Capitol Federal Financial Inc
Form 10-Q
February 06, 2012

[Missing Graphic Reference]
UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-Q

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

For the quarterly period ended December 31, 2011

or

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

Commission file number: 001-34814

Capitol Federal Financial, Inc.
(Exact name of registrant as specified in its charter)

Maryland 27-2631712
(State or other jurisdiction of incorporation (I.R.S. Employer
or organization) Identification No.)

700 Kansas Avenue, Topeka, Kansas 66603
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code:
(785) 235-1341

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 requirements for the past 90 days. Yes þ 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 þ No ¨

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

Large accelerated filer	þ	Accelerated filer	¨	Non-accelerated filer (do not check if a smaller reporting company)	¨	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 þ

As of January 30, 2012, there were 167,498,133 shares of Capitol Federal Financial, Inc. Common Stock outstanding.

PART I -- FINANCIAL INFORMATION	Page Number
Item 1. Financial Statements (Unaudited):	
Consolidated Balance Sheets at December 31, 2011 and September 30, 2011	3
Consolidated Statements of Operations for the three months ended December 31, 2011 and 2010	4
Consolidated Statement of Stockholders' Equity for the three months ended December 31, 2011	6
Consolidated Statements of Cash Flows for the three months ended December 31, 2011 and 2010	7
Notes to Consolidated Financial Statements	9
Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations	33
Item 3. Quantitative and Qualitative Disclosure about Market Risk	76
Item 4. Controls and Procedures	81
PART II -- OTHER INFORMATION	
Item 1. Legal Proceedings	81
Item 1A. Risk Factors	81
Item 2. Unregistered Sales of Equity Securities and Use of Proceeds	81
Item 3. Defaults Upon Senior Securities	81
Item 4. (Removed and Reserved)	81
Item 5. Other Information	81
Item 6. Exhibits	81
Signature Page	82
INDEX TO EXHIBITS	83

PART I -- FINANCIAL INFORMATION
Item 1. Financial Statements
CAPITOL FEDERAL FINANCIAL, INC. AND SUBSIDIARY
CONSOLIDATED BALANCE SHEETS (Unaudited)
(Dollars in thousands)

	December 31, 2011	September 30, 2011
ASSETS:		
Cash and cash equivalents (includes interest-earning deposits of $148,323 and $105,292)	$ 170,175	$ 121,070
Securities:		
Available-for-sale ("AFS") at estimated fair value (amortized cost of $1,528,191 and $1,443,529)	1,570,730	1,486,439
Held-to-maturity ("HTM") at amortized cost (estimated fair value of $2,193,944 and $2,434,392)	2,129,417	2,370,117
Loans receivable, net (of allowance for credit losses ("ACL") of $15,605 and $15,465)	5,224,942	5,149,734
Bank-owned life insurance ("BOLI")	56,947	56,534
Capital stock of Federal Home Loan Bank ("FHLB"), at cost	129,503	126,877
Accrued interest receivable	28,285	29,316
Premises and equipment, net	50,383	48,423
Real estate owned ("REO"), net	11,189	11,321
Other assets	49,469	50,968
TOTAL ASSETS	$ 9,421,040	$ 9,450,799
LIABILITIES:		
Deposits	$ 4,501,144	$ 4,495,173
Advances from FHLB, net	2,531,304	2,379,462
Other borrowings	365,000	515,000
Advance payments by borrowers for taxes and insurance	22,285	55,138
Income taxes payable	9,353	2,289
Deferred income tax liabilities, net	20,266	20,447
Accounts payable and accrued expenses	40,379	43,761
Total liabilities	7,489,731	7,511,270
STOCKHOLDERS' EQUITY:		
Preferred stock ($0.01 par value) 100,000,000 shares authorized; none issued	--	--
Common stock ($0.01 par value) 1,400,000,000 shares authorized, 167,498,133 shares issued; 167,498,133 shares outstanding as of December 31, 2011 and September 30, 2011	1,675	1,675
Additional paid-in capital	1,393,508	1,392,691
Unearned compensation, Employee Stock Ownership Plan ("ESOP")	(49,804)	(50,547)
Unearned compensation, Recognition and Retention Plan ("RRP")	(98)	(124)
Retained earnings	559,577	569,127
Accumulated other comprehensive income ("AOCI"), net of tax	26,451	26,707
Total stockholders' equity	1,931,309	1,939,529
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 9,421,040	$ 9,450,799

See accompanying notes to consolidated financial statements.
<Index>

CAPITOL FEDERAL FINANCIAL, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF OPERATIONS (Unaudited)

(Dollars in thousands, except per share data)

