.00%
Loans in process	(2,667)		(3,357)	
Unearned loan origination fees	(791)		(731)	
Allowance for loan losses	(2,790)		(2,645)	
Net Loans	\$ 238,965		\$ 230,367	

At September 30, 2010 and June 30, 2010, we had approximately \$69.9 million and \$69.4 million of loans on non-owner-occupied, one-to-four-family residences (“investor loans”), representing approximately 28.5% and 29.3% of total loans. This \$69.9 million of one- to four-family investor loans includes \$66.0 million of first mortgages; \$794,000 of second mortgages; and \$3.1 million of construction loans. At June 30, 2010, this \$69.4 million of one- to four-family investor loans includes, \$65.4 million of first mortgages; \$725,000 of second mortgages; and \$3.3 million of construction loans.

#### Note 8 – Recent Accounting Pronouncements

In January 2010, the FASB issued ASU No. 2010-06, Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements. ASU 2010-06 amends Subtopic 820-10 to clarify existing disclosures, require new disclosures, and includes conforming amendments to guidance on employers' disclosures about postretirement benefit plan assets. ASU 2010-06 is effective for interim and annual periods beginning after December 15, 2009, except for disclosures about purchases, sales, issuances, and settlements in the roll forward of activity in Level 3 fair value measurements. Those disclosures are effective for fiscal years beginning after December 15, 2010 and for interim periods within those fiscal years. The adoption of this guidance is not expected to have a significant impact on the Company's financial statements.

In April 2010, the FASB issued ASU 2010-18, Receivables (Topic 310): Effect of a Loan Modification When the Loan is a Part of a Pool That is Accounted for as a Single Asset – a consensus of the FASB Emerging Issues Task Force. ASU 2010-18 clarifies the treatment for a modified loan that was acquired as part of a pool of assets. Refinancing or restructuring the loan does not make it eligible for

Note 8 – Recent Accounting Pronouncements (Continued)

removal from the pool, the FASB said. The amendment will be effective for loans that are part of an asset pool and are modified during financial reporting periods that end July 15, 2010 or later and is not expected to have a significant impact on the Company's financial statements or the Company is currently evaluating the impact the adoption of the standard will have on the Company's financial position or results of operations.

In July 2010, FASB issued ASU No. 2010-20, Receivables (Topic 310): Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses. ASU 2010-20 is intended to provide additional information to assist financial statement users in assessing an entity's credit risk exposures and evaluating the adequacy of its allowance for credit losses. The disclosures as of the end of a reporting period are effective for interim and annual reporting periods ending on or after December 15, 2010. The disclosures about activity that occurs during a reporting period are effective for interim and annual reporting periods beginning on or after December 15, 2010. The amendments in ASU 2010-20 encourage, but do not require, comparative disclosures for earlier reporting periods that ended before initial adoption. However, an entity should provide comparative disclosures for those reporting periods ending after initial adoption. The Company is currently evaluating the impact the adoption of this guidance will have on the Company's financial position or results of operations.

Note 9: Fair Value Measurements

The Company presents enhanced disclosures about assets and liabilities carried at fair value. U. S. generally accepted accounting standards establishes a hierarchal disclosure framework associated with the level of pricing observability utilized in measuring assets and liabilities at fair value. The three broad levels of hierarchy are as follows:

- Level I: Quoted prices are available in active markets for identical assets or liabilities as of the reported date.
- Level II: Pricing inputs are other than quoted prices in active markets, which are either directly or indirectly observable as of the reported date. The nature of these assets and liabilities include items for which quoted prices are available but traded less frequently, and items that are fair valued using other financial instruments, the parameters of which can be directly observed.
- Level III: Assets and liabilities that have little to no pricing observability as of the reported date. These items do not have two-way markets and are measured using management's best estimate of fair value, where the inputs into the determination of fair value require significant management judgment or estimation.

## Note 9: Fair Value Measurements (Continued)

The following table presents the assets reported on the consolidated balance sheets at their fair value, by level within the fair value hierarchy. No liabilities are carried at fair value. Financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement.

	September 30, 2010			Total
	Level I	Level II	Level III	
Assets:				
Investments				
available-for-sale				
Mutual funds	\$ 14	\$ -	\$ -	\$ 14
Private labeled collateralized mortgage obligations	-	17,681	-	17,681
	\$ 14	\$ 17,681	\$ -	\$ 17,695
	June 30, 2010			Total
	Level I	Level II	Level III	
Assets:				
Investments				
available-for-sale				
Mutual funds	\$ 13	\$ -	\$ -	\$ 13
Private labeled collateralized mortgage obligations	-	16,434	-	16,434
	\$ 13	\$ 16,434	\$ -	\$ 16,447

## Assets and Liabilities Measured on a Non-Recurring Basis

Certain assets and liabilities may be required to be measured at fair value on a nonrecurring basis in periods subsequent to their initial recognition. Generally, nonrecurring valuation is the result of the application of other accounting pronouncements which require assets and liabilities to be assessed for impairment or recorded at the lower of cost or fair value.

Impaired loans are generally measured for impairment using the fair value of the collateral supporting the loan. Evaluating impaired loan collateral is based on level 2 inputs utilizing outside appraisals adjusted by management for sales costs and other assumptions regarding market conditions to arrive at fair value. At September 30, 2010, impaired loans with a carrying value of \$7,800,000 were reduced by specific valuation allowance totaling \$949,000 resulting in a net fair value of \$6,851,000. At June 30, 2010, impaired loans with a carrying value of \$7,801,000 were reduced by specific valuation allowance totaling \$983,000 resulting in a net fair value of \$6,818,000, based on Level 2 inputs.

