EXTREME NETWORKS INC
Form 10-Q
February 08, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D. C. 20549

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 December 31, 2017

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to

Commission file number 000-25711

EXTREME NETWORKS, INC.

(Exact name of registrant as specified in its charter)

| | |
|---|---|
| DELAWARE | 77-0430270 |
| [State or other jurisdiction of incorporation or organization] | [I.R.S Employer Identification No.] |

| | |
|---|---|
| 6480 Via Del Oro, | |
| San Jose, California | 95119 |
| [Address of principal executive office] | [Zip Code] |

Registrant’s telephone number, including area code: (408) 579-2800


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 (§ 229.405 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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company or an emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer” and “smaller reporting company” and “an emerging growth company” in Rule 12b-2 of the Exchange Act.

| | | |
|---|---|---|
| Large accelerated filer | | Accelerated filer |
| Non-accelerated filer | (Do not check if a smaller reporting company) | Smaller reporting company |
| Emerging growth company | | |

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

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

The number of shares of the Registrant’s Common Stock, $.001 par value, outstanding at February 2, 2018, was 115,267,499

EXTREME NETWORKS, INC.

FORM 10-Q

QUARTERLY PERIOD ENDED 2018

INDEX

EXTREME NETWORKS, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands, except share and per share amounts)

(Unaudited)

| | December 31, 2017 | June 30, 2017 (As adjusted) |
|---|---|---|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | $ 127,108 | $ 130,450 |
| Accounts receivable, net of allowance for doubtful accounts of $1,382 at December 31, 2017 and $1,190 at June 30, 2017 | 154,906 | 93,115 |
| Inventories | 83,377 | 47,410 |
| Prepaid expenses and other current assets | 24,772 | 27,867 |
| Total current assets | 390,163 | 298,842 |
| Property and equipment, net | 68,565 | 30,240 |
| Intangible assets, net | 92,925 | 25,337 |
| Goodwill | 130,988 | 80,216 |
| Other assets | 44,267 | 25,065 |
| Total assets | $ 726,908 | $ 459,700 |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Current portion of long-term debt | $ 22,426 | $ 12,280 |
| Accounts payable | 73,553 | 31,587 |
| Accrued compensation and benefits | 49,104 | 42,662 |
| Accrued warranty | 13,010 | 10,584 |
| Deferred revenue | 113,664 | 79,048 |
| Other accrued liabilities | 74,517 | 37,044 |
| Total current liabilities | 346,274 | 213,205 |
| Deferred revenue, less current portion | 38,693 | 25,293 |
| Long-term debt, less current portion | 160,712 | 80,422 |
| Deferred income taxes | 5,163 | 6,576 |
| Other long-term liabilities | 64,347 | 8,526 |
| Commitments and contingencies (Note 9) | | |
| Stockholders' equity: | | |
| Convertible preferred stock, $.001 par value, issuable in series, 2,000,000 shares authorized; none issued | — | — |
| Common stock, $.001 par value, 750,000,000 shares authorized; 113,931,341 shares issued and outstanding at December 31, 2017 and 110,924,508 shares issued and | 114 | 111 |

| | | |
|---|---|---|
| outstanding at June 30, 2017 | | |
| Additional paid-in-capital | 921,716 | 909,155 |
| Accumulated other comprehensive loss | (1,278 ) | (2,302 ) |
| Accumulated deficit | (808,833 ) | (781,286 ) |
| Total stockholders' equity | 111,719 | 125,678 |
| Total liabilities and stockholders' equity | $ 726,908 | $ 459,700 |

See accompanying notes to condensed consolidated financial statements.

EXTREME NETWORKS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except per share amounts)

(Unaudited)

| | Three Months Ended | | Six Months Ended | |
|---|---|---|---|---|
| | December 31, 2017 | December 31, 2016 (As adjusted) | December 31, 2017 | December 31, 2016 (As adjusted) |
| Net revenues: | | | | |
| Product | $174,850 | $ 118,055 | $339,624 | $ 208,148 |
| Service | 56,273 | 38,322 | 103,214 | 70,833 |
| Total net revenues | 231,123 | 156,377 | 442,838 | 278,981 |
| Cost of revenues: | | | | |
| Product | 78,472 | 62,627 | 158,517 | 106,876 |
| Service | 23,665 | 14,098 | 42,954 | 26,567 |
| Total cost of revenues | 102,137 | 76,725 | 201,471 | 133,443 |
| Gross profit: | | | | |
| Product | 96,378 | 55,428 | 181,107 | 101,272 |
| Service | 32,608 | 24,224 | 60,260 | 44,266 |
| Total gross profit | 128,986 | 79,652 | 241,367 | 145,538 |
| Operating expenses: | | | | |
| Research and development | 45,907 | 24,013 | 80,192 | 42,312 |
| Sales and marketing | 65,659 | 41,025 | 121,220 | 77,884 |
| General and administrative | 11,669 | 9,397 | 23,854 | 17,684 |
| Acquisition and integration costs, net of bargain purchase gain | 34,115 | 4,169 | 38,359 | 6,490 |
| Restructuring and related charges, net of reversals | — | 1,853 | — | 1,853 |
| Amortization of intangibles | 2,746 | 2,175 | 4,360 | 6,317 |
| Total operating expenses | 160,096 | 82,632 | 267,985 | 152,540 |
| Operating loss | (31,110) | (2,980) | (26,618) | (7,002) |
| Interest income | 717 | 81 | 1,364 | 138 |
| Interest expense | (2,504) | (1,176) | (4,719) | (1,823) |
| Other income (expense), net | (643) | 1,025 | 2,484 | 802 |
| Loss before income taxes | (33,540) | (3,050) | (27,489) | (7,885) |
| Provision (benefit) for income taxes | (1,617) | 1,179 | 58 | 2,086 |
| Net loss | $(31,923) | $ (4,229) | $(27,547) | $ (9,971) |
| Basic and diluted net loss per share: | | | | |
| Net loss per share - basic | $(0.28) | $ (0.04) | $(0.24) | $ (0.09) |
| Net loss per share - diluted | $(0.28) | $ (0.04) | $(0.24) | $ (0.09) |
| Shares used in per share calculation - basic | 113,621 | 107,425 | 112,931 | 106,690 |
| Shares used in per share calculation - diluted | 113,621 | 107,425 | 112,931 | 106,690 |

See accompanying notes to condensed consolidated financial statements.

EXTREME NETWORKS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

(In thousands)

(Unaudited)

| | Three Months Ended | | Six Months Ended | |
|---|---|---|---|---|
| | December 31, | December 31, | December 31, | December 31, |
| | 2017 | 2016 (As adjusted) | 2017 | 2016 (As adjusted) |
| Net loss: | $(31,923) | $ (4,229) | $(27,547) | $ (9,971) |
| Other comprehensive income (loss), net of tax: | | | | |
| Available for sale securities: | | | | |
| Change in unrealized gains on available for sale securities | 54 | — | 237 | — |
| Net change in foreign currency translation adjustments | 432 | (421) | 787 | (974) |
| Other comprehensive income (loss), net of tax: | 486 | (421) | 1,024 | (974) |
| Total comprehensive loss | $(31,437) | $ (4,650) | $(26,523) | $ (10,945) |

See accompanying notes to condensed consolidated financial statements.

EXTREME NETWORKS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

| | Six Months Ended December 31, 2017 | Six Months Ended December 31, 2016 (As adjusted) |
|---|---|---|
| Cash flows from operating activities: | | |
| Net loss | $ (27,547) | $ (9,971) |
| Adjustments to reconcile net loss to net cash provided by operating activities: | | |
| Depreciation | 8,093 | 4,832 |
| Amortization of intangible assets | 11,023 | 11,593 |
| Provision for doubtful accounts | 1,180 | 154 |
| Stock-based compensation | 11,828 | 6,856 |
| Deferred income taxes | (2,135) | 923 |
| Non-cash restructuring and related charges | — | 1,718 |
| Realized gain on sale of non-marketable equity investment | (3,757) | — |
| Realized gain on bargain purchase | (4,920) | — |
| Other non-cash items | 1,818 | (243) |
| Changes in operating assets and liabilities, net of assets acquired and liabilities assumed | | |
| Accounts receivable | (11,188) | (7,756) |
| Inventories | (449) | 4,313 |
| Prepaid expenses and other assets | 1,188 | 6,823 |
| Accounts payable | 17,547 | (4,444) |
| Accrued compensation and benefits | 3,734 | (916) |
| Deferred revenue | 4,446 | (2,469) |
| Other current and long-term liabilities | 3,387 | 7,875 |
| Net cash provided by operating activities | 14,248 | 19,288 |
| Cash flows from investing activities: | | |
| Capital expenditures | (13,309) | (4,662) |
| Acquisitions | (97,581) | (51,088) |
| Proceeds from sale of non-marketable equity investment | 4,922 | — |
| Net cash used in investing activities | (105,968) | (55,750) |
| Cash flows from financing activities: | | |
| Borrowings under Term Loan | 100,000 | 48,250 |
| Repayments of debt | (8,686) | (5,513) |
| Loan fees on borrowings | (1,494) | (1,327) |
| Proceeds from issuance of common stock, net of tax withholding | (1,536) | 4,831 |
| Net cash provided by financing activities | 88,284 | 46,241 |
| Foreign currency effect on cash | 94 | (115) |
| Net (decrease) increase in cash and cash equivalents | (3,342) | 9,664 |

| | | |
|---|---|---|
| Cash and cash equivalents at beginning of period | 130,450 | 94,122 |
| Cash and cash equivalents at end of period | $127,108 | $ 103,786 |

See accompanying notes to the condensed consolidated financial statements.

EXTREME NETWORKS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

## 1. Description of Business and Basis of Presentation

Extreme Networks, Inc., together with its subsidiaries (collectively referred to as “Extreme” or the “Company”) is a leader in providing software-driven networking solutions for enterprise customers. The Company conducts its sales and marketing activities on a worldwide basis through distributors, resellers and the Company’s field sales organization. Extreme was incorporated in California in 1996 and reincorporated in Delaware in 1999.

The unaudited condensed consolidated financial statements of Extreme included herein have been prepared under the rules and regulations of the Securities and Exchange Commission (“SEC”). Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted under such rules and regulations. The condensed consolidated balance sheet at June 30, 2017 was derived from audited financial statements as of that date but does not include all disclosures required by generally accepted accounting principles for complete financial statements. These interim financial statements and notes should be read in conjunction with the Company’s audited consolidated financial statements and notes thereto included in the Company’s Annual Report on Form 10-K for the fiscal year ended June 30, 2017.

The unaudited condensed consolidated financial statements reflect all adjustments, consisting only of normal recurring adjustments that, in the opinion of management, are necessary for a fair presentation of the results of operations and cash flows for the interim periods presented and the financial condition of Extreme at December 31, 2017. The results of operations for the three and six months ended December 31, 2017 are not necessarily indicative of the results that may be expected for fiscal 2018 or any future periods.

Effective July 1, 2017, the Company adopted the requirements of Accounting Standards Update (“ASU”) No. 2014-09, Revenue from Contracts with Customers. All amounts and disclosures set forth in this Form 10-Q have been updated to comply with the new standards, as indicated by the “as adjusted” footnote.

### Fiscal Year

The Company uses a fiscal calendar year ending on June 30. All references herein to “fiscal 2018” or “2018” represent the fiscal year ending June 30, 2018. All references herein to “fiscal 2017” or “2017” represent the fiscal year ending June 30, 2017.

### Principles of Consolidation

The consolidated financial statements include the accounts of Extreme and its wholly-owned subsidiaries. All inter-company accounts and transactions have been eliminated.

The Company predominantly uses the United States Dollar as its functional currency. The functional currency for certain of its foreign subsidiaries is the local currency. For those subsidiaries that operate in a local currency functional environment, all assets and liabilities are translated to United States Dollars at current month end rates of exchange; and revenue and expenses are translated using the monthly average rate.

### Accounting Estimates

The preparation of financial statements and related disclosures in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Estimates are used for, but are not limited to, the accounting for the allowances for doubtful accounts and sales returns, determining the fair value of acquired assets and assumed liabilities, estimated selling prices, inventory valuation and purchase commitments, depreciation and amortization, impairment of long-lived assets including goodwill, warranty accruals, restructuring liabilities, measurement of share-based compensation costs and income taxes. Actual results could differ from these estimates.

Reclassification

Certain amounts from prior years have been reclassified to conform to the current year's presentation in the accompanying condensed consolidated statements of cash flow. The reclassification had no impact on previously reported net loss or accumulated deficit.

2. Business Combinations

The Company completed three acquisitions during the six months ended December 31, 2017. The acquisitions have been accounted for using the acquisition method of accounting. The purchase price has been allocated on a preliminary basis to tangible and identifiable intangible assets acquired and liabilities assumed. The fair value of working capital related items, such as other current assets and accrued liabilities, approximated their book values at the date of acquisition. Inventories were valued at fair value using the net realizable value approach. The fair value of property and equipment was determined using a cost approach. The fair value of the acquired deferred revenue was estimated using the cost build-up approach. The cost build-up approach determines fair value using estimates of the costs required to provide the contracted deliverables plus an assumed profit. The total costs including the assumed profit were adjusted to present value using a discount rate considered appropriate. The resulting fair value approximates the amount that the Company would be required to pay to a third party to assume the obligation. Valuations of the intangible assets were valued using income approaches based on management projections, which we consider to be Level 3 inputs. The Company also continues to analyze the tax implications of the acquisition of the intangible assets which may ultimately impact the overall level of goodwill associated with the acquisition.

The final purchase price allocation is pending the finalization of valuations, which may result in an adjustment to the preliminary purchase price allocation. Also, additional information which existed as of the acquisition dates, but was unknown to the Company at that time, may become known to the Company during the remainder of the measurement period (up to one year from the acquisition dates), and may result in a change in the purchase price allocation. While management believes that its preliminary estimates and assumptions underlying the valuations are reasonable, different estimates and assumptions could result in different valuations assigned to the individual assets acquired and liabilities assumed, and the resulting amount of goodwill. Results of operations of the acquired entities are included in the Company’s operations beginning with the closing date of each acquisition.

Fiscal 2018 Acquisitions

Data Center Business

On October 27, 2017 (the “Brocade Closing”), the Company completed its acquisition of the data center business (the “Data Center Business”) of Brocade Communication Systems, Inc.’s (“Brocade”), pursuant to an Asset Purchase Agreement (the “Brocade APA”) dated as of October 3, 2017, by and between the Company and Brocade. Under the terms and conditions of the Brocade APA, the Company acquired customers, employees, technology and other assets of the Data Center Business as well as assumed certain contracts and other liabilities of the Data Center Business.