	For the Three Months Ended December 31,	
	2011	2010
INTEREST AND DIVIDEND INCOME:		
Loans receivable	$60,675	$65,943
Mortgage-backed securities (“MBS”)	18,373	15,440
Investment securities	4,637	4,775
Capital stock of FHLB	1,091	902
Cash and cash equivalents	51	187
Total interest and dividend income	84,827	87,247
INTEREST EXPENSE:		
FHLB advances	22,339	23,131
Deposits	12,787	17,381
Other borrowings	4,327	6,730
Total interest expense	39,453	47,242
NET INTEREST INCOME	45,374	40,005
PROVISION FOR CREDIT LOSSES	540	650
NET INTEREST INCOME AFTER PROVISION FOR CREDIT LOSSES	44,834	39,355
OTHER INCOME:		
Retail fees and charges	4,164	3,943
Loan fees	575	655
Insurance commissions	569	818
Income from BOLI	412	332
Other income, net	432	569
Total other income	6,152	6,317
OTHER EXPENSES:		
Salaries and employee benefits	10,587	9,991
Communications, information technology, and occupancy	3,909	3,876
Regulatory and outside services	1,435	1,189
Deposit and loan transaction costs	1,230	1,352
Federal insurance premium	1,092	1,858
Advertising and promotional	910	831
Contribution to Capitol Federal Foundation (“Foundation”)	--	40,000
Other expenses, net	2,904	4,241
Total other expenses	22,067	63,338
INCOME (LOSS) BEFORE INCOME TAX EXPENSE	28,919	(17,666)

INCOME TAX EXPENSE (BENEFIT)	10,130	(6,408)
NET INCOME (LOSS)	$18,789	$(11,258)

(Continued)

4

Basic earnings (loss) per common share	$0.12	$(0.07)
Diluted earnings (loss) per common share	$0.12	$(0.07)
Dividends declared per public share	$0.18	$0.80
Basic weighted average common shares	161,922,633	165,540,789
Diluted weighted average common shares	161,930,727	165,540,789

(Concluded)

See accompanying notes to consolidated financial statements.

CAPITOL FEDERAL FINANCIAL, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY
(Unaudited)
(Dollars in thousands, except per share data)

	Common Stock	Additional Paid-In Capital	Unearned Compensation - ESOP	Unearned Compensation - RRP	Retained Earnings	AOCI (Loss)	Total Stockholders' Equity
Balance at October 1, 2011	$ 1,675	$ 1,392,691	$ (50,547)	$ (124)	$ 569,127	$ 26,707	$ 1,939,529
Comprehensive income:							
Net income					18,789		18,789
Changes in unrealized gain/losses on securities AFS, net of deferred income taxes of $115						(256)	(256)
Total comprehensive income							18,533
ESOP activity, net		790	743				1,533
Stock based compensation - stock options and RRP		27		26			53
Dividends on common stock to stockholders ($0.175 per share)					(28,339)		(28,339)
Balance at December 31, 2011	$ 1,675	$ 1,393,508	$ (49,804)	$ (98)	$ 559,577	$ 26,451	$ 1,931,309

See accompanying notes to consolidated financial statements.
<Index>

CAPITOL FEDERAL FINANCIAL, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
(Dollars in thousands)

	For the Three Months Ended December 31,	
	2011	2010
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income (loss)	$18,789	$(11,258)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
FHLB stock dividends	(1,091)	(902)
Provision for credit losses	540	650
Originations of loans receivable held-for-sale (“LHFS”)	(1,641)	(5,424)
Proceeds from sales of LHFS	1,595	6,895
Amortization and accretion of premiums and discounts on securities	2,065	1,431
Depreciation and amortization of premises and equipment	1,199	1,108
Amortization of deferred amounts related to FHLB advances, net	1,842	1,755
Common stock committed to be released for allocation - ESOP	1,533	1,260
Stock based compensation - stock options and RRP	53	74
Changes in:		
Prepaid federal insurance premium	964	1,738
Accrued interest receivable	1,031	1,284
Other assets, net	70	394
Income taxes payable/receivable	6,998	(6,410)
Accounts payable and accrued expenses	(4,995)	662
Net cash provided by (used in) operating activities	28,952	(6,743)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of AFS securities	(273,634)	--
Purchase of HTM securities	(149,706)	(486,425)
Proceeds from calls, maturities and principal reductions of AFS securities	187,947	130,673
Proceeds from calls, maturities and principal reductions of HTM securities	389,366	245,632
Proceeds from the redemption of capital stock of FHLB	2,117	--
Purchases of capital stock of FHLB	(3,652)	--
Loan originations and purchases, net of principal collected and deferred loan fees	(77,848)	42,438
Purchases of premises and equipment	(1,546)	(1,633)
Proceeds from sales of REO	2,330	2,665
Net cash provided by (used in) investing activities	75,374	(66,650)

(Continued)

	For the Three Months Ended December 31,	
	2011	2010
CASH FLOWS FROM FINANCING ACTIVITIES:		
Dividends paid	(28,339)	(16,956)
Deposits, net of withdrawals	5,971	313,481
Proceeds from borrowings	250,000	300,000
Repayments of borrowings	(250,000)	(300,000)
Change in advance payments by borrowers for taxes and insurance	(32,853)	(34,074)
Net proceeds from common stock offering	--	1,075,585
Excess tax benefits from stock options	--	1
Net cash (used in) provided by financing activities	(55,221)	1,338,037
NET INCREASE IN CASH AND CASH EQUIVALENTS	49,105	1,264,644
CASH AND CASH EQUIVALENTS:		
Beginning of period	121,070	65,217
End of period	$170,175	$1,329,861
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Income tax payments	$3,197	$--
Interest payments	$38,471	$46,412
SUPPLEMENTAL DISCLOSURE OF NON-CASH INVESTING AND FINANCING ACTIVITIES:		
Note received from ESOP in exchange for common stock	$--	$47,260
Customer deposit holds related to common stock offering	$--	$17,690

(Concluded)

See accompanying notes to consolidated financial statements.