Other real estate owned (OREO) is measured at fair value, based on appraisals less cost to sell at the date of foreclosure. Valuations are periodically performed by management and the assets are carried at the lower of carrying amount or fair value, less cost to sell. Income and expenses from operations and changes in valuation allowance are included in the net expenses from OREO.



Assets measured at fair value on a non-recurring basis are summarized (in thousands):

	September 30, 2010			
	Level I	Level II	Level III	Total
Assets:				
Impaired loans	\$ -	\$ 6,851	\$ -	\$ 6,851
Other real estate owned	-	1	-	1
	\$ -	\$ 6,852	\$ -	\$ 6,852
	June 30, 2010			
	Level I	Level II	Level III	Total
Assets:				
Impaired loans	\$ -	\$ 6,818	\$ -	\$ 6,818
Other real estate owned	-	233	-	233
	\$ -	\$ 7,051	\$ -	\$ 7,051

Management uses its best judgment in estimating the fair value of the Company's financial instruments; however, there are inherent weaknesses in any estimation technique. Therefore, for substantially all financial instruments, the fair value estimates herein are not necessarily indicative of the amounts the Company could have realized in sales transaction on the dates indicated. The estimated fair value amounts have been measured as of their respective year-ends and have not been reevaluated or updated for purposes of these financial statements subsequent to those respective dates. As such, the estimated fair values of these financial instruments subsequent to the respective reporting dates may be different than the amounts reported at each year-end.

The following information should not be interpreted as an estimate of the fair value of the entire Company, since a fair value calculation is only provided for a limited portion of the Company's assets and liabilities. Due to a wide range of valuation techniques and the degree of subjectivity used in making the estimates, comparisons between the Company's disclosures and those of other companies may not be meaningful. The following methods and assumptions were used to estimate the fair values of the Company's financial instruments.

#### Cash and Due from Banks and Interest Bearing Time Deposits

The carrying amounts of cash and due from banks and interest bearing time deposits approximate their fair value.

#### Securities Available for Sale and Held to Maturity

The fair value of investment and mortgage-backed securities is equal to the available quoted market price. If no quoted market price is available, fair value is estimated using the quoted market price for similar securities.

#### Loans Receivable, net

For variable-rate loans that reprice frequently and which entail no significant changes in credit risk, fair values are based on carrying values. The fair values of fixed rate loans are estimated using discounted cash flow analyses at market interest rates currently offered for loans with similar terms to borrowers of similar credit quality.

#### Federal Home Loan Bank Stock

The carrying amount of Federal Home Loan Bank stock approximates fair value.





## Accrued Interest Receivable and Payable

The carrying amount of accrued interest receivable and payable approximates fair value.

## Deposits

Fair values for demand deposits, savings accounts, and certain money market deposits are, by definition, equal to the amount payable on demand at the reporting date. Fair values of fixed-maturity certificates of deposit are estimated using a discounted cash flow calculation that applies market interest rates currently being offered on similar instruments with similar maturities.

## Advances from Federal Home Loan Bank

Fair value of advances from Federal Home Loan Bank is estimated using discounted cash flow analyses, based on rates currently available to the Company for advances from Federal Home Loan Bank with similar terms and remaining maturities.

The estimated fair values of the Company's financial instruments were as follows (in thousands):

	September 30, 2010		June 30, 2010	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Financial assets:				
Cash and amounts due from banks	\$ 17,556	\$ 17,556	\$ 19,628	\$ 19,628
Interest-bearing time deposits	1,180	1,180	779	779
Securities available for sale	17,695	17,695	16,447	16,447
Securities held to maturity	33,119	33,703	48,014	48,689
Loans receivable, net	238,965	253,945	230,367	244,808
Federal Home Loan Bank stock	4,974	4,974	4,974	4,974
Accrued Interest receivable:				
Loans receivable	1,146	1,146	1,075	1,075
Investment securities	191	191	184	184
Mortgage-backed securities	80	80	82	82
Financial liabilities:				
Non-interest bearing demand deposits				
	1,920	1,920	2,341	2,341
NOW accounts	15,604	15,604	15,584	15,584
Money market accounts	42,059	42,059	43,896	43,896
Savings and club accounts	14,550	14,550	14,437	14,437
Certificates of deposit	104,311	107,349	105,023	108,082
Advances from Federal Home Loan Bank				
	85,500	92,610	89,000	96,401
Accrued interest payable	248	248	321	321

Off-balance sheet financial  
instruments

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

Throughout this Form 10-Q, the terms “we”, “us” or “our” refer to William Penn Bancorp, Inc. or William Penn Bank, FSB, or both, as the context indicates. We also refer to William Penn Bank, FSB as “the Bank” and to William Penn Bancorp, Inc. as “the Registrant” or “the Company.”

### Forward-Looking Statements

This Form 10-Q contains forward-looking statements, which can be identified by the use of words such as “believes,” “expects,” “anticipates,” “estimates” or similar expressions. Forward-looking statements include:

- statements of our goals, intentions and expectations;
- statements regarding our business plans, prospects, growth and operating strategies;
- statements regarding the quality of our loan and investment portfolios; and
- estimates of our risks and future costs and benefits.