The fair value of consideration transferred on the Brocade Closing date includes:

- upfront cash closing payment equal to $23.0 million,
- deferred payments of $1.0 million per quarter for the next twenty full fiscal quarters of the Company following the acquisition date discounted to their present value,
- contingent consideration in the form of quarterly earnout payments equal to 50% of the profits of the Data Center Business for the five-year period commencing at the end of the first full fiscal quarter of the Company following the acquisition of the Data Center Business discounted to their present value,
- an amount payable due to the excess working capital acquired over the target working capital agreed upon in the Brocade APA, and,
-

portion of the fair value of replacement stock awards granted to employees assumed from Brocade for which their services were provided prior to the Brocade Closing date.

The components of aggregate estimated purchase consideration are as follows (in thousands):

| Estimated purchase consideration | October 27, 2017 |
|---|---|
| Cash paid to sellers at closing | $23,000 |
| Deferred payments | 18,430 |
| Contingent consideration | 34,100 |
| Working capital adjustment | 6,534 |
| Replacement of stock-based awards | 2,273 |
| Aggregate estimated purchase consideration | $84,337 |

The following table below summarizes the preliminary allocation as of October 27, 2017 of the tangible and identifiable intangible assets acquired and liabilities assumed:

| | Preliminary Allocation as of October 27, 2017 |
|---|---|
| Accounts receivables | $ 33,488 |
| Inventories | 19,973 |
| Prepaid expenses and other current assets | 988 |
| Property and equipment | 29,160 |
| Other assets | 4,734 |
| Accounts payable and accrued expenses | (15,850) |
| Deferred revenue | (33,519) |
| Net tangible assets acquired | 38,974 |
| Identifiable intangible assets | 28,600 |
| Goodwill | 16,763 |
| Total intangible assets acquired | 45,363 |
| Total net assets acquired | $ 84,337 |

The following table presents details of the identifiable intangible assets acquired as part of the acquisition (in thousands, except years):

| Intangible Assets | Estimated Useful Life (in years) | Amount |
|---|---|---|
| Developed technology | 2 - 5 | $21,800 |
| Customer relationships | 5 | 5,400 |
| Trade names | 4 | 1,400 |
| Total identifiable intangible assets | | $28,600 |

The amortization for the developed technology is recorded in “Cost of revenues” for product and the amortization for the remaining intangibles is recorded in “Amortization of intangibles” in the accompanying condensed consolidated statements of operations. The goodwill recognized is attributable primarily to expected synergies and the assembled workforce of the Data Center Business. The Company anticipates both the goodwill and intangible assets to be fully deductible for income tax purposes.

The results of operations of the Data Center Business are included with those of the Company beginning October 28, 2017. The associated expenses of the Data Center Business have been incorporated with the results of operations of the Company as a product line and, therefore, stand-alone operating results are not available. In the three and six months ended December 31, 2017 the Company incurred $32.5 million and $33.8 million, respectively, of acquisition and integration related expenses associated with the acquisition of the Data Center Business, including a $25.0 consent fee paid to terminate a previous asset purchase agreement entered into by the Company to purchase the Data Center Business from Broadcom Corporation, in anticipation of Broadcom’s proposed acquisition of Brocade. The fee was paid to allow the Company to buy the Data Center Business directly from Brocade. Such acquisition-related costs are included in “Acquisition and integration costs, net of bargain purchase gain” in the accompanying condensed consolidated statements of operations. The costs, which the Company expensed as incurred, consist primarily of professional fees to financial and legal advisors and IT consultants and companies.

Campus Fabric Business

On July 14, 2017, (the “Avaya Closing Date”) the Company completed its acquisition of Avaya Inc.’s. (“Avaya”) fabric-based secure networking solutions and network security solutions business (the “Campus Fabric Business”) that had been announced on March 7, 2017. Upon the terms and subject to the conditions of the Asset Purchase Agreement (the “Avaya APA”), the Company acquired the customers, employees, technology and other assets of the

Campus Fabric Business, as well as assumed certain contracts and other liabilities of the Campus Fabric Business, for total provisional consideration of $79.8 million, calculated as $100.0 million, less adjustments set forth in the Avaya APA related to net working capital, deferred revenue, certain assumed lease obligations and certain assumed pension obligations for transferring employees of the Campus Fabric Business. Pursuant to certain ancillary agreements, Avaya will also provide the Company with transition services for a period of time following the Avaya Closing Date. As a condition of the Avaya APA, the Company had made deposits of $10.2 million in the third quarter of fiscal 2017, which were applied to the purchase price upon the Avaya Closing Date.

The following table below summarizes the preliminary allocation as of December 31, 2017 of the tangible and identifiable intangible assets acquired and liabilities assumed:

| | Preliminary Allocation as of September 30, 2017 | Change during three months ended December 31, 2017 | | Preliminary Allocation as of December 31, 2017 |
|---|---|---|---|---|
| Accounts receivables | $ 18,112 | $ 183 | (a) | $ 18,295 |
| Inventories | 16,605 | (1,060) | (b)(c) | 15,545 |
| Prepaid expenses and other current assets | 673 | — | | 673 |
| Property and equipment | 3,768 | — | | 3,768 |
| Other assets | 2,568 | 2,743 | (c) | 5,311 |
| Accounts payable and accrued expenses | (29,716) | (2,203) | (d)(f) | (31,919) |
| Deferred revenue | (10,214) | 163 | (d)(e) | (10,051) |
| Other long-term liabilities | (6,608) | 1,403 | (f) | (5,205) |
| Net tangible assets acquired | (4,812) | 1,229 | | (3,583) |
| Identifiable intangible assets | 44,000 | 2,900 | (g) | 46,900 |
| In-process research and development | 2,300 | 200 | (g) | 2,500 |
| Goodwill | 38,338 | (4,329) | | 34,009 |
| Total intangible assets acquired | 84,638 | (1,229) | | 83,409 |
| Total net assets acquired | $ 79,826 | $ — | | $ 79,826 |

The changes during the period in the table above include: a) additional information on accounts receivable as of the acquisition date, b) additional receipts of product, c) a reclassification from inventories to other assets related to service parts, d) a reclassification from deferred revenue to accounts payable, e) an adjustment of the fair value of deferred maintenance revenue, f) a reclassification from long-term liabilities to short-term related to liabilities assumed, g) revised net realizable value based on usefulness of identifiable intangible assets and in-process research and development acquired.

The following table presents details of the identifiable intangible assets acquired as part of the acquisition (in thousands, except years):

| Intangible Assets | Estimated Useful Life (in years) | Amount |
|---|---|---|
| Developed technology | 6 | $37,400 |
| Customer relationships | 4 | 5,100 |
| Trademarks | 5 | 2,600 |
| Backlog | 1 | 1,800 |
| Total identifiable intangible assets | | $46,900 |

The amortization for the developed technology is recorded in “Cost of revenues” for product and the amortization for the remaining intangibles is recorded in “Amortization of intangibles” in the accompanying condensed consolidated statement of operations.  The goodwill recognized is attributable primarily to expected synergies and the assembled workforce of the Campus Fabric Business.  The Company anticipates both the goodwill and intangible assets to be fully deductible for income tax purposes.

The Company also acquired an indefinite lived asset of $2.5 million which represents the fair value of in-process research and development activities. Once the related research and development efforts are completed, the Company will determine whether the asset will continue to be an indefinite lived asset or become a finite lived asset and apply the appropriate accounting accordingly.

The results of operations of the Campus Fabric Business are included in the accompanying condensed consolidated results of operations beginning July 14, 2017. The associated expenses of the Campus Fabric Business have been incorporated with the results of operations of the Company as a product line and, therefore, stand-alone operating results are not available. In the three and six months ended December 31, 2017, the Company incurred $6.6 million and $9.5 million, respectively, of acquisition and integration related expenses associated with the acquisition of the Campus Fabric Business. Such acquisition-related costs are included in “Acquisition and integration costs, net of bargain purchase gain” in the accompanying condensed consolidated statements of operations. The costs, which the Company expensed as incurred, consist primarily of professional fees to financial and legal advisors and IT consultants and companies.

Capital Financing Business

On December 1, 2017, Company completed its acquisition of a capital financing business (the “CF Business”), pursuant to a Bill of Sale and Assignment and Assumption Agreement (the “Assumption Agreement”) between the Company and Broadcom. Under the terms and conditions of the Assumption Agreement, the Company acquired customers, employees, contracts and lease equipment of the CF Business equal to the earn out payments to Broadcom of 90% of acquired financing receivables to be collected commencing at the closing date.

Net assets acquired included financing receivables of $13.8 million, lease equipment of $3.5 million and identifiable intangible assets of $0.6 million, and the fair value of the contingent consideration was $12.9 million. As the preliminary fair value of the net assets acquired exceeded the fair value of the purchase consideration, the Company recorded a gain from the bargain purchase of $4.9 million in “Acquisition and integration costs, net of bargain purchase gain” in the accompanying condensed consolidated statements of operations for the second quarter of fiscal 2018. Acquisition and integration related expenses associated with the acquisition of the CF Business were immaterial.

Fiscal 2017 Acquisition

On October 28, 2016, the Company completed the acquisition of the wireless local area network business (“WLAN Business”) from Zebra Technologies Corporation. Under the terms of the WLAN Asset Purchase Agreement, the Company acquired customers, employees, technology and other assets as well as assumed certain contracts and other liabilities of the WLAN Business, for a net cash consideration to $49.5 million. The following table below summarizes the final allocation of the tangible and identifiable intangible assets acquired and liabilities assumed:

| | Final Allocation as of October 28, 2016 |
|---|---|
| Accounts receivables, net | $ 14,636 |
| Inventories | 13,593 |
| Other current assets | 808 |
| Property and equipment | 3,159 |
| Other assets | 7,634 |
| Deferred revenue | (14,159) |
| Other liabilities | (7,201) |
| Total tangible assets acquired and liabilities assumed | 18,470 |
| Identifiable intangible assets | 20,300 |
| In-process research and development | 1,400 |
| Goodwill | 9,339 |
| Total intangible assets acquired | 31,039 |
| Total net assets acquired | $ 49,509 |

Pro forma financial information

The following unaudited pro forma results of operations are presented as though the acquisitions of the Data Center Business, CF Business, Campus Fabric Business and WLAN Businesses had occurred as of the beginning of the earliest period presented after giving effect to purchase accounting adjustments relating to inventories, deferred revenue, depreciation and amortization on acquired property and equipment and intangibles, acquisition costs, interest income and expense and related tax effects.

The pro forma results of operations are not necessarily indicative of the combined results that would have occurred had the acquisition been consummated as of the earliest period presented, nor are they necessarily indicative of future operating results. The unaudited pro forma results do not include the impact of synergies, nor any potential impacts on current or future market conditions which could alter the unaudited pro forma results.

The unaudited pro forma financial information for the three and six months ended December 31, 2017, combines the results for Extreme for the three and six months ended December 31, 2017, which include the results of the Data Center Business, CF Business and Campus Fabric Business subsequent to the acquisition date and their historical results up to the acquisition date.

The unaudited pro forma financial information for the three and six months ended December 31, 2016, combines the historical results for Extreme for those periods, as adjusted for the adoption of ASC 606, with the historical results of the Data Center Business, CF Business and Campus Fabric Business for the three and six months ended December 31, 2016, as well as the historical results of the WLAN Business up to the acquisition date.

Pro forma results of operations from the Data Center Business, CF Business, Campus Fabric Business and WLAN Business acquisitions included in the pro forma results of operations for the three and six months ended December 31, 2016 or 2017 have not been adjusted for the adoption of ASC 606 because the Company determined that it is impractical to estimate the impact of the adoption.

The following table summarizes the unaudited pro forma financial information (in thousands, except per share amounts):

| | Three Months Ended | | Six Months Ended | |
|---|---|---|---|---|
| | December 31, 2017 | December 31, 2016 (As adjusted) | December 31, 2017 | December 31, 2016 (As adjusted) |
| Net revenues | $252,532 | $ 311,503 | $537,040 | $ 644,435 |
| Net income (loss) | $1,152 | $ (62,134 ) | $(7,622 ) | $ (95,972 ) |
| Net income (loss) per share - basic | $0.01 | $ (0.58 ) | $(0.07 ) | $ (0.90 ) |
| Net income (loss) per share - diluted | $0.01 | $ (0.58 ) | $(0.07 ) | $ (0.90 ) |
| Shares used in per share calculation - basic | 113,621 | 107,425 | 112,931 | 106,690 |
| Shares used in per share calculation - diluted | 119,656 | 107,425 | 112,931 | 106,690 |

3. Summary of Significant Accounting Policies

For a description of significant accounting policies, see Note 3, Summary of Significant Accounting Policies, to the consolidated financial statements included in the Company's Annual Report on Form 10-K for the fiscal year ended June 30, 2017. Except for the following policies, there have been no material changes to the Company's significant accounting policies since the filing of the Annual Report on Form 10-K.

Revenue Recognition

The Company accounts for revenue in accordance with ASC Topic 606, Revenue from Contracts with Customers, which the Company adopted on July 1, 2017, using the retrospective method. The Company derives the majority of its revenue from sales of its networking equipment, with the remaining revenue generated from service fees relating to maintenance contracts, professional services, and training for its products. The Company sells its products and maintenance contracts direct to customers and to partners in two distribution channels, or tiers. The first tier consists of a limited number of independent distributors that stock its products and sell primarily to resellers. The second tier of the distribution channel consists of a non-stocking distributors and value-added resellers that sell directly to end-users. Products and services may be sold separately or in bundled packages.

The Company considers customer purchase orders, which in some cases are governed by master sales agreements, to be the contracts with a customer. For each contract, the Company considers the promise to transfer products and services, each of which are distinct, to be the identified performance obligations. In determining the transaction price the Company evaluates whether the price is subject to refund or adjustment to determine the net consideration to which the Company expects to be entitled.

For all of the Company's sales and distribution channels, revenue is recognized when control of the product is transferred to the customer (i.e., when the Company's performance obligation is satisfied), which typically occurs at shipment for product sales. Revenue from maintenance contracts is recognized over time as the Company's performance obligations are satisfied. This is typically the contractual service period, which ranges from one to three years. For product sales to value-added resellers of the Company, non-stocking distributors and end-user customers, the Company generally does not grant return privileges, except for defective products during the warranty period, nor does the Company grant pricing credits. Sales incentives and other programs that the Company may make available to these customers are considered to be a form of variable consideration and the Company maintains estimated accruals and allowances using the expected value method. There were no material changes in the current period to the estimated transaction price for performance obligations which were satisfied or partially satisfied during previous periods.