<Index>

Notes to Consolidated Financial Statements (Unaudited)

1. Summary of Significant Accounting Policies

Basis of Presentation - The accompanying consolidated financial statements of the Company have been prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation have been included. These statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2011, filed with the Securities and Exchange Commission ("SEC"). Interim results are not necessarily indicative of results for a full year.

In preparing the financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and revenues and expenses during the reporting periods. The ACL is a significant estimate that involves a high degree of complexity and requires management to make difficult and subjective judgments and assumptions about highly uncertain matters. The use of different judgments and assumptions could cause reported results to differ significantly. In addition, bank regulators periodically review the Bank's ACL. The bank regulators have the authority to require the Bank, as they can require all banks, to increase the ACL or recognize additional charge-offs based upon their judgments, which may differ from management's judgments. Any increases in the ACL or recognition of additional charge-offs required by bank regulators could adversely affect the Company's financial condition and results of operations.

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary, the Bank. The Bank has a wholly-owned subsidiary, Capitol Funds, Inc. Capitol Funds, Inc. has a wholly-owned subsidiary, Capitol Federal Mortgage Reinsurance Company. All intercompany accounts and transactions have been eliminated in consolidation.

Loans Receivable - Loans receivable that management has the intent and ability to hold for the foreseeable future are carried at the amount of unpaid principal, net of ACL, undisbursed loan funds, unamortized premiums and discounts, and deferred loan origination fees and costs. Net loan origination fees and costs and premiums and discounts are amortized as yield adjustments to interest income using the level-yield method, adjusted for the estimated prepayment speeds of the related loans when applicable. Interest on loans is credited to income as earned and accrued only if deemed collectible.

A loan is considered delinquent when payment has not been received within 30 days of its contractual due date. The accrual of income on loans is discontinued when interest or principal payments are 90 days in arrears. Loans on which the accrual of income has been discontinued are designated as non-accrual and impaired loans and outstanding interest previously credited beyond 90 days delinquent is reversed. A non-accrual loan is returned to accrual status once the contractual payments have been made to bring the loan less than 90 days past due.

Existing loan customers, whose loans have not been sold to third parties and who have not been delinquent on their contractual loan payments during the previous 12 months have the opportunity, for a fee, to endorse their original loan terms to current loan terms being offered. The fee assessed for endorsing the mortgage loan is deferred and amortized over the remaining life of the endorsed loan using the level-yield method and is reflected as an adjustment to interest income. Each endorsement is examined on a loan-by-loan basis and if the new loan terms represent more than a minor change to the loan, then the unamortized balance of the pre-endorsement deferred fees and/or costs associated

with the mortgage loan are recognized in interest income at the time of the endorsement. If the endorsement of terms does not represent more than a minor change to the loan, then the unamortized balance of the pre-endorsement deferred fees or costs continue to be deferred.

For borrowers experiencing financial difficulties, the Bank may grant a concession to the borrower. Generally, the Bank grants a short-term payment accommodation to borrowers who are experiencing a temporary cash flow problem. The most frequently used accommodation is to reduce the monthly payment amount for a period of six to 12 months, often by requiring payments of only interest and escrow during this period. These restructurings result in an extension of the maturity date of the loan. For more severe situations requiring long-term solutions, the Bank also offers interest rate reductions to currently-offered rates and more lengthy extensions of the maturity date. All such concessions are considered a troubled debt restructuring ("TDR"). The Bank does not forgive principal or interest nor does it commit to lend additional funds to debtors whose terms have been modified in TDRs.

A loan is considered impaired when, based on current information and events, it is probable that the Bank will be unable to collect all amounts due, including principal and interest, according to the contractual terms of the loan agreement. Interest income on impaired loans is recognized in the period collected unless the ultimate collection of principal is considered doubtful. Management considers the following loans to be impaired loans: all non-accrual loans, loans classified as substandard, loans with specific valuation allowances ("SVAs"), and TDRs that have not been performing under the new terms for 12 consecutive months or are required by the accounting literature to be classified as a TDR for the life of the loan due to a reduction in the stated interest rate to a rate lower than the current market rate for new debt with similar risk.

Allowance for Credit Losses - The ACL represents management's best estimate of the amount of known and inherent losses in the loan portfolio as of the balance sheet date. Management's methodology for assessing the appropriateness of the ACL consists of a formula analysis model and the establishment of SVAs for identified problem loans. Management maintains the ACL through provisions for credit losses that are charged to income.