These forward-looking statements are subject to significant risks and uncertainties. Actual results may differ materially from those contemplated by the forward-looking statements due to, among others, the following factors:

- general economic conditions, either nationally or in our market area, that are worse than expected;
- changes in the interest rate environment that reduce our interest margins or reduce the fair value of financial instruments;
- our ability to enter into new markets and/or expand product offerings successfully and take advantage of growth opportunities;
- increased competitive pressures among financial services companies;
- changes in consumer spending, borrowing and savings habits;
- legislative or regulatory changes that adversely affect our business;
- adverse changes in the securities markets;
- our ability to successfully manage our growth; and
- changes in accounting policies and practices, as may be adopted by the bank regulatory agencies, the Financial Accounting Standards Board or the Public Company Accounting Oversight Board.

Any of the forward-looking statements that we make in this Form 10-Q and in other public statements we make may turn out to be wrong because of inaccurate assumptions we might make, because of the factors illustrated above or because of other factors that we cannot foresee. Consequently, no forward-looking statement can be guaranteed.



## Overview

This discussion and analysis reflects the Company's consolidated financial statements and other relevant statistical data and is intended to enhance your understanding of our financial condition and results of operations. You should read the information in this section in conjunction with the Company's unaudited consolidated financial statements and accompanying notes thereto included in this Form 10-Q.

Our primary business is attracting retail deposits from the general public and using those deposits, together with funds generated from operations, principal repayments on securities and loans, and borrowed funds, for our lending and investing activities. Our results of operations depend mainly on our net interest income, which is the difference between the interest income earned on our loan and investment portfolios and interest expense paid on our deposits and borrowed funds. Net interest income is a function of the average balances of loans and investments versus deposits and borrowed funds outstanding in any one period and the yields earned on those loans and investments and the cost of those deposits and borrowed funds.

## Anticipated Increase in Operating Expenses

Noninterest expense in the future will be impacted by our plan to expand our branch network. Construction has begun on a new branch in Levittown which will be completed in the Spring of 2011. We also anticipate additional branch expansion over the next five years. This will lead to higher compensation and benefits expenses going forward as the result of our plans to hire additional personnel and expand the size of our lending department.

The Bank's deposits are insured to applicable limits by the FDIC. The maximum deposit insurance amount has been permanently increased from \$100,000 to \$250,000 by the Dodd-Frank Act. On October 13, 2008, the FDIC established a Temporary Liquidity Guarantee Program under which the FDIC fully guarantees all non-interest-bearing transaction accounts until December 31, 2009 (the "Transaction Account Guarantee Program") and all senior unsecured debt of insured depository institutions or their qualified holding companies issued between October 14, 2008 and June 30, 2009, with the FDIC's guarantee expiring by June 30, 2012 (the "Debt Guarantee Program"). Senior unsecured debt would include federal funds purchased and certificates of deposit standing to the credit of the bank. After November 12, 2008, institutions that did not opt out of the Programs by December 5, 2008 were assessed at the rate of ten basis points for transaction account balances in excess of \$250,000 and at a rate between 50 and 100 basis points of the amount of debt issued. In May, 2009, the Debt Guarantee Program issue end date and the guarantee expiration date were both extended, to October 31, 2009 and December 31, 2012, respectively. Participating holding companies that have not issued FDIC-guaranteed debt prior to April 1, 2009 must apply to remain in the Debt Guarantee Program. Participating institutions will be subject to surcharges for debt issued after that date. Effective October 1, 2009, the Transaction Account Guarantee Program was extended until December 31, 2010, with an assessment of between 15 and 25 basis points after January 1, 2010. The Company and the Bank did not opt out of the Debt Guarantee Program. The Bank did not opt out of the original Transaction Account Guarantee Program or its extension. The Dodd-Frank Act has extended unlimited deposit insurance to non-interest-bearing transaction accounts until December 31, 2013.

The FDIC has adopted a risk-based premium system that provides for quarterly assessments based on an insured institution's ranking in one of four risk categories based on their examination ratings and capital ratios. Well-capitalized institutions with the CAMELS ratings of 1 or 2 are grouped in Risk Category I and, until 2009, were assessed for deposit insurance at an annual rate of between five and seven basis points with the assessment rate for an individual institution determined according to a formula based on a weighted average of the institution's individual CAMELS component ratings plus either five



financial ratios or the average ratings of its long-term debt. Institutions in Risk Categories II, III and IV were assessed at annual rates of 10, 28 and 43 basis points, respectively.