Sales to stocking distributors are made under terms allowing certain price adjustments and limited rights of return (known as “stock rotation”) of the Company’s products held in their inventory. Revenue from sales to distributors is recognized upon the transfer of control to the distributor. Frequently, distributors need to sell at a price lower than the contractual distribution price in order to win business, and submit rebate requests for Company pre-approval prior to selling the product through at the discounted price. At the time the distributor invoices its customer or soon thereafter, the distributor submits a rebate claim to the Company to adjust the distributor’s cost from the contractual price to the pre-approved lower price. After the Company verifies that the claim was pre-approved, a credit memo is issued to the distributor for the rebate claim. In determining the transaction price, the Company considers these rebate adjustments to be variable consideration. Such price adjustments are estimated using the expected value method based on an analysis of actual claims, at the distributor level over a trailing twelve-month period of time considered adequate to account for current pricing and business trends. Stock rotation rights grant the distributor the ability to return certain specified amounts of inventory. Stock rotation adjustments are an additional form of variable consideration and are also estimated using the expected value method based on historical return rates. There were no material changes in the current period to the estimated variable consideration for performance obligations which were satisfied or partially satisfied during previous periods.

Performance Obligations. A performance obligation is a promise in a contract to transfer a distinct good or service to the customer, and is the unit of account in ASC Topic 606. A contract's transaction price is allocated to each distinct performance obligation and recognized as revenue when, or as, the performance obligation is satisfied. Certain of the Company's contracts have multiple performance obligations, as the promise to transfer individual goods or services is separately identifiable from other promises in the contracts and, therefore, is distinct. For contracts with multiple performance obligations, the Company allocates the contract's transaction price to each performance obligation based on its relative standalone selling price. The stand-alone selling prices are determined based on the prices at which the Company separately sells these products. For items that are not sold separately, the Company estimates the stand-alone selling prices using the best estimated selling price approach.

The Company's performance obligations are satisfied at a point in time or over time as work progresses. Substantially all of the Company's product sales revenues as reflected on the consolidated statements of operations for the three-month and six-month periods ended December 31, 2017, and 2016 are recognized at a point in time. Substantially all of the Company's service revenue is recognized over time. For revenue recognized over time, the Company uses an input measure, days elapsed, to measure progress.

On December 31, 2017, the Company had $152.4 million of remaining performance obligations, which is comprised of deferred maintenance revenue and services not yet delivered. The Company expects to recognize approximately 54 percent of its remaining performance obligations as revenue in fiscal 2018, an additional 31 percent by fiscal 2019 and 15 percent of the balance thereafter.

Contract Balances. The timing of revenue recognition, billings and cash collections results in billed accounts receivable and deferred revenue in the consolidated balance sheet. Services provided under renewable support arrangements of the Company are billed in accordance with agreed-upon contractual terms, which are typically at periodic intervals (e.g., quarterly or annually). The Company sometimes receives payments from its customers in advance of services being provided, resulting in deferred revenues. These liabilities are reported on the consolidated balance sheet on a contract-by-contract basis at the end of each reporting period.

Revenue recognized for the six-month periods ended December 31, 2017 and 2016, that was included in the deferred revenue balance at the beginning of each period was $53.1 million and $49.7 million respectively. Revenue recognized for the three-month periods ended December 31, 2017 and 2016, that was included in the deferred revenue balance at the beginning of each period was $36.9 million and $33.5 million, respectively.

Contract Costs. The Company recognizes the incremental costs of obtaining contracts as an expense when incurred if the amortization period of the assets that the Company otherwise would have recognized is one year or less. Management expects that commission fees paid to sales representative as a result of obtaining service contracts and contract renewals are recoverable and therefore the Company capitalized them as contract costs in the amount of $3.0 million and $2.5 million at December 31, 2017 and June 30, 2017, respectively. Capitalized commission fees are amortized on a straight-line basis over the average period of service contracts of approximately three years, and are included in "Sales and marketing" in the accompanying condensed consolidated statements of operations. Amortization recognized during the three-month period ended December 31, 2017 and 2016, was $0.5 million and $0.4 million, respectively. Amortization recognized during the six-month period ended December 31, 2017 and 2016, was $0.9 million and $0.7 million, respectively. There was no impairment loss in relation to the costs capitalized.

Revenue by Category: The following table sets forth the Company's revenue disaggregated by sales channel and geographic region based on the billing addresses of its customers (in thousands, unaudited):

| | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Three Months Ended | | | | | | | | | |
| | December 31, | | December 31, | | | | | | | |
| | 2017 | | 2016 | | | | | | | |
| | —% | $2,999 | 3,015 | 1.22 | % | | | | | |
| State and municipal obligations | —— | — | — | 1,212 | 2.30 | 8,614 | 1.54 | 9,826 | 9,992 | 1.64 |
| Corporate debt securities | —— | — | — | 3,916 | 3.82 | — | — | 3,916 | 3,993 | 3.82 |
| Mortgage-backed securities | —— | — | — | — | — | 23,810 | 1.78 | 23,810 | 23,817 | 1.78 |
| Total | $—— % | $2,999 | 1.22% | $5,128 | 3.46% | $32,424 | 1.71% | 40,551 | 40,817 | 1.90% |
| Total Investment Securities | $—— % | $27,463 | 2.45% | $36,294 | 3.01% | $42,734 | 1.82% | $106,491 | $107,204 | 2.39% |

For information regarding the carrying value of the investment portfolio, see Note 6 and Note 12 of the Notes to the Consolidated Financial Statements.

The following table sets forth the carrying value of the Company’s investment securities, as of September 30, for each of the last three years.

| (In thousands) | 2016 | 2015 | 2014 |
|---|---|---|---|
| Investment Securities Available-for-Sale: | | | |
| U.S. government agencies | $— | $815 | $19,256 |
| State and municipal obligations | 25,307 | 42,083 | 2,500 |
| Single issuer trust preferred security | 878 | 850 | 880 |
| Corporate debt securities | 40,202 | 69,982 | 1,525 |
| Mortgage-backed securities: | | | |
| Federal National Mortgage Association | — | 8,692 | 17,226 |
| Federal Home Loan Mortgage Company | — | 5,932 | 15,591 |
| Collateralized mortgage obligations | — | — | 43,965 |
| Total available-for-sale | $66,387 | $128,354 | $100,943 |
| Investment Securities Held-to-Maturity: | | | |
| U.S. government agencies | $2,999 | $14,301 | $— |
| State and municipal obligations | 9,826 | 10,075 | — |
| Corporate debt securities | 3,916 | 4,011 | — |
| Mortgage-backed securities: | | | |
| Collateralized mortgage obligations, fixed-rate | 23,810 | 28,834 | — |
| Total held-to-maturity | $40,551 | $57,221 | $— |
| Total investment securities | $106,938 | $185,575 | $100,943 |

For information regarding the Company’s investment portfolio, see Note 6 and Note 12 of the Notes to the Consolidated Financial Statements.

**Loan Portfolio**

Lending is one of the Company’s primary business activities. The Company’s loan portfolio consists of residential, construction and development, commercial and consumer loans, serving the diverse customer base in its market area. The composition of the Company’s portfolio continues to change due to the local economy. Factors such as the economic climate, interest rates, real estate values and employment all contribute to these changes. Growth is generated through business development efforts, repeat customer requests for new financings, penetration into existing markets and entry into new markets.

At September 30, 2016, total gross loans amounted to $578.4 million, an increase of $184.2 million or 46.7 percent as compared to September 30, 2015. For the year ended September 30, 2016, growth of $181.2 million in commercial loans and $20.8 million in construction and development loans were partially offset by decreases of $5.8 million in residential mortgage loans and $12.0 million in total consumer loans. Even though the Company continues to be challenged by the competition for lending relationships that exist within its market, growth in volume has been achieved through successful lending sales efforts to build on continued customer relationships.

Total average loan volume increased $123.8 million or 32.2 percent in fiscal 2016, while the portfolio yield decreased by 11 basis points compared with fiscal 2015. The increased total average loan volume was due in part to enhanced visibility in the Company’s markets coupled with the aggressive business development activities of its sales team and the opening of our location in Villanova, Pennsylvania, and our Private Banking Loan Production headquarters in Morristown, New Jersey. The volume related factors during the period contributed increased revenue of $5.3 million, while the rate related changes decreased revenue by $589,000. Total average loan volume increased to $508.0 million with a net interest yield of 4.18 percent, compared to $384.1 million with a yield of 4.29 percent for the year ended September 30, 2015. The Company seeks to create growth in commercial lending by offering sound products and competitive pricing and by capitalizing on new and existing relationships in its market area. Products are offered to meet the financial requirements of the Company’s clients. It is the objective of the Company’s credit policies to diversify the commercial loan portfolio to limit concentrations in any single industry.

The loan portfolio is segmented into residential mortgage loans, construction and development loans, commercial loans and consumer loans. The residential mortgage loan segment has one class, one- to four-family first lien residential mortgage loans. The construction and development loan segment consists of the following classes: residential and commercial construction loans and land loans. Residential construction loans are made for the acquisition of and/or construction on a lot or lots on which a residential dwelling is to be built and occupied by the home-owner. Commercial construction loans are made for the purpose of acquiring, developing and constructing a commercial use structure and for acquisition, development and construction of residential properties by residential developers. The commercial loan segment consists of the following classes: commercial real estate loans, multi-family real estate loans, and other commercial loans, which are also generally known as commercial and industrial loans or commercial business loans. The consumer loan segment consists of the following classes: home equity lines of credit, second mortgage loans and other consumer loans, primarily unsecured consumer lines of credit.

*Residential Lending.* Residential mortgages include loans secured by first liens on residential real estate, and are generally made to existing customers of the Bank to purchase or refinance primary and secondary residences. Our residential real estate loans totaled $209.2 million at September 30, 2016, a decrease of $5.8 million, or 2.7%, compared to $215.0 million at September 30, 2015.

*Construction and Development Loans.* Construction and development loans are loans to finance the construction of commercial or residential properties secured by first liens on such properties. We generally limit construction loans to builders and developers with whom we have an established relationship, or who are otherwise known to officers of the Bank. Our construction and development loans totaled $28.6 million at September 30, 2016, an increase of $20.8 million, or 265.7%, compared to $7.8 million at September 30, 2015.

At September 30, 2016, our residential and commercial construction loans totaled $18.6 million, an increase of $12.9 million, or 227.3 percent, compared to $5.7 million at September 30, 2015. Our land loans totaled $10.0 million, an increase of $7.9 million or 367.5 percent, compared to $2.1 million at September 30, 2015.

*Commercial Lending.* Commercial loans are loans made for business purposes and are primarily secured by collateral such as cash balances with the Bank, marketable securities held by or under the control of the Bank, business assets including accounts receivable, inventory and equipment and liens on commercial and residential real estate. Commercial real estate loans include loans secured by first liens on completed commercial properties, including multi-family properties, to purchase or refinance such properties.

Our commercial real estate totaled $231.4 million at September 30, 2016, an increase of $143.8 million, or 163.9 percent, compared to $87.7 million at September 30, 2015.

Our multi-family loans totaled $19.5 million at September 30, 2016, an increase of $12.1 million or 162.2 percent, compared to $7.4 million at September 30, 2015.

Our commercial business loans totaled $38.8 million at September 30, 2016, an increase of $25.4 million or 189.8 percent, compared to $13.4 million at September 30, 2015.

*Consumer Lending.* In our efforts to provide a full range of financial services to our customers, we offer automobile loans, unsecured personal loans and loans secured by deposits.

Our consumer loans totaled $50.9 million at September 30, 2016, a decrease of $12.0 million, or 19.1 percent, compared to $62.9 million at September 30, 2015. Our home equity loans totaled $19.8 million at September 30, 2016, a decrease of $3.2 million, or 13.8 percent, compared to $22.9 million at September 30, 2015. Second mortgages totaled $29.2 million at September 30, 2016, a decrease of $8.4 million or 22.4 percent, compared to $37.6 million at September 30, 2015.

The following table presents information regarding the components of the Company's loan portfolio on the dates indicated.

| | September 30, | | | | |
|---|---|---|---|---|---|
| | 2016 | 2015 | 2014 | 2013 | 2012 |
| | (In thousands) | | | | |
| Residential mortgage | $209,186 | $214,958 | $231,324 | $239,900 | $231,803 |
| Construction and Development: | | | | | |
| Residential and commercial | 18,579 | 5,677 | 5,964 | 6,672 | 20,500 |
| Land | 10,013 | 2,142 | 1,033 | 2,439 | 632 |
| Total construction and development | 28,592 | 7,819 | 6,997 | 9,111 | 21,132 |
| Commercial: | | | | | |
| Commercial real estate | 231,439 | 87,686 | 71,579 | 70,571 | 112,199 |
| Multi-family | 19,515 | 7,444 | 1,032 | 1,971 | 2,087 |
| Farmland | — | — | — | — | — |
| Other | 38,779 | 13,380 | 5,480 | 5,573 | 7,517 |
| Total commercial | 289,733 | 108,510 | 78,091 | 78,115 | 121,803 |
| Consumer: | | | | | |
| Home equity lines of credit | 19,757 | 22,919 | 22,292 | 20,431 | 20,959 |
| Second mortgages | 29,204 | 37,633 | 47,034 | 54,532 | 65,703 |
| Other | 1,914 | 2,359 | 2,839 | 2,648 | 762 |
| Total consumer | 50,875 | 62,911 | 72,165 | 77,611 | 77,611 |
| Total loans | 578,386 | 394,198 | 388,577 | 404,737 | 462,162 |
| Deferred loan fees and costs, net | 1,208 | 1,776 | 2,086 | 2,210 | 2,420 |
| Allowance for loan losses | (5,434 ) | (4,667 ) | (4,589 ) | (5,090 ) | (7,581 ) |
| Loans receivable, net | $574,160 | $391,307 | $386,074 | $401,857 | $457,001 |

The following table presents the contractual maturity of our loans held in portfolio at September 30, 2016. The table does not include the effect of prepayments or scheduled principal amortization. Loans having no stated repayment schedule or maturity and overdraft loans are reported as being due in one year or less.

| | At September 30, 2016, Maturing | | | |
|---|---|---|---|---|
| | In One Year or Less | After One Years Through Five Years | After Five Years | Total |
| | (In thousands) | | | |
| Residential mortgage | $136 | $5,850 | $203,200 | $209,186 |
| Construction and Development: | | | | |
| Residential and commercial | 8,975 | 1,975 | 7,629 | 18,579 |
| Land | — | 10,013 | — | 10,013 |
| Total construction and development | 8,975 | 11,988 | 7,629 | 28,592 |
| Commercial: | | | | |
| Commercial real estate | 10,420 | 49,647 | 171,372 | 231,439 |
| Multi-family | 62 | 7,033 | 12,420 | 19,515 |
| Other | 1,275 | 33,281 | 4,223 | 38,779 |
| Total commercial | 11,757 | 89,961 | 188,015 | 289,733 |
| Consumer: | | | | |
| Home equity lines of credit | — | — | 19,757 | 19,757 |
| Second mortgages | 19 | 2,912 | 26,273 | 29,204 |
| Other | 44 | 1,493 | 377 | 1,914 |
| Total consumer | 63 | 4,405 | 46,407 | 50,875 |
| Total | $20,931 | $112,204 | $445,251 | $578,386 |
| | | | | |
| Loans with: | | | | |
| Fixed rates | $880 | $22,591 | $277,571 | $301,042 |
| Variable rates | 20,051 | 89,613 | 167,680 | 277,344 |
| Total | $20,931 | $112,204 | $445,251 | $578,386 |

For additional information regarding loans, see Note 7 of the Notes to the Consolidated Financial Statements.