For one- to four-family loans, losses are charged-off when a loan is transferred to REO or if there is a short-sale of the collateral. For consumer home equity loans where the Bank holds the first mortgage, if the loan balance is in excess of the fair value and the loan is in foreclosure, the difference between the loan balances and the fair value is charged-off. Estimated selling costs are also taken into consideration when calculating the amount to charge-off for home equity loans. For consumer home equity loans where the Bank does not hold the first mortgage, foreclosure is pursued or the loan balance is charged-off. Other consumer loans that are unsecured are entirely charged-off once the loan is 120 days past due. For multi-family and commercial loans, the Bank records an SVA when it is determined that the collection of all or a portion of a loan may not be collected and the amount of that loss is reasonably estimated.

As permitted by the Office of Thrift Supervision, the Bank had been establishing SVAs for potential loan loss amounts. Starting with the March 31, 2012 reporting period, the Bank will be required to file a Call Report with the Office of the Comptroller of the Currency ("OCC"). The OCC requirements do not permit SVAs; rather, loan charge-offs are required. Management will implement a loan charge-off policy during the second quarter of fiscal year 2012 in order to be in compliance with the OCC requirements. When the charge-off policy is implemented, all SVAs recorded at December 31, 2011, or $3.5 million, will be charged off. This will not impact the provision for credit losses in the consolidated statements of income as the amounts were expensed in previous periods; however, it will reduce the ACL and related loan balances.

The Bank's primary lending emphasis is the origination and purchase of one- to four-family first mortgage loans on residential properties and, to a lesser extent, second mortgage loans on one- to four-family residential properties, resulting in a loan concentration in residential mortgage loans. The Bank has a concentration of loans secured by residential property located in Kansas and Missouri. Based on the composition of the Bank's loan portfolio, the primary risks inherent in the one- to four-family and consumer loan portfolios are the continued weakened economic conditions, continued high levels of unemployment or underemployment, and a continuing decline in residential real estate values. Any one or a combination of these events may adversely affect borrowers' ability to repay their loans, resulting in increased delinquencies, non-performing assets, loan losses, and future loan loss provisions. Although the multi-family and commercial loan portfolio also shares the risk of continued weakened economic conditions, the primary risks for this portfolio include the ability of the borrower to sustain sufficient cash flows from leases and to control expenses to satisfy their contractual debt payments, and/or the ability to utilize personal and/or business resources to pay their contractual debt payments if the cash flows are not sufficient. Additionally, if the Bank were to repossess the secured collateral of a multi-family or commercial loan, the pool of potential buyers is limited more than that for a residential property, therefore, the Bank could hold the property for an extended period of time and/or potentially be forced to sell at a discounted price, resulting in additional losses.

Management considers several quantitative and qualitative factors quarterly while monitoring the credit quality of the loan portfolio and evaluating the adequacy of the ACL. Such factors include: the trend and composition of delinquent and non-performing loans; the results of foreclosed property and short-sale transactions (historical losses and net charge-offs); charge-offs and the establishment of and increase in SVAs; the current status and trends of local and national economies; the trends and current conditions in the residential real estate markets; and loan portfolio growth and concentrations.

The formula analysis model is updated each quarter. Within the formula analysis model, the loan portfolio is segregated into the following categories: one- to four-family loans; multi-family and commercial loans; consumer home equity loans; and other consumer loans. Home equity loans with the same underlying collateral as a one- to four-family loan are combined with the one- to four-family loan in the formula analysis model to calculate a

combined loan-to-value ("LTV") ratio. Impaired loans are excluded from the formula analysis model as they are individually evaluated for impairment. The one- to four-family loan portfolio and related home equity loans are segregated into additional categories based on the following risk characteristics: originated or bulk purchased; interest payments (fixed-rate, adjustable-rate, and interest-only); LTV ratios; borrower's credit scores; and geographic location. The categories were derived by management based on reviewing the historical performance of the one- to four-family loan portfolio and taking into consideration current economic conditions, such as trends in residential real estate values in certain areas of the U.S. and unemployment rates. The geographic location category pertains primarily to certain states in which the Bank has experienced measurable losses on REO and short-sales.

Quantitative loss factors are applied to each loan category in the formula analysis model based on the historical loss experience, which includes charge-offs and current SVAs, adjusted for loan delinquency trends, for each respective loan category. Each quarter, management reviews the historical loss time periods and utilizes the historical loss time periods believed to be the most reflective of the current economic conditions and recent charge-off experience for each respective loan category.

Qualitative loss factors are applied to each loan category in the formula analysis model. The qualitative factors for the one- to four-family and consumer loan portfolios are: unemployment rate trends; collateral value trends; credit score trends; and delinquent loan trends. The qualitative factors for the multi-family and commercial loan portfolio are: unemployment rate trends; collateral value trends; and delinquent loan trends. As loans are classified as special mention or become 30 to 89 days delinquent, the qualitative loss factors increase based upon delinquent loan trends. The qualitative factors were derived by management based on a review of the historical performance of the respective loan portfolios and consideration of current economic conditions and their likely impact to the loan portfolio.