Pursuant to the Federal Deposit Insurance Reform Act of 2005 (the "Reform Act"), the FDIC is authorized to set the reserve ratio for the Deposit Insurance Fund annually at between 1.15% and 1.5% of estimated insured deposits. Due to recent bank failures, the FDIC determined that the reserve ratio was 1.01% as of June 30, 2008. In accordance with the Reform Act, as amended by the Helping Families Save Their Home Act of 2009, the FDIC has established and implemented a plan to restore the reserve ratio to 1.15% within eight years. For the quarter beginning January 1, 2009, the FDIC raised the base annual assessment rate for institutions in Risk Category I to between 12 and 14 basis points while the base annual assessment rates for institutions in Risk Categories II, III and IV were increased to 17, 35 and 50 basis points, respectively. For the quarter beginning April 1, 2009 the FDIC set the base annual assessment rate for institutions in Risk Category I to between 12 and 16 basis points and the base annual assessment rates for institutions in Risk Categories II, III and IV at 22, 32 and 45 basis points, respectively. An institution's assessment rate could be lowered by as much as five basis points based on the ratio of its long-term unsecured debt to deposits or, for smaller institutions based on the ratio of certain amounts of Tier 1 capital to adjusted assets. The assessment rate may be adjusted for Risk Category I institutions that have a high level of brokered deposits and have experienced higher levels of asset growth (other than through acquisitions) and could be increased by as much as ten basis points for institutions in Risk Categories II, III and IV whose ratio of brokered deposits to deposits exceeds 10%. Reciprocal deposit arrangements like CDARS® were treated as brokered deposits for Risk Category II, III and IV institutions but not for institutions in Risk Category I. An institution's base assessment rate would also be increased if an institution's ratio of secured liabilities (including FHLB advances and repurchase agreements) to deposits exceeds 25%. The maximum adjustment for secured liabilities for institutions in Risk Categories I, II, III and IV would be 8, 11, 16 and 22.5 basis points, respectively, provided that the adjustment may not increase an institution's base assessment rate by more than 50%.

The FDIC imposed a special assessment equal to five basis points of assets less Tier 1 capital as of June 30, 2009, payable on September 30, 2009, and reserved the right to impose additional special assessments. In November, 2009, instead of imposing additional special assessments, the FDIC amended the assessment regulations to require all insured depository institutions to prepay their estimated risk-based assessments for the fourth quarter of 2009, and for all of 2010, 2011 and 2012 on December 30, 2009. For purposes of estimating the future assessments, each institution's base assessment rate in effect on September 30, 2009 was used, assuming a 5% annual growth rate in the assessment base and a 3 basis point increase in the assessment rate in 2011 and 2012. The prepaid assessment will be applied against actual quarterly assessments until exhausted. Any funds remaining after June 30, 2013 will be returned to the institution. If the prepayment would impair an institution's liquidity or otherwise create significant hardship, it may apply for an exemption. Requiring this prepaid assessment does not preclude the FDIC from changing assessment rates or from further revising the risk-based assessment system.

The Dodd-Frank Act requires the FDIC to increase the reserve ratio of the Deposit Insurance Fund from 1.15% to 1.35% of insured deposits by September 30, 2020 and eliminates the requirement that the FDIC pay dividends to insured depository institutions when the reserve ratio exceeds certain thresholds. The Dodd-Frank Act also broadens the base for FDIC insurance assessments. Assessments will now be based on the average consolidated total assets less tangible equity capital of a financial institution. In setting the assessments necessary to meet the minimum reserve ratio, the FDIC must offset the effect on depository institutions with total consolidated assets of less than \$10.0 billion. The FDIC has adopted a new restoration plan reflecting the new statutory requirements. Under the revised restoration plan, the DIF reserve ratio will reach 1.35% by September 30, 2020. Because of lower projected losses, the FDIC has determined that the reserve ratio will reach 1.15% by the fourth quarter of 2018 without a 3 basis point increase in assessment rates and the FDIC has determined to forgo such





increase. The FDIC has indicated that it will pursue further rulemaking in 2011 regarding the method that will be used to reach 1.35% by September 30, 2020 and offset the effect on insured depository institutions with total consolidated assets of less than \$10.0 billion as required by the Dodd-Frank Act.

In addition, all FDIC-insured institutions are required to pay assessments to the FDIC to fund interest payments on bonds issued by the Financing Corporation ("FICO"), an agency of the Federal government established to recapitalize the Federal Savings and Loan Insurance Corporation. The FICO assessment rates, which are determined quarterly, averaged .01% of insured deposits on an annualized basis in fiscal year 2009. These assessments will continue until the FICO bonds mature in 2017.

#### Critical Accounting Policies

Our accounting policies are integral to understanding the results reported and our significant policies are described in Note 2 to our consolidated financial statements included in the William Penn Bancorp, Inc. 2010 Annual Report on Form 10-K. In preparing the consolidated financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the dates of the consolidated balance sheets and statements of income for the periods then ended. Actual results could differ significantly from those estimates. Material estimates that are particularly susceptible to significant change relate to the determination of the allowance for loan losses, the valuation allowance for deferred tax assets and other-than-temporary impairment of securities.

**Allowance for Loan Losses.** The allowance for loan losses is maintained by management at a level which represents their evaluation of known and inherent losses in the loan portfolio at the consolidated balance sheet date that are both probable and reasonable to estimate. Management's periodic evaluation of the adequacy of the allowance is based on the Bank's past loan loss experience, known and inherent losses in the portfolio, adverse situations that may affect the borrower's ability to repay, the estimated value of any underlying collateral, composition of the loan portfolio, current economic conditions, and other relevant factors. This evaluation is inherently subjective as it requires material estimates that may be susceptible to significant change, including the amounts and timing of future cash flows expected to be received on impaired loans.

The allowance consists of specific and general components. The specific component relates to loans that are classified as doubtful, substandard, or special mention. For such loans that are also classified as impaired, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan. The general component covers nonclassified loans and is based on historical loss experience adjusted for qualitative factors.