Allowance for Loan Losses and Related Provision

The allowance for loan losses is a reserve established through charges to earnings in the form of a provision for loan lease losses. We maintain an allowance for loan losses at a level considered adequate to provide for all known and probable incurred losses in the portfolio. The level of the allowance is based on management's evaluation of estimated losses in the portfolio, after consideration of risk characteristics of the loans and prevailing and anticipated economic conditions. Loan charge-offs (i.e., loans judged to be uncollectible) are charged against the reserve and any subsequent recovery is credited. Our officers analyze risks within the loan portfolio on a continuous basis and through an external independent loan review function, and the results of the loan review function are also reviewed by our Audit Committee. A risk system, consisting of multiple grading categories for each portfolio class, is utilized as an analytical tool to assess risk and appropriate reserves. In addition to the risk system, management further evaluates risk characteristics of the loan portfolio under current and anticipated economic conditions and considers such factors as the financial condition of the borrower, past and expected loss experience, and other factors which management feels deserve recognition in establishing an appropriate reserve. These estimates are reviewed at least quarterly and, as adjustments become necessary, they are recognized in the periods in which they become known. Although management strives to maintain an allowance it deems adequate, future economic changes, deterioration of borrowers' creditworthiness, and the impact of examinations by regulatory agencies all could cause changes to our allowance for loan losses.

At September 30, 2016, the allowance for loan losses was $5.4 million, an increase of $767,000 or 16.4%, from $4.7 million for the year ended September 30, 2015. Net charge-offs totaled $180,000 during fiscal 2016 and $12,000 for fiscal 2015. The allowance for loan losses as a percentage of loans receivable was 0.94% at September 30, 2016 and 1.18% at September 30, 2015.

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Five-Year Statistical Allowance for Loan Losses

The following table reflects the relationship of loan volume, the provision and allowance for loan losses and net charge-offs for the past five years.

| | September 30, | | | | |
|---|---|---|---|---|---|
| | 2016 | 2015 | 2014 | 2013 | 2012 |
| | (Dollars in thousands) | | | | |
| Average loans outstanding | $507,973 | $384,125 | $407,169 | $447,196 | $481,424 |
| Total loans at end of period | $578,386 | $394,198 | $388,577 | $404,737 | $462,162 |
| Analysis of the Allowance of Loan Losses | | | | | |
| Balance at beginning of year | $4,667 | $4,589 | $5,090 | $7,581 | $10,101 |
| Charge-offs: | | | | | |
| Residential mortgage | 9 | — | 83 | 994 | 1,367 |
| Construction and Development: | | | | | |
| Residential and commercial | 91 | 1 | 37 | 5,768 | 826 |
| Land | — | — | — | 99 | — |
| Commercial: | | | | | |
| Commercial real estate | 99 | 48 | 183 | 6,315 | 951 |
| Multi-family | — | — | — | — | 113 |
| Other | — | — | — | 94 | 88 |
| Consumer: | | | | | |
| Home equity lines of credit | — | — | 14 | — | 72 |
| Second mortgages | 291 | 138 | 618 | 1,042 | 1,184 |
| Other | 70 | 34 | 6 | 9 | 22 |
| Total charge-offs | 560 | 221 | 941 | 14,321 | 4,623 |
| Recoveries: | | | | | |
| Residential mortgage | 17 | 17 | 23 | 199 | — |
| Construction and Development: | | | | | |
| Residential and commercial | 243 | 98 | 1 | — | 1,139 |
| Commercial: | | | | | |
| Commercial real estate | 3 | 9 | 9 | 117 | 5 |
| Other | 3 | 3 | 3 | 23 | 2 |
| Consumer: | | | | | |
| Home equity lines of credit | 1 | 2 | 1 | 17 | 2 |
| Second mortgages | 100 | 69 | 136 | 235 | 141 |
| Other | 13 | 11 | 4 | 4 | 4 |
| Total recoveries | 380 | 209 | 177 | 595 | 1,293 |
| Net charge-offs | 180 | 12 | 764 | 13,726 | 3,330 |
| Provision for loan losses | 947 | 90 | 263 | 11,235 | 810 |
| Balance at end of year | $5,434 | $4,667 | $4,589 | $5,090 | $7,581 |
| | 0.04 % | 0.00 % | 0.19 % | 3.07 % | 0.60 % |

| | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| Ratio of net charge-offs during the year to average loans outstanding during the year | | | | | | | | | | |
| Allowance for loan losses as a percentage of total loans at end of year | 0.94 | % | 1.18 | % | 1.18 | % | 1.26 | % | 1.64 | % |

For additional information regarding loans, see Note 7 of the Notes to the Consolidated Financial Statements.

Implicit in the lending function is the fact that loan losses will be experienced and that the risk of loss will vary with the type of loan being made, the creditworthiness of the borrower and prevailing economic conditions. The allowance for loan losses has been allocated in the table below according to the estimated amount deemed to be reasonably necessary to provide for the possibility of losses being incurred within the following categories of loans at September 30, for each of the past five years.

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The table below shows, for three types of loans, the amounts of the allowance allocable to such loans and the percentage of such loans to total loans.

| | September 30, 2016 | | 2015 | | 2014 | | 2013 | | 2012 | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Amount | Loans to Total Loans | Amount | Loans to Total Loans | Amount | Loans to Total Loans | Amount | Loans to Total Loans | Amount | Loans to Total Loans |
| | (Dollars in thousands) | | | | | | | | | |
| Residential mortgage | $1,201 | 36.2 % | $1,486 | 54.5 % | $1,672 | 59.5 % | $1,414 | 59.3 % | $1,487 | 50.2 % |
| Construction and Development: | | | | | | | | | | |
| Residential and commercial | 199 | 3.2 | 30 | 1.5 | 291 | 1.5 | 164 | 1.6 | 724 | 4.4 |
| Land loans | 97 | 1.7 | 35 | 0.5 | 13 | 0.3 | 56 | 0.6 | 11 | 0.1 |
| Commercial: | | | | | | | | | | |
| Commercial real estate | 1,874 | 40.0 | 1,235 | 22.2 | 1,248 | 18.4 | 1,726 | 17.4 | 3,493 | 24.3 |
| Multi-family | 109 | 3.4 | 104 | 1.9 | 29 | 0.3 | 40 | 0.5 | 10 | 0.5 |
| Other | 158 | 6.7 | 108 | 3.4 | 50 | 1.4 | 59 | 1.4 | 226 | 1.6 |
| Consumer: | | | | | | | | | | |
| Home equity lines of credit | 116 | 3.4 | 139 | 5.8 | 168 | 5.8 | 137 | 5.0 | 160 | 4.5 |
| Second mortgages | 467 | 5.0 | 761 | 9.6 | 1,033 | 12.1 | 1,393 | 13.5 | 1,389 | 14.2 |
| Other | 34 | 0.4 | 24 | 0.6 | 23 | 0.7 | 22 | 0.7 | 16 | 0.2 |
| Total allocated | 4,255 | 100.0 | 3,922 | 100.0 | 4,527 | 100.0 | 5,011 | 100.0 | 7,516 | 100.0 |
| Unallocated | 1,179 | — | 745 | — | 62 | — | 79 | — | 65 | — |
| Balance at end of period | $5,434 | 100.0% | $4,667 | 100.0% | $4,589 | 100.0% | $5,090 | 100.0% | $7,581 | 100.0% |

Asset Quality

The Company manages asset quality and credit risk by maintaining diversification in its loan portfolio and through review processes that include analysis of credit requests and ongoing examination of outstanding loans, delinquencies, and potential problem loans, with particular attention to portfolio dynamics and mix. The Company strives to identify loans experiencing difficulty early enough to correct the problems, to record charge-offs promptly based on realistic assessments of current collateral values and cash flows, and to maintain an adequate allowance for loan losses at all times.

It is generally the Company's policy to discontinue interest accruals once a loan is past due as to interest or principal payments for a period of ninety days. When a loan is placed on non-accrual status, interest accruals cease and uncollected accrued interest is reversed and charged against current income. Payments received on non-accrual loans are applied against principal. A loan may be restored to an accruing basis when it again becomes well-secured, all past due amounts have been collected and the borrower continues to make payments for the next six months on a timely basis. Accruing loans past due 90 days or more are generally well-secured and in the process of collection. For additional information regarding loans, see Note 7 of the Notes to the Consolidated Financial Statements.

Non-Performing and Past Due Loans and OREO

Non-performing loans include non-accrual loans and accruing loans which are contractually past due 90 days or more. Non-accrual loans represent loans on which interest accruals have been suspended. In general, it is the policy of management to consider the charge-off of loans at the point they become past due in excess of 90 days, with the exception of loans that are both well-secured and in the process of collection. Non-performing assets include non-performing loans and other real estate owned. Troubled debt restructured loans represent loans to borrowers experiencing financial difficulties on which a concession was granted, such as a reduction in interest rate which is lower than the current market rate for new debt with similar risks, or modified repayment terms, and are performing under the restructured terms. Such loans, as long as they are performing in accordance with their restructured terms, are not included within the Company’s non-performing loans. For additional information regarding loans, see Note 6 of the Notes to the Consolidated Financial Statements.

The following table sets forth, as of the dates indicated, the amount of the Company’s non-accrual loans, accruing loans past due 90 days or more, other real estate owned (‘‘OREO’’) and troubled debt restructurings.

| | At September 30, | | | | |
|---|---|---|---|---|---|
| | 2016 | 2015 | 2014 | 2013 | 2012 |
| | (In thousands) | | | | |
| Non-accrual loans | $1,617 | $1,399 | $2,391 | $1,901 | $9,749 |
| Accruing loans past due 90 days or more | 696 | — | — | — | — |
| Total non-performing loans | 2,313 | 1,399 | 2,391 | 1,901 | 9,749 |
| Other real estate owned | — | 1,168 | 1,964 | 3,962 | 4,594 |
| Total non-performing assets | $2,313 | $2,567 | $4,355 | $5,863 | $14,343 |
| Troubled debt restructured loans — performing | $2,039 | $1,091 | $1,009 | $1,346 | $8,187 |

At September 30, 2016, non-performing assets totaled $2.3 million, or 0.28% of total assets, as compared with $2.6 million, or 0.39%, at September 30, 2015. The reduction in non-performing assets from September 30, 2015 was attributable to two commercial loans to one borrower with an outstanding balance of approximately $492,000 at September 30, 2015 which were returned to accruing status during fiscal 2016, as well as, $117,000 in charge-offs, payments of $212,000, offset in part by the addition of seven single residential loans (totaling approximately $658,000), one commercial real estate loan (totaling approximately $193,000) and six consumer loans (totaling approximately $186,000) into non-accrual status. In addition, the Company reduced other real estate owned at September 30, 2016 to zero as compared to $1.2 million at September 30, 2015. The decrease was attributable to three single residential loans and one commercial real estate loan sold during the fiscal 2016. The decrease in REO at September 30, 2016 compared to September 30, 2015, was due to $1.2 million of sales of REO, at a net gain of $19,000, as well as $20,000 in reduction to fair value which are reflected in other REO expense during fiscal 2016.

Troubled debt restructured loans, totaled $2.2 million and $1.6 million at September 30, 2016 and at September 30, 2015. A total of $2.0 and $1.1 million of troubled debt restructured loans were performing pursuant to the terms of their respective modifications at September 30, 2016 and September 30, 2015, respectively. At September 30, 2016, all except one troubled debt restructured loan with an outstanding balance of approximately $139,000, were deemed performing, while $492,000 in troubled debt restructured loans were deemed non-performing at September 30, 2015. The increase in performing troubled debt restructured loans at September 30, 2016 compared to September 30, 2015 was primarily due to the two commercial loans to one borrower, with an outstanding balance of approximately $492,000 at September 30, 2015, being returned to accruing status, as well as one residential mortgage loan with an outstanding balance of $85,000 and one commercial loan with an outstanding balance of $386,000 being classified as a performing TDR fiscal 2016.

Total non-performing assets decreased $1.8 million from September 30, 2014 to September 30, 2015. The reduction in non-performing assets from September 30, 2014 was achieved notwithstanding the addition of one new residential loan (totaling approximately $40,000), one construction and development loan (totaling approximately $12,000), two commercial loans (totaling approximately $97,000), and two second mortgage loans (totaling approximately $41,000) into non-performing status. This was more than offset by decreases from pay-downs and pay offs of $527,000 of non-performing loans and the return to performing status of $368,000, while $288,000 was moved within the non-performing asset category from non-accrual to OREO. We also sold OREO properties with an aggregate carrying value of $1.1 million with a gain of approximately $124,000 during fiscal 2015.

Other Income

The following table presents the principal categories of non-interest income for each of the years in the three-year period ended September 30, 2016.

| | Year Ended September 30, | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | 2016 | 2015 | **Increase (Decrease)** | % Change | 2015 | 2014 | **Increase (Decrease** | % Change |
| | (Dollars in thousands) | | | | | | | |
| Service charges and other fees | $923 | $989 | $ (66 ) | (6.67 )% | $989 | $947 | $ 42 | 4.44 % |
| Rental income-other | 211 | 249 | (38 ) | (15.26 ) | 249 | 255 | (6 ) | (2.35 ) |
| Gain on sale of investments, net | 565 | 515 | 50 | 9.71 | 515 | 83 | 432 | 520.48 |
| Gain (loss) on disposal of fixed assets | 1 | — | 1 | 100.00 | — | (41 ) | 41 | 100.00 |
| Gain on sale of loans, net | 116 | 102 | 14 | 13.73 | 102 | 352 | (250 ) | (71.02 ) |
| Earnings on bank-owned life insurance | 517 | 680 | (163 ) | (23.97 ) | 680 | 559 | 121 | 21.65 |
| Total other income | $2,333 | $2,535 | $ (202 ) | (7.97 )% | $2,535 | $2,155 | $ 380 | 17.64 % |

For the year ended September 30, 2016, total other income decreased $202,000 compared to fiscal 2015. This was primarily as a result of a $66,000 decrease in service charges, a $38,000 decrease in rental income, and a $163,000 decrease in earnings on bank-owned insurance, partially offset by an increase of $50,000 in net gains on sales of investment securities, an increase of $14,000 in net gain on sale of loans and an increase in gain on disposal of fixed assets of $1,000. Excluding net securities gains and losses, a non-GAAP measure, the Company recorded other income of $1.8 million for the twelve months ended September 30, 2016 compared to $2.0 million for the comparable period in fiscal 2015, a decrease of $252,000, or 12.5 percent.