SVAs have been established in connection with individual loan reviews of impaired loans. Since the majority of the Bank's loan portfolio is composed of residential real estate, determining the estimated fair value of the underlying collateral is important in evaluating the amount of SVAs or charge-offs required for impaired one- to four-family loans. If the estimated fair value of the collateral, less estimated costs to sell and anticipated private mortgage insurance ("PMI") proceeds, is less than the current loan balance, an SVA is established, or a charge-off recorded, for the difference. Once a purchased one- to four-family loan is 90 days delinquent, new collateral values are obtained through automated valuation models ("AVMs") or broker price opinions ("BPOs"). An updated AVM or BPO is then requested approximately every six months while the loan is greater than 90 days delinquent. Due to the relatively stable home values in Kansas and Missouri, new appraisals on originated one- to four- family loans are not obtained until a loan enters foreclosure. For originated one- to four-family loans and home equity loans that are impaired and the most recent appraisal is more than one year old, management estimates the fair value of the collateral using the most recently published Federal Housing Finance Agency ("FHFA") index. For those loans where the FHFA fair value estimate results in a value less than the outstanding loan balance, an updated appraisal is obtained and is used to establish the SVA or charge-off amount. If the Bank holds the first and second mortgage, both loans are combined when evaluating the need for an SVA or charge-off amount.

Loans with an outstanding balance of $1.5 million or more are reviewed annually if secured by property in one of the following categories: multi-family (five or more units) property; unimproved land; other improved commercial property; acquisition and development of land projects; developed building lots; office building; single-use building; or retail building. Management may charge-off such losses if deemed appropriate.

Since the Bank's loan portfolio is primarily concentrated in one- to four-family real estate, management monitors residential real estate market value trends in the Bank's local market areas and geographic sections of the U.S. by reference to various industry and market reports, economic releases and surveys, and management's general and specific knowledge of the real estate markets in which the Bank lends, in order to determine what impact, if any, such trends may have on the level of ACL. Reviewing these quantitative and qualitative factors assists management in

evaluating the overall credit quality of the loan portfolio and the reasonableness of the ACL on an ongoing basis, and whether changes need to be made to the Bank's ACL methodology.

Management seeks to apply the ACL methodology in a consistent manner; however, the methodology can be modified in response to changing conditions. During the current quarter, management increased the historical loss amounts in the formula analysis model related to purchased loans and changed the time periods used for certain qualitative loss factors in the formula analysis model to reflect more recent data trends. The increase in historical losses for purchased loans was due to management's plan to implement a charge-off policy during the quarter ended March 31, 2012, as discussed above. Prior to December 31, 2011, the SVAs on purchased loans were not included in their entirety in historical losses, rather, they were adjusted for delinquent loan trends. Starting with the current quarter, the SVAs on purchased loans were included in their entirety in the historical loss amounts.

Assessing the adequacy of the ACL is inherently subjective. Actual results could differ from estimates as a result of changes in economic or market conditions. Changes in estimates could result in a material change in the ACL. In the opinion of management, the ACL, when taken as a whole, is adequate to absorb estimated losses inherent in the loan portfolio. However, future adjustments may be necessary if loan portfolio performance or economic or market conditions differ substantially from the conditions that existed at the time of the initial determinations.

Recent Accounting Pronouncements - In December 2011, the Financial Accounting Standards Board ("FASB") issued Accounting Standard Update ("ASU") 2011-12, Comprehensive Income (Topic 220): Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05, which defers certain provisions of ASU 2011-05, Presentation of Comprehensive Income. One of ASU 2011-05's provisions requires entities to present reclassification adjustments out of accumulated other comprehensive income by component in both the statement in which net income is presented and the statement in which other comprehensive income is presented (for both interim and annual financial statements). Accordingly, this requirement is indefinitely deferred by ASU 2011-12 and will be further deliberated by the FASB at a future date. ASUs 2011-05 and 2011-12 are effective for fiscal years, and interim periods within those years, beginning after December 15, 2011, which is October 1, 2012 for the Company, and should be applied retrospectively for all periods presented in the financial statements. The Company has not yet decided which statement format it will adopt.

In December 2011, the FASB issued ASU 2011-11, Balance Sheet (Topic 210): Disclosures about Offsetting Assets and Liabilities. The ASU requires new disclosures regarding the nature of an entity's rights of setoff and related arrangements associated with its financial instruments and derivative instruments. The new disclosures are designed to make GAAP financial statements more comparable to those prepared under International Financial Reporting Standards. The new disclosures entail presenting information about both gross and net exposures. The new disclosure requirements are effective for annual reporting periods beginning on or after January 1, 2013, which is October 1, 2013 for the Company, and interim periods therein; retrospective application is required. The Company has not yet completed its evaluation of this ASU; however, since the provisions of ASU 2011-11 are disclosure-related, the Company's adoption of this ASU is not expected to have an impact to its financial condition or results of operations.