Although specific and general loan loss allowances are established in accordance with management's best estimate, actual losses are dependent upon future events and, as such, further provisions for loan losses may be necessary. For example, our evaluation of the allowance includes consideration of current economic conditions, and a change in economic conditions could reduce the ability of our borrowers to make timely repayments of their loans. This could result in increased delinquencies and increased non-performing loans, and thus a need to make increased provisions to the allowance for loan losses, which would require us to record a charge against income during the period the provision is made, resulting in a reduction of our earnings. A change in economic conditions could also adversely affect the value of the properties collateralizing our real estate loans, resulting in increased charge-offs against the allowance and reduced recoveries of loans previously charged-off, and thus a need to make increased provisions to the allowance for loan losses. Furthermore, a change in the composition of our loan portfolio or growth of our loan portfolio could result in the need for additional provisions.



**Deferred Income Taxes.** We use the asset and liability method of accounting for income taxes. Under this method, deferred tax assets and liabilities 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 expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. If current available information raises doubt as to the realization of the deferred tax assets, a valuation allowance is established. We consider the determination of this valuation allowance to be a critical accounting policy because of the need to exercise significant judgment in evaluating the amount and timing of recognition of deferred tax liabilities and assets, including projections of future taxable income. These judgments and estimates are reviewed on a continual basis as regulatory and business factors change. A valuation allowance for deferred tax assets may be required if the amount of taxes recoverable through loss carryback declines, or if we project lower levels of future taxable income. Such a valuation allowance would be established through a charge to income tax expense which would adversely affect our operating results.

**Other-than-Temporary Investment Security Impairment.** Securities are evaluated periodically to determine whether a decline in their value is other-than-temporary. Management utilizes criteria such as the magnitude and duration of the decline, in addition to the reasons underlying the decline, to determine whether the loss in value is other-than-temporary. The term “other-than-temporary” is not intended to indicate that the decline is permanent, but indicates that the prospect for a near-term recovery of value is not necessarily favorable, or that there is a lack of evidence to support a realizable value equal to or greater than the carrying value of the investment. Once a decline in value is determined to be other-than-temporary, the value of the security is reduced and a corresponding charge to earnings is recognized.

#### Comparison of Financial Condition at September 30, 2010 and June 30, 2010

Our total assets decreased by \$6.4 million to \$320.0 million at September 30, 2010 from \$326.4 million at June 30, 2010, primarily due to a \$14.9 million decrease in securities held-to-maturity. This decrease was partially offset by an \$8.6 million increase in loans receivable to \$239.0 million at September 30, 2010 from \$230.4 million at June 30, 2010. The growth in the loan portfolio was mainly due to an increase in home equity lines of credit by \$4.8 million to \$23.4 million at September 30, 2010 as compared to \$18.7 million at June 30, 2010. There was also an increase of \$1.8 million in one-to-four family residential loans. Multi-family residential loans also grew by \$1.0 million to \$11.1 million at September 30, 2010 from \$10.1 million at June 30, 2010. Available for sale securities at September 30, 2010 increased to \$17.7 million compared to \$16.4 million at June 30, 2010, interest-bearing time deposits increased nominally to \$1.2 million at September 30, 2010 from \$800,000 at June 30, 2010. These increases were offset by the decrease in cash and cash equivalents by \$2.1 million to \$17.6 million at September 30, 2010 from \$19.6 million at June 30, 2010.

Deposits decreased by \$2.9 million to \$178.4 million at September 30, 2010 from \$181.3 million at June 30, 2010. Advances from the FHLB decreased by \$3.5 million to \$85.5 million at September 30, 2010, from \$89.0 million at June 30, 2010. One borrowing with a high interest rate of 6.54% matured, which resulted in a decrease in the interest expense. Also advances from borrowers for taxes and insurance decreased \$1.3 million to \$783,000 at September 30, 2010 from \$2.1 million at June 30, 2010. This was attributable to the real estate taxes paid on behalf of our borrowers.

Stockholders' equity grew by \$1.1 million to \$52.3 million at September 30, 2010, from \$51.2 million at June 30, 2010. The increase was primarily the result of the Company's net income of \$830,000 for the three months ended September 30, 2010 and a \$216,000 increase in accumulated other comprehensive income relating to unrealized gains on the available-for-sale securities portfolio.



Comparison of Operating Results for the Three Months Ended September 30, 2010 and 2009

General. Net income for the three months ended September 30, 2010 was \$830,000 (\$0.23 per share) compared to a net income of \$855,000 (\$0.24 per share) for the same period ending September 30, 2009.

Interest Income. Total interest income declined \$156,000 to \$3.9 million for the three months ended September 30, 2010 as compared to \$4.0 million for the same period ending September 30, 2009. The decrease was primarily due to a decrease in interest income from securities. Interest income from securities declined by \$237,000 from \$646,000 for the three months ended September 30, 2009 to \$409,000 for the three month period ended September 30, 2010. The average balance of securities went up by \$2.3 million, to \$61.9 million for the three months ended September 30, 2010 from \$59.6 million for the three months ended September 30, 2009. The average yield declined 167 basis points, decreasing the interest income on securities. Interest income from loans receivable for the three months September 30, 2010 and 2009 were \$3.4 million and \$3.3 million respectively, a very nominal increase of \$89,000. Average loan balances increased from \$221.4 million for the three months ended September 30, 2009 to \$235.5 million for the three months ended September 30, 2010. Even though the average balance of loans receivable increased by \$14.1 million, the average yield declined by 22 basis points, resulting in the interest income on loans receivable to be approximately the same for the two periods. The average balance of other interest earning assets decreased to \$20.8 million at September 30, 2010 compared to \$21.5 million at September 30, 2009. The average yield on interest earning assets also declined 20 basis points resulting in a decrease in interest income from other interest earning assets.