For fiscal 2015, other income increased by $380,000 compared to fiscal 2014, primarily as a result of $432,000 increase in net securities gains, an increase of $42,000 in service charges on deposit accounts, an increase in bank owned life insurance income of $121,000 and a decrease of $41,000 in loss of disposal of fixed assets, offset in part by decreased income on rental income, and net gain on sale of loans. Excluding net securities gains and losses, a non-GAAP measure, the Company had recorded other income of $2.0 million for the year ended September 30, 2015 compared to other income, excluding net securities gains and losses, of $2.1 million for fiscal 2014, representing an increase of $52,000 or 2.5 percent.

The Company’s other income is presented in the table below excluding net investment security gains.

| | For the Year Ended September 30, | | |
| --- | --- | --- | --- |
| | 2016 | 2015 | 2014 |
| | (In thousands) | | |
| Other income (GAAP basis) | $2,333 | $2,535 | $2,155 |
| Less: Net investment securities gains | 565 | 515 | 83 |
| Other income, excluding net investment securities gain (Non-GAAP) | $1,768 | $2,020 | $2,072 |

Other Expense

The following table presents the principal categories of other expense for each of the years in the three-year period ended September 30, 2016.

| | Year Ended September 30, | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | 2016 | 2015 | Increase (Decrease) | % Change | 2015 | 2014 | Increase (Decrease | % Change |
| | (Dollars in thousands) | | | | | | | |
| Salaries and employee benefits | $6,290 | $5,998 | $ 292 | 4.87 % | $5,998 | $7,770 | $ (1,772 ) | (22.81 )% |
| Occupancy expense | 1,820 | 1,715 | 105 | 6.12 | 1,715 | 2,091 | (376 ) | (17.98 ) |
| Federal deposit insurance premium | 579 | 784 | (205 ) | (26.15 ) | 784 | 735 | 49 | 6.67 |
| Advertising | 131 | 239 | (108 ) | (45.19 ) | 239 | 561 | (322 ) | (57.40 ) |
| Data processing | 1,128 | 1,236 | (108 ) | (8.74 ) | 1,236 | 1,245 | (9 ) | (0.70 ) |
| Professional fees | 1,683 | 1,571 | 112 | 7.13 | 1,571 | 2,205 | (634 ) | (28.75 ) |
| Other real estate owned expense, net | 27 | (46 ) | 73 | (158.70) | (46 ) | (299 ) | 253 | (84.62 ) |
| Other operating expense | 2,264 | 2,464 | (200 ) | (8.12 ) | 2,464 | 2,336 | 128 | 5.48 |
| Total other expense | $13,922 | $13,961 | $ (39 ) | (0.28 )% | $13,961 | $16,644 | $ (2,683 ) | (16.12 )% |

Total other expense decreased $39,000, or 0.3 percent, in fiscal 2016 from fiscal 2015 as compared with a decrease of $2.7 million, or 16.1 percent, from fiscal 2014 to fiscal 2015. Decreases in fiscal 2016 compared to fiscal 2015, primarily included a $205,000 decrease in federal deposit insurance, a $108,000 decrease in advertising, a $108,000 decrease in data processing expense and a $200,000 decrease in other operating expenses. These decreases were partially offset by an increase in salaries and employee benefits of $292,000, a $105,000 increase in occupancy expense, an $112,000 increase in professional fees and a $73,000 change in other real estate owned (income) expense, net.

Prudent management of operating expenses has been and will continue to be a key objective of management in an effort to improve earnings performance. The Company's ratio of other expenses to average assets decreased to 1.85 percent in fiscal 2016 compared to 2.25 percent in fiscal 2015 and 2.84 percent in fiscal 2014.

Salaries and employee benefits increased $292,000 or 4.9 percent in fiscal 2016 compared to fiscal 2015 and decreased $1.8 million or 22.8 percent from fiscal 2014 to fiscal 2015. The increase in fiscal 2016 was primarily attributable to workforce increases. The decrease in fiscal 2015 was primarily attributable to workforce reductions. Salaries and employee benefits accounted for 45.2 percent of total non-interest expense in fiscal 2016, as compared to

43.0 percent and 46.7 percent in fiscal 2015 and fiscal 2014, respectively.

Occupancy expense for fiscal 2016 increased by $105,000 or 6.1 percent, over fiscal 2015. Occupancy expense for fiscal 2015 decreased by $376,000 or 18.0 percent, compared to fiscal 2014. The increase during fiscal 2016 primarily reflected the cost associated with our two new private banking / loan production offices in Villanova, Pennsylvania and Morristown, New Jersey. The increase in fiscal 2016 compared to fiscal 2015 was primarily due to an increase in rent expense of $75,000, an $11,000 increase in real estate taxes and a $15,000 increase in depreciation expense. For the year ended September 30, 2015, the Company recorded decreases of $21,000 in utility expense, $153,000 in insurance, $68,000 in building and equipment maintenance expense, $109,000 in rent expense and $37,000 in real estate taxes compared to fiscal 2014. These decreases were off by an increase of $12,000 in depreciation expense.

Federal deposit insurance premium for fiscal 2016 decreased $205,000, or 26.2 percent, compared to fiscal 2015. The decrease in the federal deposit insurance premium for fiscal 2016 is due to the termination on January 21, 2016 of the Formal Agreement with the Office of the Comptroller of the Currency ("OCC"). For the year ended September 30, 2015, FDIC insurance expense increased $49,000 compared to fiscal 2014.

Advertising expense for fiscal 2016 decreased $108,000, or 44.8 percent, compared to fiscal 2015. The decrease for fiscal 2016 is due to reductions in advertising retainers. For fiscal 2015, these expenses decreased $322,000 or 57.4 percent compared to fiscal 2014.

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Data processing expense for fiscal 2016 decreased $108,000, or 8.7 percent, compared to the fiscal 2015. For fiscal 2015, data processing expense decreased $9,000, or 0.7 percent, over fiscal 2014.

Professional fees for fiscal 2016 increased $112,000, or 7.1 percent, compared to fiscal 2015. The increase is due primarily to an $185,000 increase in legal fees and a $129,000 increase in fees associated with audit and accounting services. The increase was offset by $205,000 reduction in professional services. Professional fees decreased $634,000 in fiscal 2015 from fiscal 2014 primarily due to reduced compliance and legal loan workout issues due to improvements in our level of non-performing assets.

OREO expense (income), net for fiscal 2016 changed by $73,000 or 158.7 percent, compared to fiscal 2015. The change was due to the sale of three single residential loans and one commercial real estate loan sold during fiscal 2016. Due to the sale of such properties, there was a net gain of $19,000, offset by a $20,000 write-down on the commercial property. OREO expense for fiscal 2015 decreased by $253,000 from fiscal 2014 due primarily to a decreased level of OREO properties. The change in other real estate owned expense was primarily due to a $500,000 insurance reimbursement of a fire claim for a property located in Melrose Park, Pennsylvania received during the fourth quarter of fiscal 2014.

Other operating expense decreased in fiscal 2016 by approximately $200,000, or 8.1 percent, compared to fiscal 2015. The decrease during the year ended September 30, 2016 was primarily due to a $373,000 decrease in other operating expense related to $105,000 in reimbursement for an insurance claim paid in fiscal 2015, a $27,000 decrease in OCC assessment fees, a $19,000 decrease in expenses related to director compensation and a reduction of $14,000 in expenses related to education, subscriptions and dues. These expenses were offset by an increase of $135,000 in business expenses related to entertainment and meals and auto expense, a $65,000 increase in telephone expense, a $17,000 increase in contribution expense and an $11,000 increase in expenses associated with annual credit review such as appraisals. Other operating expense increased in fiscal 2015 by approximately $128,000, or 5.5 percent, compared to fiscal 2014. The increase in other operating expense during fiscal 2015 was primarily due to an increase of $121,000 in insurance and bond expense, a $274,000 increase in other operating expense and a $104,000 increase in amortization of mortgage servicing rights, offset by decreases in various expenses. The decreases in other operating expense were due to a $139,000 decrease associated with annual credit review such as appraisals and searches, a $61,000 decrease due to expenses related to education, subscriptions and dues, and a $127,000 decrease for third party fees associated with the dissolution of two former Delaware subsidiaries of the Company during the fourth quarter of fiscal 2014.

Provision for Income Taxes (As Restated)

The Company recorded $6.2 million in income tax benefit in fiscal 2016, compared to $970,000 income tax benefit in fiscal 2015 and a $367,000 income tax benefit in fiscal 2014, respectively. The change in fiscal 2016 resulted from the reversal of approximately $7.8 million representing the valuation allowance related to net deferred tax assets. The effective tax rates for the Company for the years ended September 30, 2016, 2015 and 2014 were 103.3 percent, 26.2

percent and 106.7 percent, respectively. For a more detailed description of income taxes see Note 13 of the Notes to Consolidated Financial Statements.

**Recent Accounting Pronouncements**

Please refer to the note on Recent Accounting Pronouncements in Note 2 to the consolidated financial statements in Item 8 for a detailed discussion of new accounting pronouncements.

**Asset and Liability Management**

Asset and Liability management encompasses an analysis of market risk, the control of interest rate risk (interest sensitivity management) and the ongoing maintenance and planning of liquidity and capital. The composition of the Company’s statement of condition is planned and monitored by the Asset and Liability Committee (“ALCO”). In general, management’s objective is to optimize net interest income and minimize market risk and interest rate risk by monitoring the components of the statement of condition and the interaction of interest rates.

Short-term interest rate exposure analysis is supplemented with an interest sensitivity gap model. The Company utilizes interest sensitivity analysis to measure the responsiveness of net interest income to changes in interest rate levels. Interest rate risk arises when an earning asset matures or when its interest rate changes in a time period different than that of a supporting interest-bearing liability, or when an interest-bearing liability matures or when its interest rate changes in a time period different than that of an earning asset that it supports. While the Company matches only a small portion of specific assets and liabilities, total earning assets and interest-bearing liabilities are grouped to determine the overall interest rate risk within a number of specific time frames. The difference between interest-sensitive assets and interest-sensitive liabilities is referred to as the interest sensitivity gap. At any given point in time, the Company may be in an asset-sensitive position, whereby its interest-sensitive assets exceed its interest-sensitive liabilities, or in a liability-sensitive position, whereby its interest-sensitive liabilities exceed its interest-sensitive assets, depending in part on management's judgment as to projected interest rate trends.

The Company's interest rate sensitivity position in each time frame may be expressed as assets less liabilities, as liabilities less assets, or as the ratio between rate sensitive assets ("RSA") and rate sensitive liabilities ("RSL"). For example, a short-funded position (liabilities repricing before assets) would be expressed as a net negative position, when period gaps are computed by subtracting repricing liabilities from repricing assets. When using the ratio method, a RSA/RSL ratio of 1 indicates a balanced position, a ratio greater than 1 indicates an asset-sensitive position and a ratio less than 1 indicates a liability-sensitive position.

A negative gap and/or a rate sensitivity ratio less than 1 tends to expand net interest margins in a falling rate environment and reduce net interest margins in a rising rate environment. Conversely, when a positive gap occurs, generally margins expand in a rising rate environment and contract in a falling rate environment. From time to time, the Company may elect to deliberately mismatch liabilities and assets in a strategic gap position.

At September 30, 2016, the Company reflected a negative interest sensitivity gap with an interest sensitivity ratio of 0.26:1.00 at the cumulative one-year position. Based on management's perception of interest rates remaining low through 2016, emphasis has been, and is expected to continue to be, placed on controlling liability costs while extending the maturities of liabilities in our efforts to insulate the net interest spread from rising interest rates in the future. However, no assurance can be given that this objective will be met.

The following table sets forth the amounts of our interest-earning assets and interest-bearing liabilities outstanding at September 30, 2016, which we expect, based upon certain assumptions, to reprice or mature in each of the future time periods shown (the "GAP Table"). Except as stated below, the amount of assets and liabilities shown which reprice or mature during a particular period were determined in accordance with the earlier of term to repricing or the contractual maturity of the asset or liability. The table sets forth approximation of the projected repricing of assets and liabilities at September 30, 2016, on the basis of contractual maturities, anticipated prepayments, and scheduled rate adjustments within a three-month period and subsequent selected time intervals. The loan amounts in the table reflect principal balances expected to be redeployed and/or repriced as a result of contractual amortization and anticipated prepayments of adjustable-rate loans and fixed-rate loans, and as a result of contractual rate adjustments on adjustable-rate loans.

| | **6 Months or Less** | **More than 6 Months to 1 Year** | **More than 1 Year to 3 Years** | **More than 3 Year to 5 Years** | **More than 5 Years** | Total Amount |
|---|---|---|---|---|---|---|
| | (Dollars in thousands) | | | | | |
| Interest-earning assets[1]: | | | | | | |
| Loans receivable[2] | $135,248 | $43,968 | $109,614 | $119,185 | $168,750 | $576,765 |
| Investment securities and restricted securities | 11,614 | 3,234 | 28,590 | 40,355 | 28,122 | 111,915 |
| Other interest-earning assets | 95,465 | — | — | — | — | 95,465 |
| Total interest-earning assets | 242,327 | 47,202 | 138,204 | 159,540 | 196,872 | 784,145 |
| Interest-bearing liabilities: | | | | | | |
| Demand and NOW accounts | 95,041 | — | — | — | — | 95,041 |
| Money market accounts | 177,486 | — | — | — | — | 177,486 |
| Savings accounts | 44,714 | — | — | — | — | 44,714 |
| Certificate accounts | 89,944 | 60,670 | 65,887 | 24,769 | 8,988 | 250,258 |
| FHLB advances | 35,000 | — | 55,000 | 28,000 | — | 118,000 |
| Total interest-bearing liabilities | 442,185 | 60,670 | 120,887 | 52,769 | 8,988 | 685,499 |
| Interest-earning assets less interest-bearing liabilities | $(199,858) | $(13,468) | $17,317 | $106,771 | $187,884 | $98,646 |
| Cumulative interest-rate sensitivity gap[3] | $(199,858) | $(213,326) | $(196,009) | $(89,238) | $98,646 | |
| Cumulative interest-rate gap as a percentage of total assets at September 30, 2016 | (24.34)% | (25.98)% | (23.87)% | (10.87)% | 12.01% | |
| Cumulative interest-earning assets as a percentage of cumulative interest-bearing liabilities at September 30, 2016 | 54.80% | 57.58% | 68.58% | 86.81% | 114.39% | |

(1) Interest-earning assets are included in the period in which the balances are expected to be redeployed and /or repriced as a result of anticipated prepayments, scheduled rate adjustments and contractual maturities.
(2) For purposes of the gap analysis, loans receivable includes non-performing loans gross of the allowance for loan losses, undisbursed loan funds, unamortized discounts and deferred loans fees.
(3) Interest-rate sensitivity gap represents the net cumulative difference between interest-earning assets and interest-bearing liabilities.