2. Earnings Per Share

The Company accounts for the shares acquired by its ESOP and the shares awarded pursuant to its RRP in accordance with Accounting Standards Codification ("ASC") 260, which requires that unvested RRP awards that contain nonforfeitable rights to dividends be treated as participating securities in the computation of earnings per share pursuant to the two-class method. The two-class method is an earnings allocation that determines earnings per share for each class of common stock and participating security. Shares acquired by the ESOP are not considered in the basic average shares outstanding until the shares are committed for allocation or vested to an employee's individual account.

	For the Three Months Ended December 31,	
	2011	2010
	(Dollars in thousands, except per share data)	
Net income (loss) (1)	$18,789	$(11,258)
Average common shares outstanding	161,921,133	165,539,517
Average committed ESOP shares outstanding	1,500	1,272
Total basic average common shares outstanding	161,922,633	165,540,789
Effect of dilutive RRP shares (2)	4,351	--
Effect of dilutive stock options (2)	3,743	--
Total diluted average common shares outstanding	161,930,727	165,540,789
Net earnings (loss) per share:		
Basic	$0.12	$(0.07)
Diluted	$0.12	$(0.07)
Antidilutive stock options and RRP shares, excluded from the diluted average common shares outstanding calculation	897,136	--

(1) Net income (loss) available to participating securities (unvested RRP shares) was inconsequential for the three months ended December 31, 2011 and 2010.

(2) RRP shares totaling 4,753 and options totaling 4,743 which were outstanding at December 31, 2010 were not included in the computation of diluted earnings per share as the effect on earnings per share would be antidilutive, due to the net loss for the three months ended December 31, 2010.

3. Securities

The following tables reflect the amortized cost, estimated fair value, and gross unrealized gains and losses of AFS and HTM securities at December 31, 2011 and September 30, 2011. The majority of the MBS and investment portfolios are composed of securities issued by U.S. government-sponsored enterprises ("GSEs").

	December 31, 2011			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
	(Dollars in thousands)			
AFS:				
GSE debentures	$879,175	$3,264	$111	$882,328
Municipal bonds	2,450	117	--	2,567
Trust preferred securities	3,547	--	545	3,002
MBS	643,019	39,814	--	682,833
	1,528,191	43,195	656	1,570,730
HTM:				
GSE debentures	349,922	1,498	--	351,420
Municipal bonds	56,643	2,130	--	58,773
MBS	1,722,852	61,092	193	1,783,751
	2,129,417	64,720	193	2,193,944
	$3,657,608	$107,915	$849	$3,764,674

	September 30, 2011			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
	(Dollars in thousands)			
AFS:				
GSE debentures	$746,545	$1,996	$233	$748,308
Municipal bonds	2,628	126	--	2,754
Trust preferred securities	3,681	--	740	2,941
MBS	690,675	41,764	3	732,436
	1,443,529	43,886	976	1,486,439
HTM:				
GSE debentures	633,483	3,171	--	636,654
Municipal bonds	56,994	2,190	4	59,180
MBS	1,679,640	59,071	153	1,738,558
	2,370,117	64,432	157	2,434,392
	$3,813,646	$108,318	$1,133	$3,920,831

The following tables summarize the estimated fair value and gross unrealized losses of those securities on which an unrealized loss at December 31, 2011 and September 30, 2011 was reported and the continuous unrealized loss position for at least 12 months or less than 12 months as of December 31, 2011 and September 30, 2011.

	December 31, 2011					
		Less Than 12 Months			Equal to or Greater Than 12 Months	
	Count	Estimated Fair Value	Unrealized Losses	Count	Estimated Fair Value	Unrealized Losses
	(Dollars in thousands)					
AFS:						
GSE debentures	3	$56,712	$111	--	$--	$--
Trust preferred securities	--	--	--	1	3,002	545
MBS	--	--	--	--	--	--
	3	$56,712	$111	1	$3,002	$545
HTM:						
GSE debentures	--	$--	$--	--	$--	$--
Municipal bonds	--	--	--	--	--	--
MBS	1	24,356	193	--	--	--
	1	$24,356	$193	--	$--	$--

	September 30, 2011					
		Less Than 12 Months			Equal to or Greater Than 12 Months	
	Count	Estimated Fair Value	Unrealized Losses	Count	Estimated Fair Value	Unrealized Losses
	(Dollars in thousands)					
AFS:						
GSE debentures	7	$230,848	$233	--	$--	$--
Trust preferred securities	--	--	--	1	2,941	740
MBS	5	1,189	3	--	--	--
	12	$232,037	$236	1	$2,941	$740
HTM:						
GSE debentures	--	$--	$--	--	$--	$--
Municipal bonds	2	615	4	--	--	--
MBS	1	25,142	153	--	--	--
	3	$25,757	$157	--	$--	$--

On a quarterly basis, management conducts a formal review of securities for the presence of an other-than-temporary impairment. Management assesses whether an other-than-temporary impairment is present when the fair value of a security is less than its amortized cost basis at the balance sheet date. For such securities, other-than-temporary impairment is considered to have occurred if the Company intends to sell the security, if it is more likely than not the Company will be required to sell the security before recovery of its amortized cost basis, or if the present value of expected cash flows is not sufficient to recover the entire amortized cost.