Interest Expense. Total interest expense decreased \$339,000 to \$1.5 million for the three months ended September 30, 2010 as compared to \$1.8 million for the same period in 2009. The decrease resulted from a decrease in interest expense on deposits to \$672,000 for the three months ended September 30, 2010 from \$846,000 for the same period in 2009. The average balance of interest bearing deposits went up to \$178.1 million at September 30, 2010 as compared to \$165.0 million at September 30, 2009, however due to the low interest rate environment, there was a 54 basis point decrease in the average cost of the deposits resulting in a decline in interest expense. Interest expense on borrowings decreased by \$165,000 to \$810,000 for the three months ended September 30, 2010 from \$975,000 for the same period ending September 30, 2009 due to a 68 basis point decrease in the average cost and also a decrease in the average balance of Federal Home Loan Bank advances ("FHLB") to \$86.7 million at September 30, 2010 from \$88.2 million at September 30, 2009. One borrowing with a high interest rate of 6.54% matured, which also resulted in a decrease in the interest expense.

Net Interest Income. Our interest rate spread and net interest margin for the three months ended September 30, 2010, were 2.63% and 3.00%, respectively, compared to 2.45% and 2.92%, respectively, for the three months ended September 30, 2009. Though the average balance of the interest earning assets increased to \$318.2 million at September 30, 2010 from \$302.4 million at September 30, 2009 the average yield declined 46 basis points. Average interest-bearing liabilities were \$264.7 million and \$253.2 million for the three months ended September 30, 2010 and 2009, respectively. Average cost of interest bearing liabilities also declined 64 basis points, resulting in a small increase in our interest rate spread. There was an 8 basis points increase in our net interest margin for the three months ended September 30, 2010, resulting from an increase in net interest income of \$183,000 for the three months ended September 30, 2010.

Provision for Loan Losses. We charge to operations provisions for loan losses at a level required to reflect credit losses in the loan portfolio that are both probable and reasonable to estimate. Management, in determining the allowance for loan losses, considers the losses inherent in the loan portfolio and changes in the nature and volume of our loan activities, along with general economic and

real estate market conditions. We utilize a two-tier approach: (1) identification of impaired loans and establishment of specific loss allowances on such loans; and (2) establishment of general valuation allowances on the remainder of our loan portfolio. We establish a specific loan loss allowance for an impaired loan based on delinquency status, size of loan, type of collateral and/or appraisal of the underlying collateral and financial condition of the borrower. We base general loan loss allowances upon a combination of factors including, but not limited to, actual loan loss experience, composition of the loan portfolio, current economic conditions, industry trends and management's judgment.

There was a provision for loan losses of \$145,000 and \$94,000 made during the three months ended September 30, 2010 and 2009, respectively. The allowance as a percentage of total loans was 1.15% at September 30, 2010 as compared to 1.14% at June 30, 2010. Management believes that the allowance for loan and lease losses is sufficient given the status of the loan portfolio at this time.

Other Income. Other income decreased by \$47,000 to \$93,000 for the three months ended September 30, 2010 compared to \$140,000 for the same period in 2009. This was primarily due to a \$70,000 profit on the sale of a private label CMO investment for the three months ended September 30, 2009, which was partially offset by a nominal increase of \$20,000 in other miscellaneous income. Traditionally, other income has not been a significant part of our operations as we have not in the past focused on fee generation. We hold the bulk of our securities portfolio as held to maturity so gains or losses on the sales of securities are not expected to be a large item in non interest income. We have no current plans to seek additional fee income generation through the offering of complementary services or acquisition of fee-producing subsidiaries such as title insurance or third-party securities sales.

Other Expenses. There was an increase of \$134,000 in other expenses for the three months ended September 30, 2010 as compared to the same period ending September 30, 2009. There was an \$83,000 increase in Salaries and employee benefits as a result of normal salary increases, combined with the increased cost of maintaining benefits. Other expenses increased by \$52,000 which was mainly attributable to increase in advertising costs to create market awareness. FDIC deposit insurance premium, professional fees and occupancy and equipment expenses remained virtually the same for both periods ending September 30, 2010 and 2009.

Average Balance Sheets. The following table sets forth certain information for the three months ended September 30, 2010 and 2009. The average yields and costs are derived by dividing income or expense by the average balance of assets or liabilities, respectively, for the periods presented. Average balances are derived from daily average balances.

	Three months ended September 30,					
	2010			2009		
	Average Balance	Interest	Average Yield/Cost	Average Balance	Interest	Average Yield/Cost
<b>Interest -earning assets:</b>						
Net loans receivable (1) (2)	\$ 235,488	\$ 3,446	5.85%	\$ 221,360	\$ 3,357	6.07%
Securities	61,887	412	2.66%	59,614	646	4.33%
Other interest earning assets(3)	20,835	13	0.25%	21,461	24	0.45%
Total interest earning assets	318,210	3,871	4.87%	302,435	4,027	5.33%
Non-interest earning assets	4,687			4,199		
Total Assets	322,897			306,634		
<b>Interest -bearing liabilities:</b>						
NOW accounts	15,910	9	0.23%	14,027	13	0.37%
Money Market Accounts	43,101	83	0.77%	40,440	115	1.14%
Savings and Club accounts	14,500	16	0.44%	13,570	30	0.88%
Certificates of deposit	104,547	564	2.16%	96,984	688	2.84%
Total Deposits	178,058	672	1.51%	165,021	846	2.05%
Federal Home Loan Bank Advances	86,685	810	3.74%	88,177	975	4.42%
Total interest-bearing liabilities	264,743	1,482	2.24%	253,198	1,821	2.88%
Non interest bearing deposits	2,017			1,491		
Non interest bearing liabilities	4,573			4,554		
Total Liabilities	271,333			259,243		
Stockholders equity	51,564			47,391		
Total Liabilities and Stockholders Equity	\$ 322,897			\$ 306,634		
Net interest income		\$ 2,389			\$ 2,206	
Interest rate spread (4)			2.63%			2.45%
Net interest margin (5)			3.00%			2.92%
Ratio of average interest -earning assets to average interest-bearing liabilities	120.20%			119.45%		