**Net Portfolio Value and Net Interest Income Analysis.** Our interest rate sensitivity also is monitored by management through the use of models which generate estimates of the change in its net portfolio value ("NPV") and net interest income ("NII") over a range of interest rate scenarios. NPV is the present value of expected cash flows from assets, liabilities, and off-balance sheet contracts. The NPV ratio, under any interest rate scenario, is defined as the NPV in that scenario divided by the market value of assets in the same scenario.

The table below sets forth as of September 30, 2016 and 2015, the estimated changes in our net portfolio value that would result from designated instantaneous changes in the United States Treasury yield curve. Computations of prospective effects of hypothetical interest rates changes are based on numerous assumptions including relative levels of market interest rates, loan prepayments and deposit decay, and should not be relied upon as indicative of actual results.

| **Changes in Interest Rates (basis points)**[(1)] | As of September 30, 2016 | | | As of September 30, 2015 | | |
|---|---|---|---|---|---|---|
| | Amount | Dollar Change from Base | Percentage Change from Base | Amount | Dollar Change from Base | Percentage Change from Base |
| | (Dollars in thousands) | | | | | |
| +300 | $82,438 | $(22,296) | (21)% | $62,346 | $(31,016) | (33)% |
| +200 | 91,344 | (13,390) | (13) | 73,513 | (19,849) | (21) |
| +100 | 99,266 | (5,468) | (5) | 84,140 | (9,222) | (10) |
| 0 | 104,734 | — | — | 93,362 | — | — |
| -100 | 106,608 | 1,874 | 2 | 94,944 | 1,582 | 2 |

(1) Assumes an instantaneous uniform change in interest rates. A basis point equals 0.01%.

In addition to modeling changes in NPV, we also analyze potential changes to NII for a twelve-month period under rising and falling interest rate scenarios. The following table shows our NII model as of September 30, 2016.

| Changes in Interest Rates in Basis Points (Rate Shock) | Net Interest Income | $ Change | % Change |
|---|---|---|---|
| | (Dollars in thousands) | | |
| 200 | $23,100 | $ 1,380 | 6.35 % |
| 100 | 22,440 | 720 | 3.31 |
| Static | 21,720 | — | — |
| (100) | 21,191 | (529) | (2.44) |

As is the case with the GAP Table, certain shortcomings are inherent in the methodology used in the above interest rate risk measurements. Modeling changes in NPV and NII require the making of certain assumptions which may or may not reflect the manner in which actual yields and costs respond to changes in market interest rates. In this regard, the models presented assume that the composition of our interest sensitive assets and liabilities existing at the beginning of a period remains constant over the period being measured and also assumes that a particular change in interest rates is reflected uniformly across the yield curve regardless of the duration to maturity or repricing of specific assets and liabilities. Accordingly, although the NPV measurements and net interest income models provide an indication of interest rate risk exposure at a particular point in time, such measurements are not intended to and do not provide a precise forecast of the effect of changes in market interest rates on net interest income and will differ from actual results.

**Estimates of Fair Value**

The estimation of fair value is significant to a number of the Company’s assets, including investment securities available-for-sale. These are all recorded at either fair value or the lower of cost or fair value. Fair values are volatile and may be influenced by a number of factors. Circumstances that could cause estimates of the fair value of certain assets and liabilities to change include a change in prepayment speeds, discount rates, or market interest rates. Fair values for most available-for-sale investment securities are based on quoted market prices. If quoted market prices are not available, fair values are based on judgments regarding future expected loss experience, current economic condition risk characteristics of various financial instruments, and other factors. These estimates are subjective in nature, involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

**Impact of Inflation and Changing Prices**

The financial statements and notes thereto presented elsewhere herein have been prepared in accordance with generally accepted accounting principles, which require the measurement of financial position and operating results in terms of historical dollars without considering the change in the relative purchasing power of money over time due to inflation. The impact of inflation is reflected in the increased cost of operations; unlike most industrial companies, nearly all of the Company’s assets and liabilities are monetary. As a result, interest rates have a greater impact on performance than do the effects of general levels of inflation. Interest rates do not necessarily move in the same direction or to the same extent as the prices of goods and services.

**Liquidity**

The liquidity position of the Company is dependent primarily on successful management of the Bank's assets and liabilities so as to meet the needs of both deposit and credit customers. Liquidity needs arise principally to accommodate possible deposit outflows and to meet customers' requests for loans. Scheduled principal loan repayments, maturing investments, short-term liquid assets and deposit inflows, can satisfy such needs. The objective of liquidity management is to enable the Company to maintain sufficient liquidity to meet its obligations in a timely and cost-effective manner.

Management monitors current and projected cash flows, and adjusts positions as necessary to maintain adequate levels of liquidity. Under its liquidity risk management program, the Company regularly monitors correspondent bank funding exposure and credit exposure in accordance with guidelines issued by the banking regulatory authorities. Management uses a variety of potential funding sources and staggering maturities to reduce the risk of potential funding pressure. Management also maintains a detailed contingency funding plan designed to respond adequately to situations which could lead to stresses on liquidity. Management believes that the Company has the funding capacity to meet the liquidity needs arising from potential events. The Company maintains borrowing capacity through the Federal Home Loan Bank of Pittsburgh secured with loans and marketable securities.

The Company's primary sources of short-term liquidity consist of cash and cash equivalents and investment securities available-for-sale.

At September 30, 2016, the Company had $96.8 million in cash and cash equivalents compared to $40.3 million at September 30, 2015. In addition, our investment securities available-for-sale amounted to $66.4 million at September 30, 2016 and $128.4 million at September 30, 2015.

**Deposits**

Total deposits increased to $602.0 million at September 30, 2016 from $465.5 million at September 30, 2015. Total interest-bearing deposits increased from $438.5 million at September 30, 2015 to $567.5 million at September 30, 2016, an increase of $129.0 million or 29.4 percent. Interest-bearing demand, savings, money market and time deposits under $100,000 increased $75.7 million to a total of $400.4 million at September 30, 2016 as compared to $324.7 million at September 30, 2015. Time deposits $100,000 and over increased $53.3 million at September 30, 2016 as compared to September 30, 2015. Time deposits $100,000 and over represented 27.8 percent of total deposits at September 30, 2016 compared to 24.5 percent at September 30, 2015. We had brokered deposits totaling $58.8 million at September 30, 2016. We had no brokered deposits at September 30, 2015.

The Company derives a significant proportion of its liquidity from its core deposit base. Total demand deposits, savings and money market accounts of $351.8 million at September 30, 2016 increased by $88.0 million, or 33.4 percent, from September 30, 2015. Total demand deposits, savings and money market accounts were 58.4 percent of total deposits at September 30, 2016 and 56.7 percent at September 30, 2015. Alternatively, the Company uses a more stringent calculation for the management of its liquidity positions internally, which calculation consists of total demand, savings accounts and money market accounts (excluding money market accounts and certificates of deposit greater than $100,000) as a percentage of total deposits. This number increased by $13.8 million, or 5.4 percent, from $258.1 million at September 30, 2015 to $272.0 million at September 30, 2016 and represented 45.2 percent of total deposits at September 30, 2016 as compared with 55.5 percent at September 30, 2015.

The Company continues to place the main focus of its deposit gathering efforts in the maintenance, development, and expansion of its core deposit base. Management believes that the emphasis on serving the needs of our communities will provide a long term relationship base that will allow the Company to efficiently compete for business in its market. The success of this strategy is reflected in the growth of the demand, savings and money market balances during fiscal 2016.

The following table depicts the Company's core deposit mix at September 30, 2016 and 2015 based on the Company's alternative calculation:

| | September 30, | | | | Net Change 2016 vs. 2015 |
|---|---|---|---|---|---|
| | 2016 | | 2015 | | |
| | Amount | Percentage | Amount | Percentage | |
| | (Dollars in thousands) | | | | |
| Non interest-bearing demand | $34,547 | 12.7 % | $27,010 | 10.5 % | $7,537 |
| Interest-bearing demand | 95,041 | 35.0 | 82,897 | 32.1 | 12,144 |
| Savings | 44,714 | 16.4 | 45,189 | 17.5 | (475) |
| Money market deposits under $100,000 | 14,543 | 5.3 | 15,154 | 5.9 | (611) |
| Certificates of deposit under $100,000 | 83,110 | 30.6 | 87,880 | 34.0 | (4,770) |
| Total core deposits | $271,955 | 100.0 % | $258,130 | 100.0 % | $13,825 |
| | | | | | |
| Total deposits | $602,046 | | $465,522 | | $136,524 |
| Core deposits to total deposits | | 45.2 % | | 55.5 % | |

At September 30, 2016, our certificates of deposit and other time deposits with a balance of $100,000 or more amounted to $167.1 million, of which $110.1 million are scheduled to mature within twelve months. At September 30, 2016, the weighted average remaining maturity of our certificate of deposit accounts was 16.4 months. The following table presents the maturity of our certificates of deposit and other time deposits with balances of $100,000 or more.

| | Amount (In thousands) |
|---|---|
| Maturity Period: | |
| Three months or less | $48,256 |
| Over three months through six months | 20,229 |
| Over six months through twelve months | 41,635 |
| Over twelve months | 57,028 |
| Total | $167,148 |

**Borrowings**

Borrowings from the Federal Home Loan Bank ("FHLB") of Pittsburgh are available to supplement the Company's liquidity position and, to the extent that maturing deposits do not remain with the Company, management may replace such funds with advances. As of September 30, 2016 and 2015, the Company’s outstanding balance of FHLB advance, totaled $118.0 million and $103.0 million, respectively. Of the $118.0 million in advances, $28.0 million represent long-term, fixed-rate advances maturing in 2020 that have terms enabling the FHLB to call the borrowing at their option prior to maturity. The remaining balance of long-term, fixed rate advances totaled $55.0 million, representing five separate advances maturing during fiscal year 2019. At September 30, 2016, there were two short-term FHLB advances totaling $35.0 million of fixed-rate borrowing with rollover of 90 days.

**Cash Flows (As Restated)**

The Consolidated Statements of Cash Flows present the changes in cash and cash equivalents resulting from the Company’s operating, investing and financing activities. During the year ended September 30, 2016, cash and cash equivalents increased by $56.5 million over the balance at September 30, 2015. Net cash of $9.3 million was provided by operating activities in fiscal 2016, primarily, net income as adjusted to net cash. Net income of $12.2 million in fiscal 2016 was adjusted principally by net gains on sales of investment securities of $565,000, amortization of premiums and accretion of discounts on investment securities net of $1.2 million, an increase in other assets of $44,000 and an increase in other liabilities of $766,000. Net cash used by investing activities amounted to approximately $104.2 million in fiscal 2016, primarily reflecting a net decrease in investment securities of $78.6 million. Net cash of $151.4 million was provided by financing activities in fiscal 2016, primarily from the increase in deposits of $136.5 million and an increase of $15.0 million in FHLB advances.

**Payments Due Under Contractual Obligations**

The following table presents information relating to the Company's payments due under contractual obligations as of September 30, 2016.

| | Payments Due by Period | | | | |
|---|---|---|---|---|---|
| | Less than One Year | One to Three Years | Three to Five Years | More than Five Years | Total |
| | (In thousands) | | | | |
| Long-term debt obligations[1] | $35,057 | $30,995 | $56,776 | $— | $122,828 |
| Certificates of deposit[1] | 152,538 | 67,012 | 25,225 | 9,159 | 253,934 |
| Operating lease obligations | 385 | 860 | 900 | 2,225 | 4,370 |
| Total contractual obligations | $187,980 | $98,867 | $82,901 | $11,384 | $381,132 |

[1] Includes interest payments.

**Off-Balance Sheet Arrangements**

In the normal course of operations, the Company engages in a variety of financial transactions that, in accordance with U.S. GAAP, are not recorded in its financial statements. These transactions involve, to varying degrees, elements of credit, interest rate, and liquidity risk. Such transactions are used primarily to manage customers' requests for funding and take the form of loan commitments, lines of credit and letters of credit.

The contractual amounts of commitments to extend credit represent the amounts of potential accounting loss should the contract be fully drawn upon, the customer defaults and the value of any existing collateral becomes worthless. We use the same credit policies in making commitments and conditional obligations as we do for on-balance sheet instruments. Financial instruments whose contract amounts represent credit risk at September 30, 2016 and 2015 were as follows:

| | September 30, | |
|---|---|---|
| | 2016 | 2015 |

| | (In thousands) | |
|---|---|---|
| Commitments to extend credit:[1] | | |
| Future loan commitments | $97,566 | $26,849 |
| Undisbursed construction loans | 33,135 | 14,187 |
| Undisbursed home equity lines of credit | 25,270 | 27,074 |
| Undisbursed Commercial lines of credit | 48,667 | 25,600 |
| Overdraft protection lines | 850 | 840 |
| Standby letters of credit | 1,927 | 566 |
| Total commitments | $207,415 | $95,116 |

(1) 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 may require payment of a fee and generally have fixed expiration dates or other termination clauses.

We anticipate that we will continue to have sufficient funds and alternative funding sources to meet our current commitments.

Shareholders’ Equity (As Restated)

Total shareholders’ equity amounted to $96.2 million, or 11.7 percent of total assets, at September 30, 2016, compared to $82.7 million or 12.6 percent of total assets at September 30, 2015. Book value per common share was $14.66 at September 30, 2016, compared to $12.62 at September 30, 2015.

**Capital (As Restated)**

At September 30, 2016, the Bank's common equity tier 1 ratio was 14.50 percent, tier 1 leverage ratio was 10.98 percent, tier 1 risk-based capital ratio was 14.50 percent and the total risk-based capital ratio was 15.42 percent. At September 30, 2015, the Bank's common equity tier 1 ratio was 16.21 percent, tier 1 leverage ratio was 11.01 percent, tier 1 risk-based capital ratio was 16.21 percent and the total risk-based capital ratio was 17.30 percent. At September 30, 2016, the Bank was in compliance with all applicable regulatory capital requirements.