The unrealized losses at December 31, 2011 and September 30, 2011 are primarily a result of increases in market yields from the time of purchase. In general, as market yields rise, the fair value of securities will decrease; as market yields fall, the fair value of securities will increase. Management generally views changes in fair value caused by changes in interest rates as temporary; therefore, these securities have not been classified as other-than-temporarily impaired. Additionally, the impairment is also considered temporary because scheduled coupon payments have been made, it is anticipated that the entire principal balance will be collected as scheduled, and management neither intends to sell the securities, nor is it more likely than not that the Company will be required to sell the securities before the recovery of the remaining amortized cost amount, which could be at maturity.

The amortized cost and estimated fair value of securities by remaining contractual maturity without consideration for call features or pre-refunding dates as of December 31, 2011 are shown below. Actual maturities of MBS may differ from contractual maturities because borrowers have the right to prepay obligations, generally without penalties. As of December 31, 2011, the amortized cost of the securities in our portfolio which are callable or have pre-refunding dates within one year totaled $788.2 million. Maturities of MBS depend on the repayment characteristics and experience of the underlying financial instruments. Issuers of certain investment securities have the right to call and prepay obligations with or without prepayment penalties.

	AFS		HTM	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
	(Dollars in thousands)			
One year or less	$271,316	$271,821	$2,429	$2,445
One year through five years	585,866	588,643	381,204	383,871
Five years through ten years	170,854	182,375	452,046	470,494
Ten years and thereafter	500,155	527,891	1,293,738	1,337,134
	$1,528,191	$1,570,730	$2,129,417	$2,193,944

The following table presents the carrying value of the MBS in our portfolio by issuer at December 31, 2011 and September 30, 2011.

	December 31, 2011	September 30, 2011
	(Dollars in thousands)	
Federal National Mortgage Association (“FNMA”)	$1,346,180	$1,384,396
Federal Home Loan Mortgage Corporation (“FHLMC”)	859,644	823,728
Government National Mortgage Association	198,505	202,340
Private Issuer	1,356	1,612
	$2,405,685	$2,412,076

The following table presents the taxable and non-taxable components of interest income on investment securities for the three months ended December 31, 2011 and 2010.

	For the Three Months Ended December 31,

	2011	2010
	(Dollars in thousands)	
Taxable	$4,196	$4,271
Non-taxable	441	504
	$4,637	$4,775

The following table summarizes the amortized cost and estimated fair value of securities pledged as collateral as of the dates indicated.

	December 31, 2011		September 30, 2011	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
	(Dollars in thousands)			
Repurchase agreements	$408,804	$429,311	$571,016	$597,286
Retail deposits	--	--	44,429	44,991
Public unit deposits	126,161	133,683	116,472	124,785
Federal Reserve Bank	61,486	63,752	26,666	27,939
	$596,451	$626,746	$758,583	$795,001

4. Loans Receivable and Allowance for Credit Losses

Loans receivable, net at December 31, 2011 and September 30, 2011 is summarized as follows:

	December 31, 2011	September 30, 2011
	(Dollars in thousands)	
Real estate loans:		
One- to four-family	$5,003,708	$4,918,778
Multi-family and commercial	52,524	57,965
Construction	58,869	47,368
Total real estate loans	5,115,101	5,024,111
Consumer loans:		
Home equity	160,029	164,541
Other	7,355	7,224
Total consumer loans	167,384	171,765
Total loans receivable	5,282,485	5,195,876
Less:		
Undisbursed loan funds	33,239	22,531
ACL	15,605	15,465
Discounts/unearned loan fees	20,315	19,093
Premiums/deferred costs	(11,616)	(10,947)
	$5,224,942	$5,149,734

Lending Practices and Underwriting Standards - Originating and purchasing loans secured by one- to four-family residential properties is the Bank's primary business, resulting in a loan concentration in residential first mortgage

loans. The Bank purchases one- to four-family loans, on a loan-by-loan basis, from a select group of correspondent lenders located throughout the central United States. As a result of originating loans in our branches, along with the correspondent lenders in our local markets, the Bank has a concentration of loans secured by real property located in Kansas and Missouri. Additionally, the Bank purchases whole one- to four-family loans in bulk packages from nationwide and correspondent lenders. The Bank also makes consumer loans, construction loans secured by residential or commercial properties, and real estate loans secured by multi-family dwellings.

One- to four-family loans - One- to four-family loans are underwritten manually or by an automated underwriting system developed by a third party. The system's components closely resemble the Bank's manual underwriting standards which are generally in accordance with FHLMC and FNMA manual underwriting guidelines. The automated underwriting system analyzes the applicant's data, with emphasis on credit history, employment and income history, qualifying ratios reflecting the applicant's ability to repay, asset reserves, and LTV ratio. Full