(1) Non-accruing loans have been included in loans receivable and the effect of such inclusion was not material. Allowance for loan losses has been included in noninterest-earning assets. Interest income on loans includes net amortized revenues (costs) on loans.

(2) Includes both available for sale and held to maturity securities. For available for sale securities, fair value adjustments have been included in the average balance of noninterest-earning assets.

(3) Includes interest-bearing deposits at other banks, federal funds purchased and Federal Home Loan Bank of Pittsburgh capital stock.

(4) Interest rate spread represents the difference between the average yield on interest-earning assets and the average cost of interest-bearing liabilities.



- (5) Net interest margin represents net interest income as a percentage of average interest-earning assets.

Provision for Income Taxes. Income tax expense was \$406,000 and \$430,000 for the three month ending September 30, 2010 and 2009. The Company's effective tax rates for the three months ended September 30, 2010 and 2009 were 32.8% and 33.5%, respectively.

Non Performing Loans. The following table provides information regarding loans past due 90 days or more, all of which were accounted for on a non-accrual basis.

	September 30, 2010	June 30, 2010
	(dollars in thousands)	
Non-accruing Loans		
Secured by Real Estate		
Conventional	\$ 1,837	\$ 1,454
Construction	-	-
Other Loans		
Multi-family	561	
Commercial	-	-
Consumer	-	-
Home Equity Loans and Lines	1	-
Loans on Savings accounts	-	-
Total	2,399	1,454
Accruing Loans - Past 90 days		
Secured by Real Estate		
Conventional	-	-
Construction	-	-
Other Loans		
Commercial	-	-
Consumer	-	-
Home Equity Lines	-	-
Loans on Savings accounts	-	-
Total	-	-
Total non-performing loans	\$ 2,399	\$ 1,454
Real estate owned	1	233
Other non-performing assets		-
Total non-performing assets	\$ 2,400	\$ 1,687
Total non-performing loans/Loans	0.99%	0.62%
Total non-performing loans/Assets	0.75	0.45
Total non-performing Assets/Assets	0.75	0.52

Reposessed assets were \$1,000 and \$233,000 as of September 30, 2010 and June 30, 2010, respectively. The allowance includes a significant provision on a land loan secured by a tract of land in Wildwood, New Jersey due to the ongoing concerns about the financial condition of the borrower on this loan. Monthly payments were current as of September 30, 2010; however payments are being received not from the borrower but from the borrower's business partner, who could cease payment at any time as he is not a party to the loan agreement and has no legal obligation to make payments on this loan. The most recent appraisal the Bank has on this property was prepared in 2004, and although that "as is" appraisal for this undeveloped site was greater than the outstanding balance of the loan, the Bank has designated the loan as special mention in light of the uncertainty related to the development of the property. The issues that could impede the development include zoning, wetlands preservation, site improvements and environmental cleanup. The bank has established a specific reserve of \$585,000 against the balances of six impaired

loans to a troubled borrower. The loans have balances totaling \$1,243,000, they are secured by first liens against ten residential properties, eight properties are located in Trenton NJ, and two are located in Freehold, NJ. The borrowing entities have filed bankruptcy and we are concerned that resolution of the situation will be prolonged. We did not have any troubled debt restructuring (wherein the

borrower is granted a concession that we would not otherwise consider under current market conditions) as of the dates shown in the above table.

#### Liquidity, Commitments and Capital Resources

The Company must be capable of meeting its customer obligations at all times. Potential liquidity demands include funding loan commitments, cash withdrawals from deposit accounts and other funding needs as they present themselves. Accordingly, liquidity is measured by our ability to have sufficient cash reserves on hand, at a reasonable cost and/or with minimum losses.

The Asset and Liability Management Committee and the Board of Directors set limits and controls to guide senior management's monitoring of our overall liquidity position and risk. The Board of Directors and its Committee, along with senior management, are responsible for ensuring that our liquidity needs are being met on both a daily and long term basis.

Our approach to managing day-to-day liquidity is measured through our daily calculation of investable funds and/or borrowing needs to ensure adequate liquidity. In addition, we constantly evaluate our short-term and long-term liquidity risk and strategy based on current market conditions, outside investment and/or borrowing opportunities, short and long-term economic trends, and anticipated short and long-term liquidity requirements. The Company's loan and deposit rates may be adjusted as another means of managing short and long-term liquidity needs. We do not at present participate in derivatives or other types of hedging instruments to meet liquidity demands.