**Item 8. Financial Statements and Supplementary Data.**

**Report of Independent Registered Public Accounting Firm**

To the Board of Directors and Shareholders

Malvern Bancorp, Inc. and Subsidiaries

Paoli, Pennsylvania

We have audited the accompanying consolidated statement of financial condition of Malvern Bancorp Inc. and its subsidiaries (collectively the "Company") as of September 30, 2016 and 2015 and the related consolidated statements of operations, comprehensive income, changes in shareholders' equity, and cash flows for each of the three years in the period ended September 30, 2016. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Malvern Bancorp, Inc. and its subsidiaries at September 30, 2016 and 2015, and the results of their operations and their cash flows for each of the three years in the period ended September 30, 2016**,** in conformity with accounting principles generally accepted in the United States of America.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Malvern Bancorp Inc.'s internal control over financial reporting as of September 30, 2016, based on criteria established in Internal Control – Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria) and our report dated December 13, 2016 (except as to the effect of the material weakness which is dated as of December 15, 2017) expressed an adverse opinion thereon.

As discussed in Note 3 to the consolidated financial statements, the Company restated its consolidated financial statements for the years ended September 30, 2016 and 2015, to correct a misstatement.

/s/ BDO USA, LLP

Philadelphia, Pennsylvania

December 13, 2016, except Note 3 is dated as of December 15, 2017

*Malvern Bancorp, Inc. and Subsidiaries*

**Consolidated Statements of Financial Condition**

| | September 30, | |
|---|---|---|
| | 2016 | 2015 |
| | (Dollars in thousands, except per share data) | |
| | (As Restated – Note 3) | |
| Assets | | |
| Cash and due from depository institutions | $1,297 | $16,026 |
| Interest bearing deposits in depository institutions | 95,465 | 24,237 |
| Cash and Cash Equivalents | 96,762 | 40,263 |
| Investment securities available for sale, at fair value | 66,387 | 128,354 |
| Investment securities held to maturity, at cost (fair value of $40,817 and $56,825, respectively) | 40,551 | 57,221 |
| Restricted stock, at cost | 5,424 | 4,765 |
| Loans receivable, net of allowance for loan losses of $5,434 and $4,667, respectively | 574,160 | 391,307 |
| Other real estate owned | — | 1,168 |
| Accrued interest receivable | 2,558 | 2,484 |
| Property and equipment, net | 6,637 | 6,535 |
| Deferred income taxes, net | 8,827 | 2,874 |
| Bank-owned life insurance | 18,418 | 17,905 |
| Other assets | 1,548 | 2,814 |
| Total Assets | $821,272 | $655,690 |
| Liabilities and Shareholders' Equity | | |
| Liabilities | | |
| Deposits: | | |
| Deposits-noninterest-bearing | $34,547 | $27,010 |
| Deposits-interest-bearing | 567,499 | 438,512 |
| Total Deposits | 602,046 | 465,522 |
| FHLB advances | 118,000 | 103,000 |
| Advances from borrowers for taxes and insurance | 1,659 | 1,806 |
| Accrued interest payable | 427 | 396 |
| Other liabilities | 2,983 | 2,217 |
| Total Liabilities | 725,115 | 572,941 |
| Commitments and Contingencies | — | — |
| Shareholders' Equity | | |
| Preferred stock, $0.01 par value, 10,000,000 shares authorized, none issued | — | — |
| Common stock, $0.01 par value, 40,000,000 shares authorized, issued and outstanding: 6,560,403 shares at September 30, 2016 and 6,558,473 shares at September 30, 2015 | 66 | 66 |

| | | |
|---|---|---|
| Additional paid-in-capital | 60,461 | 60,365 |
| Retained earnings | 37,322 | 25,172 |
| Unearned Employee Stock Ownership Plan (ESOP) shares | (1,629 ) | (1,775 ) |
| Accumulated other comprehensive loss | (63 ) | (1,079 ) |
| Total Shareholders' Equity | 96,157 | 82,749 |
| Total Liabilities and Shareholders' Equity | $821,272 | $655,690 |

*See notes to consolidated financial statements.*

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***Malvern Bancorp, Inc. and Subsidiaries***
**Consolidated Statements of Operations**

| | Year Ended September 30, | | |
|---|---|---|---|
| | 2016 | 2015 | 2014 |
| | (Dollars in thousands, except per share data) | | |
| | (As Restated – Note 3) | | |
| Interest and Dividend Income | | | |
| Loans, including fees | $21,206 | $16,484 | $17,736 |
| Investment securities, taxable | 2,824 | 3,073 | 2,109 |
| Investment securities, tax-exempt | 751 | 522 | 145 |
| Dividends, restricted stock | 250 | 311 | 123 |
| Interest-bearing cash accounts | 213 | 72 | 54 |
| Total Interest and Dividend Income | 25,244 | 20,462 | 20,167 |
| Interest Expense | | | |
| Deposits | 4,537 | 3,431 | 3,969 |
| Long-term borrowings | 2,195 | 1,817 | 1,102 |
| Total Interest Expense | 6,732 | 5,248 | 5,071 |
| Net Interest Income | 18,512 | 15,214 | 15,096 |
| Provision for Loan Losses | 947 | 90 | 263 |
| Net Interest Income after Provision for Loan Losses | 17,565 | 15,124 | 14,833 |
| | | | |
| Other Income | | | |
| Service charges and other fees | 923 | 989 | 947 |
| Rental income-other | 211 | 249 | 255 |
| Gain on sale of investments, net | 565 | 515 | 83 |
| Loss on disposal of fixed assets | 1 | — | (41) |
| Gain on sale of loans, net | 116 | 102 | 352 |
| Earnings on bank-owned life insurance | 517 | 680 | 559 |
| Total Other Income | 2,333 | 2,535 | 2,155 |
| Other Expense | | | |
| Salaries and employee benefits | 6,290 | 5,998 | 7,770 |
| Occupancy expense | 1,820 | 1,715 | 2,091 |
| Federal deposit insurance premium | 579 | 784 | 735 |
| Advertising | 131 | 239 | 561 |
| Data processing | 1,128 | 1,236 | 1,245 |
| Professional fees | 1,683 | 1,571 | 2,205 |
| Other real estate owned expense (income), net | 27 | (46) | (299) |
| Other operating expenses | 2,264 | 2,464 | 2,336 |
| Total Other Expenses | 13,922 | 13,961 | 16,644 |
| Income before income tax benefit | 5,976 | 3,698 | 344 |
| Income tax benefit | (6,174) | (970) | (367) |
| Net Income | $12,150 | $4,668 | $711 |
| | | | |
| Earnings Per Common Share: | | | |
| Basic | $1.90 | $0.73 | $0.11 |

| | | | |
|---|---|---|---|
| Diluted | $1.90 | n/a | n/a |
| Weighted Average Common Shares Outstanding | | | |
| Basic | 6,409,265 | 6,393,330 | 6,378,930 |
| Diluted | 6,409,325 | n/a | n/a |
| Dividends Declared Per Share | $0.00 | $0.00 | $0.00 |

*See notes to consolidated financial statements.*

*Malvern Bancorp, Inc. and Subsidiaries*

**Consolidated Statements of Comprehensive Income**

| | Year Ended September 30, | | |
|---|---|---|---|
| (In thousands) | 2016 | 2015 | 2014 |
| | (As Restated – Note 3) | | |
| Net Income | $12,150 | $4,668 | $711 |
| Other Comprehensive income, Net of Tax: | | | |
| Unrealized holding gains (losses) on available-for-sale securities | 2,128 | 2,120 | 1,419 |
| Tax effect | (723) | (721) | (482) |
| Net of tax amount | 1,405 | 1,399 | 937 |
| Reclassification adjustment for net gains arising during the period[1] | (565) | (515) | (83) |
| Tax effect | 192 | 175 | 29 |
| Net of tax amount | (373) | (340) | (54) |
| Accretion of unrealized holding losses on securities transferred from available-for-sale to held-to-maturity[2] | 9 | 5 | — |
| Tax effect | (3) | (2) | — |
| Net of tax amount | 6 | 3 | — |
| Fair value adjustment on derivatives | (194) | (348) | — |
| Tax effect | 172 | 12 | — |
| Net of tax amount | (22) | (336) | — |
| Total other comprehensive income | 1,016 | 726 | 883 |
| Total comprehensive income | $13,166 | $5,394 | $1,594 |

[1] Amounts are included in net gain on sales of securities on the Consolidated Statements of Operations in total other income.

[2] Amounts are included in interest and dividends on investment securities on the Consolidated Statements of Operations.

*See notes to consolidated financial statements.*

*Malvern Bancorp, Inc. and Subsidiaries*

**Consolidated Statements of Changes in Shareholders' Equity**

**Years Ended September 30, 2016, 2015, and 2014**

| | Common Stock | Additional Paid-In Capital | Retained Earnings | Unearned ESOP Shares | Accumulated Other Comprehensive Income (Loss) | Total Shareholders' Equity |
|---|---|---|---|---|---|---|
| | (in thousands, except share data) (As Restated – Note 3) | | | | | |
| Balance, October 1, 2013 | $66 | $ 60,302 | $19,793 | $(2,067) | $ (2,688) | $ 75,406 |
| Net Income | — | — | 711 | — | — | 711 |
| Other comprehensive income | — | — | — | — | 883 | 883 |
| Committed to be released ESOP shares (14,400 shares) | — | 15 | — | 145 | — | 160 |
| Balance, September 30, 2014 | $66 | $ 60,317 | $20,504 | $(1,922) | $ (1,805) | $ 77,160 |
| Net Income | — | — | 4,668 | — | — | 4,668 |
| Other comprehensive income | — | — | — | — | 726 | 726 |
| Committed to be released ESOP shares (14,400 shares) | — | 48 | — | 147 | — | 195 |
| Balance, September 30, 2015 | $66 | $ 60,365 | $25,172 | $(1,775) | $ (1,079) | $ 82,749 |
| Net Income | — | — | 12,150 | — | — | 12,150 |
| Other comprehensive income | — | — | — | — | 1,016 | 1,016 |
| Committed to be released ESOP shares (14,400 shares) | — | 96 | — | 146 | — | 242 |
| Balance, September 30, 2016 | $66 | $ 60,461 | $37,322 | $(1,629) | $ (63) | $ 96,157 |

*See notes to consolidated financial statements.*

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***Malvern Bancorp, Inc. and Subsidiaries***
**Consolidated Statements of Cash Flows**

| | Year Ended September 30, | | |
|---|---|---|---|
| | 2016 | 2015 | 2014 |
| | (In thousands) | | |
| | (As Restated – Note 3) | | |
| Cash Flows from Operating Activities | | | |
| Net income | $12,150 | $4,668 | $711 |
| Adjustments to reconcile net income to net cash provided by (used in) operating activities: | | | |
| Depreciation expense | 650 | 646 | 638 |
| Provision for loan losses | 947 | 90 | 263 |
| Deferred income taxes (benefit) expense | (6,316) | (1,035) | (367) |
| ESOP expense | 242 | 195 | 160 |
| Amortization (accretion) of premiums and discounts on investment securities, net | 1,243 | 849 | (488) |
| Amortization (accretion) of loan origination fees and costs | 748 | 296 | (193) |
| Amortization (accretion) of mortgage service rights | 73 | 82 | (22) |
| Net gain on sale of investment securities available for sale | (565) | (515) | (83) |
| Net (gain) loss on disposal of fixed assets | (1) | — | 41 |
| Net (gain) loss on sale of loans | — | — | (281) |
| Net gain on sale of secondary market loans | (116) | (102) | (71) |
| Proceeds on sale of secondary market loans | 6,390 | 4,090 | 7,738 |
| Originations of secondary market loans | (6,274) | (3,988) | (7,667) |
| Gain on sale of other real estate owned | (19) | (124) | (93) |
| Write down of other real estate owned | 20 | 54 | 341 |
| Earnings on bank-owned life insurance | (517) | (680) | (559) |
| (Increase) decrease in accrued interest receivable | (74) | (1,162) | 82 |
| Increase (decrease) in accrued interest payable | 31 | 247 | 10 |
| Increase (decrease) in other liabilities | 766 | 349 | (79) |
| Increase in other assets | (44) | (714) | (114) |
| Net Cash Provided by (Used in) by Operating Activities | 9,334 | 3,246 | (33) |
| Cash Flows from Investing Activities | | | |
| Investment securities available-for-sale: | | | |
| Purchases | (2,116) | (160,103) | (5,258) |
| Sales | 62,818 | 70,413 | 16,751 |
| Maturities, calls and principal repayments | 2,437 | 6,032 | 14,138 |
| Investment securities held-to-maturity: | | | |
| Purchases | — | (4,152) | — |
| Maturities, calls and principal repayments | 16,391 | 4,454 | — |
| Proceeds from sale of loans | — | — | 25,836 |
| Loan buyback for sale of loans | — | — | (1,117) |
| Loan purchases | — | — | (18,952) |
| (Loan originations) and principal collections, net | (184,548) | (5,927) | 19,649 |
| Proceeds from sale of other real estate owned | 1,167 | 1,174 | 2,694 |
| Additions to mortgage servicing rights | — | (30) | (160) |
| Proceeds from cash surrender on bank-owned life insurance | — | — | 3,636 |
| Proceeds from death benefit of bank-owned life insurance | 1,049 | — | — |
| Net (increase) decrease in restricted stock | (659) | (1,262) | (465) |

| | | | |
|---|---|---|---|
| Proceeds from sale of property and equipment | 1 | — | — |
| Purchases of property and equipment | (752 ) | (358 ) | (244 ) |
| Net Cash (Used in) Provided by Investing Activities | (104,212) | (89,759 ) | 56,508 |
| Cash Flows from Financing Activities | | | |
| Net increase (decrease) in deposits | 136,524 | 52,569 | (71,643) |
| Proceeds for long-term borrowings | 121,000 | 93,000 | 14,500 |
| Repayment of long-term borrowings | (106,000) | (38,000 ) | (4,500 ) |
| Increase in advances from borrowers for taxes and insurance | (147 ) | 20 | 668 |
| Net Cash Provided by (Used in) Financing Activities | 151,377 | 107,589 | (60,975) |
| Net Increase (Decrease) in Cash and Cash Equivalents | 56,499 | 21,076 | (4,500 ) |
| Cash and Cash Equivalent - Beginning | 40,263 | 19,187 | 23,687 |
| Cash and Cash Equivalent - Ending | $96,762 | $40,263 | $19,187 |
| | | | |
| Supplementary Cash Flows Information | | | |
| Interest paid | $6,701 | $5,001 | $5,061 |
| Income taxes paid | $— | $— | $17 |
| Non-cash transfer of loans to other real estate owned | $— | $308 | $944 |
| Transfer from investment securities available-for-sale to investment securities held-to-maturity | $— | $57,523 | $— |
| Non-cash proceeds from death benefit on BOLI | $— | $1,039 | $— |

*See notes to consolidated financial statements.*

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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 1 – Organizational Structure and Nature of Operations**

On May 19, 2008, Malvern Federal Savings Bank ("Malvern Federal Savings" or the "Bank") completed its reorganization to the mutual holding company form of organization and formed Malvern Federal Bancorp, Inc. (the "Mid-Tier Holding Company") to serve as the "mid-tier" stock holding company for the Bank. An Employee Stock Ownership Plan ("ESOP") was established which borrowed approximately $2.6 million from Malvern Federal Bancorp, Inc. to purchase 241,178 shares of common stock. Principal and interest payments of the loan are being made quarterly over a term of 18 years at a fixed interest rate of 5.0%.