documentation to support the applicant's credit, income, and sufficient funds to cover all applicable fees and reserves at closing is required on all loans. Loans that do not meet the automated underwriting standards are referred to a staff underwriter for manual underwriting. Properties securing one- to four-family loans are appraised by either staff appraisers or fee appraisers, both of which are independent of the loan origination function. The underwriting standards for loans purchased from correspondent and nationwide lenders are generally similar to the Bank's internal underwriting standards. The underwriting of correspondent loans is generally performed by the Bank's underwriters. Before committing to a bulk loan purchase, the Bank's Chief Lending Officer or Secondary Marketing Manager reviews specific criteria such as loan amount, credit scores, LTV ratios, geographic location, and debt ratios of each loan in the pool. If the specific criteria do not meet the Bank's underwriting standards and compensating factors are not sufficient, then a loan will be removed from the population. Before the bulk loan purchase is funded, an internal Bank underwriter or a third party reviews at least 25% of the loan files to confirm loan terms, credit scores, debt service ratios, property appraisals, and other underwriting related documentation. For the tables within this footnote, correspondent loans are included with originated loans, and bulk loan purchases are reported as purchased loans.

The Bank also originates construction-to-permanent loans secured by one- to four-family residential real estate. The majority of the one- to four-family construction loans are secured by property located within the Bank's Kansas City market area. Construction loans are obtained by homeowners who will occupy the property when construction is complete. Construction loans to builders for speculative purposes are not permitted. The application process includes submission of complete plans, specifications, and costs of the project to be constructed. All construction loans are manually underwritten using the Bank's internal underwriting standards. Construction draw requests and the supporting documentation are reviewed and approved by management. The Bank also performs regular documented inspections of the construction project to ensure the funds are being used for the intended purpose and the project is being completed according to the plans and specifications provided.

Multi-family and commercial loans - The Bank's multi-family and commercial real estate loans are secured primarily by properties generally located in the Bank's market areas or surrounding areas. These loans are granted based on the income producing potential of the property and the financial strength of the borrower. At the time of origination, LTV ratios on multi-family and commercial real estate loans cannot exceed 80% of the appraised value of the property securing the loans. The net operating income, which is the income derived from the operation of the property less all operating expenses, must be sufficient to cover the payments related to the outstanding debt at the time of origination. The Bank generally requires personal guarantees of the borrowers covering a portion of the debt in addition to the security property as collateral for these loans. Appraisals on properties securing these loans are performed by independent state certified fee appraisers. Bank policy permits a limited amount of construction-to-permanent loans secured by multi-family dwellings and commercial real estate.

Consumer loans - The Bank offers a variety of secured consumer loans, including home equity loans and lines of credit, home improvement loans, auto loans, and loans secured by savings deposits. The Bank also originates a very limited amount of unsecured loans. The Bank does not originate any consumer loans on an indirect basis, such as contracts purchased from retailers of goods or services which have extended credit to their customers. The majority of the consumer loan portfolio is comprised of home equity lines of credit.

The underwriting standards for consumer loans include a determination of the applicant's payment history on other debts and an assessment of their ability to meet existing obligations and payments on the proposed loan. Although creditworthiness of the applicant is a primary consideration, the underwriting process also includes a comparison of the value of the security in relation to the proposed loan amount.

Credit quality indicators – Based on the Bank's lending emphasis and underwriting standards, management has segmented the loan portfolio into three segments: one- to four-family loans, consumer loans, and multi-family and

commercial loans. The one- to four-family and consumer segments are further grouped into classes for purposes of providing disaggregated information about the credit quality of the loan portfolio. The classes are: one- to four-family loans – originated, one- to four-family loans – purchased, consumer loans – home equity, and consumer loans – other.

The Bank's primary credit quality indicators for the one- to four-family loan and consumer - home equity loan portfolios are delinquency status, asset classifications in accordance with applicable regulations, LTV ratios and borrower credit scores. The Bank's primary credit quality indicators for the multi-family and commercial loan and consumer – other loan portfolios are delinquency status and asset classifications in accordance with applicable regulations.

The following table presents the recorded investment of loans, defined as the unpaid loan principal balance (net of unadvanced funds related to loans in process) inclusive of unearned loan fees and deferred costs, of the Company's 30 to 89 day delinquent loans, 90 or more day delinquent loans, total delinquent loans, total current loans, and the total loans receivable balance at December 31, 2011 and September 30, 2011 by class. In the formula analysis model, loans in the 30 to 89 day delinquent category are assigned a higher loss factor than corresponding performing loans. Loans 90 or more days delinquent are considered impaired loans and are individually evaluated for impairment. At December 31, 2011 and September 30, 2011, all loans in the 90 or more days delinquent category were on nonaccrual status and represented the entire balance of nonaccrual loans. At December 31, 2011 and September 30, 2011, there were no loans 90 or more days delinquent that were still accruing interest.

	December 31, 2011				
	30 to 89 Days Delinquent	90 or More Days Delinquent	Total Delinquent Loans	Current Loans	Total Recorded Investment
	(Dollars in thousands)				
One- to four-family loans - originated	$18,136	$13,793	$31,929	$4,449,883	$4,481,812
One- to four-family loans - purchased	6,854	14,220	21,074	516,739	537,813
Multi-family and commercial loans	--	--	--	53,538	53,538
Consumer - home equity	518	520	1,038	158,991	160,029
Consumer - other	225	8	233	7,122	