At September 30, 2010, the total approved loan origination commitments outstanding amounted to \$9.2 million. At that date, construction loans in process were \$2.7 million. Certificates of deposit scheduled to mature in one year or less at September 30, 2010, totaled \$54.8 million. Based on the competitive rates and on historical experience, management believes that a significant portion of maturing deposits will remain with the Company. At September 30, 2010, we had an unused borrowing capacity of \$53.3 million from the Federal Home Loan Bank of Pittsburgh which we may use as a funding source to meet commitments and for liquidity purposes.

#### Regulatory Capital Compliance

Consistent with its goals to operate a sound and profitable financial organization, the Bank actively seeks to maintain its status as a well-capitalized institution in accordance with regulatory standards. As of September 30, 2010, the Bank exceeded all applicable regulatory capital requirements and was well capitalized. As of September 30, 2010, our regulatory capital amounts and ratios were as follows:

	Actual	
	Amount	Ratio
	(Dollars in thousands)	
Total risk-based capital	\$ 48,951	24.65%
Core Capital (to risk-weighted assets)	\$ 47,043	23.69%
Core Capital (adjusted total assets)	\$ 47,043	14.76%
Tangible Capital (to adjusted total assets)	\$ 47,043	14.76%



### Off-Balance Sheet Arrangements

We are a party to financial instruments with off-balance-sheet risk in the normal course of our business of investing in loans and securities as well as in the normal course of maintaining and improving the Company's facilities. These financial instruments include significant purchase commitments, such as commitments related to capital expenditure plans and commitments to purchase investment securities or mortgage-backed securities, and commitments to extend credit to meet the financing needs of our customers. At September 30, 2010, we had no significant off-balance sheet commitments other than commitments to extend credit totaling \$9.2 million and unfunded commitments under lines of credit totaling \$13.9 million.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Our exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit is represented by the contractual amount of those instruments. We use the same credit policies in making commitments and conditional obligations as we do for on-balance-sheet instruments. Since a number of commitments typically expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements.

### Impact of Inflation and Changing Prices

The financial statements included in this document have been prepared in accordance with accounting principles generally accepted in the United States of America. These principles require the measurement of financial position and operating results in terms of historical dollars, without considering changes in the relative purchasing power of money over time due to inflation.

Our primary assets and liabilities are monetary in nature. As a result, interest rates have a more significant impact on our performance than the effects of general levels of inflation. Interest rates, however, do not necessarily move in the same direction or with the same magnitude as the price of goods and services, since such prices are affected by inflation. In a period of rapidly rising interest rates, the liquidity and maturities of our assets and liabilities are critical to the maintenance of acceptable performance levels.

The principal effect of inflation on earnings, as distinct from levels of interest rates, is in the area of non interest expense. Expense items such as employee compensation, employee benefits and occupancy and equipment costs may be subject to increases as a result of inflation. An additional effect of inflation is the possible increase in the dollar value of the collateral securing loans that we have made. We are unable to determine the extent, if any, to which properties securing our loans have appreciated in dollar value due to inflation or depreciated due to economic recession.

### ITEM 3 – QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

As a "smaller reporting company" as defined by Item 10 of Regulation S-K, the Company is not required to provide the information required by this item.

### ITEM 4– CONTROLS AND PROCEDURES

An evaluation was performed under the supervision, and with the participation of management, including the principal executive officer and principal financial officer, of the effectiveness of the design



and operation of the disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) promulgated under the Securities Exchange Act of 1934, as amended) as of September 30, 2010. Based on such evaluation, the principal executive officer and principal financial officer have concluded that the disclosure controls and procedures are effective as of September 30, 2010.

No change in the internal controls over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) promulgated under the Securities Exchange Act of 1934, as amended) occurred during the most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the internal control over financial reporting.

## PART II – OTHER INFORMATION

### ITEM 1 – LEGAL PROCEEDINGS

There were no material pending legal proceedings at September 30, 2010 to which the Company or its subsidiaries is a party other than ordinary routine litigation incidental to their respective businesses.

### ITEM 1A – RISK FACTORS

As a “smaller reporting company” as defined by Item 10 of Regulation S-K, the Company is not required to provide the information required by this item.

### ITEM 2 – UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

None

### ITEM 3 – DEFAULTS UPON SENIOR SECURITIES

None

### ITEM 4 –RESERVED

### ITEM 5 – OTHER INFORMATION

None

### ITEM 6 – EXHIBITS

- 3(i) Charter of William Penn Bancorp, Inc. \*
- 3(ii) Specimen Stock Certificate of William Penn Bancorp, Inc. \*
- 4.1 Bylaws of William Penn Bancorp, Inc. \*
- 10.1 Directors Consultation and Retirement Plan \*\*
- 10.2 Deferred Compensation Plan for Directors \*\*
- 10.3 Restated Deferred Compensation Plan \*\*
- 31 Rule 13a-14(a)/15d-14(a) Certifications
- 32 Section 1350 Certification



- \* Incorporated by reference from the Registrant's Registration Statement on Form S-1 (File No. 333-148219)
- \*\* Incorporated by reference from the Registrant's quarterly report Form 10-Q for the quarter ended December 31, 2008.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

WILLIAM PENN BANCORP, INC.  
(Registrant)

/s/ Terry Sager  
Terry Sager, President  
(Duly authorized officer and principal  
executive officer)

Date: November 15, 2010

/s/ Charles Corcoran  
Charles Corcoran, Executive Vice President  
(Principal financial officer)