On October 11, 2012, Malvern Bancorp, Inc. (the "Company" or "Malvern Bancorp") completed the "second-step" conversion from the mutual holding company structure to the stock holding company structure pursuant to a Plan of Conversion and Reorganization. Upon completion of the conversion and reorganization, Malvern Federal Mutual Holding Company (the "Mutual Holding Company") and the Mid-Tier Holding Company ceased to exist. Malvern Bancorp, Inc., a Pennsylvania company, became the holding company for the Bank and owns all of the issued and outstanding shares of the common stock of Malvern Federal Savings Bank. In connection with the conversion and reorganization, 3,636,875 shares of common stock, par value $0.01 per share, of Malvern Bancorp, Inc., were sold in a subscription offering to certain depositors of the Bank and other investors for $10 per share, or $36.4 million in the aggregate, and 2,921,598 shares of common stock were issued in exchange for the outstanding shares of common stock of the former federally chartered Mid-Tier Holding Company held by the "public" shareholders of the Mid-Tier Holding Company (all shareholders except Malvern Federal Mutual Holding Company). Each share of common stock of the Mid-Tier Holding Company was converted into the right to receive 1.0748 shares of common stock of the new Malvern Bancorp, Inc. in the conversion and reorganization. The total shares outstanding upon completion of the stock offering and the exchange were approximately 6,558,473.

The Company is a Pennsylvania chartered corporation which, since October 11, 2012, has owned all of the issued and outstanding shares of the Bank's common stock, the only shares of equity securities which the Bank has issued. The Company does not own or lease any property, but instead uses the premises, equipment and furniture of the Bank. At the present time, the Company employs only persons who are officers of Malvern Federal Savings to serve as officers of the Company. The Company also uses the Bank's support staff from time to time. These persons are not separately compensated by Company.

Malvern Federal Savings Bank is a federally chartered, FDIC-insured savings bank that was originally organized in 1887. The Bank conducts business from its headquarters in Paoli, Pennsylvania, a suburb of Philadelphia, as well as eight full service financial center offices in Chester and Delaware Counties, Pennsylvania and a Private Banking Loan Production headquarters office in Morristown, New Jersey. The Bank is primarily engaged in attracting deposits from the general public and using those funds to invest in loans and investment securities. The Bank's principal sources of funds are deposits, repayments of loans and investment securities, maturities of investments and interest-bearing deposits, other funds provided from operations and wholesale funds borrowed from outside sources such as the Federal Home Loan Bank of Pittsburgh (the "FHLB"). These funds are primarily used for the origination of various loan types including single-family residential mortgage loans, commercial real estate mortgage loans, construction and development loans, home equity loans and lines of credit and other consumer loans. The Bank derives its income principally from interest earned on loans, investment securities and, to a lesser extent, from fees received in connection with the origination of loans and for other services. Malvern Federal Savings' primary expenses are interest expense on deposits and borrowings and general operating expenses. Funds for activities are provided primarily by deposits, amortization of loans, loan prepayments and the maturity of loans, securities and other investments and other funds from operations.

The banking industry is highly regulated. The Bank is supervised by the Office of the Comptroller of the Currency (the "OCC") and the Company is supervised by the Board of Governors of the Federal Reserve System (the "Federal Reserve Board" or the "FRB").

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 1 – Organizational Structure and Nature of Operations (Continued)**

The Company and the Bank and the Bank's subsidiary, Strategic Asset Management Group, Inc. ("SAMG"), provide various banking services, primarily accepting deposits and originating residential and commercial mortgage loans, consumer loans and other loans through the Bank's headquarters and eight full-service branches in Chester and Delaware Counties, Pennsylvania. SAMG owns 50% of Malvern Insurance Associates, LLC. Malvern Insurance Associates, LLC offers a full line of business and personal lines of insurance products. As of September 30, 2016 and 2015, SAMG's total assets were approximately \$62,000 and \$68,000, respectively. The net loss of SAMG for the year ended September 30, 2016, was approximately \$6,000 and for the years ended September 30, 2015 and 2014, the net income was approximately \$2,000 and \$5,000, respectively. The Company is subject to competition from various other financial institutions and financial services companies. The Company is also subject to the regulations of certain federal agencies and, therefore, undergoes periodic examinations by those regulatory agencies.

In accordance with the subsequent events topic of the Financial Accounting Standards Board ("FASB") Accounting Standards Codification (the "Codification" or the "ASC"), the Company evaluates events and transactions that occur after the statement of financial condition date for potential recognition and disclosure in the consolidated financial statements. The effect of all subsequent events that provide additional evidence of conditions that existed at the statement of financial condition date are recognized in the audited consolidated financial statements as of September 30, 2016.

**Note 2 – Summary of Significant Accounting Policies**

***Basis of Presentation and Consolidation***

The consolidated financial statements at and for the years ended September 30, 2016, 2015 and 2014 include the accounts of Malvern Bancorp, Inc. and its subsidiaries. All significant intercompany transactions and balances have been eliminated.

***Use of Estimates***

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of income and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses and the valuation of deferred tax assets.

***Significant Group Concentrations of Credit Risk***

Most of the Company's activities are with customers located within Chester County, Pennsylvania. In addition to Chester County, our lending efforts are focused in neighboring Bucks County, Montgomery County and Delaware County, which are also in southeastern Pennsylvania, New Jersey and the New York metropolitan marketplace. Note 5 discusses the types of investment securities that the Company invests in. Note 6 discusses the types of lending that the Company engages in. The Company does not have any significant concentrations to any one

industry or customer. Although the Company has a diversified portfolio, its debtors ability to honor their contracts is influenced by, among other factors, the region's economy.

***Cash and Cash Equivalents***

For purposes of reporting cash flows, cash and cash equivalents include cash on hand, amounts due from depository institutions and interest bearing deposits.

The Company maintains cash deposits in other depository institutions that occasionally exceed the amount of deposit insurance available. Management periodically assesses the financial condition of these institutions and believes that the risk of any possible credit loss is minimal.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 2 - Summary of Significant Accounting Policies (Continued)**

The Company is required to maintain average reserve balances in vault cash with the Federal Reserve Bank based upon outstanding balances of deposit transaction accounts. Based upon the Company's outstanding transaction deposit balances, the Bank maintained a deposit account with the Federal Reserve Bank of Philadelphia in the amount of $4.8 million and $3.7 million at September 30, 2016 and 2015, respectively.

***Investment Securities***

Held-to-maturity ("HTM") are securities that includes debt securities that the Company has the positive intent and the ability to hold to maturity. These securities are reported at amortized cost and adjusted for unamortized premiums and discounts. Securities held for trading are securities that are bought and held principally for the purpose of selling in the near term; these securities are reported at fair value, with unrealized gains and losses reported in current earnings. At September 30, 2016 and 2015, the Company had no investment securities classified as trading. Debt securities that will be held for indefinite periods of time and equity securities, including securities that may be sold in response to changes in market interest or prepayment rates, needs for liquidity and changes in the availability of and the yield of alternative investments, are classified as available for sale. Realized gains and losses are recorded on the trade date and are determined using the specific identification method. Securities held as available for sale are reported at fair value, with unrealized gains and losses, net of tax, reported as a component of accumulated other comprehensive income ("AOCI"). Management determines the appropriate classification of investment securities at the time of purchase.

Securities are evaluated on a quarterly basis, and more frequently when market conditions warrant such an evaluation, to determine whether declines in their value are other-than-temporary. To determine whether a loss in value is other-than-temporary, management utilizes criteria such as the reasons underlying the decline, the magnitude and duration of the decline and whether or not management intends to sell or expects that it is more likely than not that it will be required to sell the security prior to an anticipated recovery of the fair value. The term "other-than-temporary" is not intended to indicate that the decline is permanent, but indicates that the prospects 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 for a debt security is determined to be other-than-temporary, the other-than-temporary impairment is separated into (a) the amount of the total other-than-temporary impairment related to a decrease in cash flows expected to be collected from the debt security (the credit loss) and (b) the amount of the total other-than-temporary impairment related to all other factors. The amount of the total other-than-temporary impairment related to the credit loss is recognized in earnings. The amount of the total other-than-temporary impairment related to all other factors is recognized in other comprehensive income.

***Loans Receivable***

The Company, through the Bank, grants mortgage, construction, commercial and consumer loans to customers. Substantially all of our loans are to individuals, businesses and real estate developers in Chester County, Pennsylvania and neighboring areas in southern Pennsylvania, New Jersey and the New York metropolitan marketplace. The ability of the Company's debtors to honor their contracts is dependent upon, among other factors, the real estate and general economic conditions in this area.

Loans receivable that management has the intent and ability to hold until maturity or payoff are stated at their outstanding unpaid principal balances, net of an allowance for loan losses and any deferred fees and costs. Interest income is accrued on the unpaid principal balance. Loan origination fees and costs are deferred and recognized as an adjustment of the yield (interest income) of the related loans using the interest method. The Company is amortizing these amounts over the contractual lives of the loans.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 2 - Summary of Significant Accounting Policies (Continued)**

The loans receivable portfolio is segmented into residential loans, construction and development loans, commercial loans and consumer loans. The residential loan segment has one class, one- to four-family first lien residential mortgage loans. The construction and development loan segment consists of the following classes: residential and commercial and land loans. Residential construction loans are made for the acquisition of and/or construction on a lot or lots on which a residential dwelling is to be built. Commercial construction loans are made for the purpose of acquiring, developing and constructing a commercial structure. The commercial loan segment consists of the following classes: commercial real estate loans, multi-family real estate loans, and other commercial loans, which are also generally known as commercial and industrial loans or commercial business loans. The consumer loan segment consists of the following classes: home equity lines of credit, second mortgage loans and other consumer loans, primarily unsecured consumer lines of credit.

For all classes of loans receivable, the accrual of interest is discontinued when the contractual payment of principal or interest has become 90 days past due or management has serious doubts about further collection of principal or interest, even though the loan is currently performing. A loan may remain on accrual status if it is in the process of collection and is either guaranteed or well secured. When a loan is placed on nonaccrual status, unpaid interest credited to income in the current year is reversed and unpaid interest accrued in prior years is charged against the allowance for loan losses. Interest received on nonaccrual loans, including impaired loans, generally is either applied against principal or reported as interest income, according to management's judgment as to the collectability of principal. Generally, loans are restored to accrual status when the obligation is brought current, has performed in accordance with the contractual terms for a reasonable period of time (generally six months) and the ultimate collectability of the total contractual principal and interest is no longer in doubt. The past due status of all classes of loans receivable is determined based on contractual due dates for loan payments.

In addition to originating loans, the Company purchases consumer and mortgage loans from brokers in our market area. Such purchases are reviewed for compliance with our underwriting criteria before they are purchased, and are generally purchased without recourse to the seller. Premiums and discounts on purchased loans are amortized as adjustments to interest income using the effective yield method.

***Allowance for Loan Losses***

The allowance for credit losses consists of the allowance for loan losses and the reserve for unfunded lending commitments. The allowance for loan losses represents management's estimate of losses inherent in the loan portfolio as of the consolidated statement of financial condition date and is recorded as a reduction to loans. Reserves for unfunded lending commitments represent management's estimate of losses inherent in its unfunded loan commitments and is recorded in other liabilities on the consolidated statement of financial condition. The allowance for loan losses

(“ALLL”) is increased by the provision for loan losses and decreased by charge-offs, net of recoveries. Loans deemed to be uncollectible are charged against the allowance for loan losses, and subsequent recoveries, if any, are credited to the allowance. All, or part, of the principal balance of loans receivable are charged off to the allowance as soon as it is determined that the repayment or collateral recovery of all, or part, of the principal balance is highly unlikely. Non-residential consumer loans are generally charged off no later than when they become 120 days past due on a contractual basis or earlier in the event of the borrower’s bankruptcy or if there is an amount deemed uncollectible. Because all identified losses are immediately charged off, no portion of the allowance for loan losses is restricted to any individual loan or groups of loans, and the entire allowance is available to absorb any and all loan losses.

The allowance for credit losses is maintained at a level considered adequate to provide for losses that can be reasonably estimated. Management performs a quarterly evaluation of the adequacy of the allowance. The allowance is based on the Company’s past loan loss experience, known and inherent risks in the portfolio, adverse situations that may affect the borrower’s ability to repay, the estimated value of any underlying collateral, the 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 revision as more information becomes available.

The allowance consists of specific, general and unallocated components. The specific component relates to loans that are classified as impaired. For loans that are classified as impaired, a charge-off is recognized 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 pools of loans by loan class that are not considered impaired.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 2 - Summary of Significant Accounting Policies (Continued)**

These pools of loans are evaluated for loss exposure based upon historical loss rates for each of these classes of loans, as adjusted for qualitative factors. These qualitative risk factors include:

1. Lending policies and procedures, including underwriting standards and collection, charge-off, and recovery practices.
2. National, regional, and local economic and business conditions as well as the condition of various market segments, including the value of underlying collateral for collateral dependent loans.
3. The nature and volume of the loan portfolio and terms of loans.
4. The experience, ability, and depth of lending management and staff.
5. The volume and severity of past due, classified and nonaccrual loans as well as any other loan modifications.
6. The quality of the Company's loan review system, and the degree of oversight by the Company's Board of Directors.
7. The existence and effect of any concentrations of credit and changes in the level of such concentrations.
8. Value of underlying collateral.

The qualitative factors are applied to the historical loss rates for each class of loan. In addition, while not reported as a separate factor, changes in the value of underlying collateral (for regional property values) for collateral dependent loans is considered and addressed within the economic trends factor. A quarterly calculation is made adjusting the reserve allocation for each factor within a risk weighted range as it relates to each particular loan type, collateral type and risk rating within each segment. Data is gathered and evaluated through internal, regulatory, and government sources quarterly for each factor.

An unallocated component is maintained to cover uncertainties that could affect management's estimate of probable losses. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general losses in the portfolio.

In addition, the allowance calculation methodology includes further segregation of loan classes into risk rating categories. The borrower's overall financial condition, repayment sources, guarantors and value of collateral, if appropriate, are evaluated annually for commercial loans or when credit deficiencies arise, such as delinquent loan payments, for commercial and consumer loans. Credit quality risk ratings include categories of "pass," "special mention," "substandard" and "doubtful." Assets classified as "Pass" are those protected by the current net worth and paying capacity of the obligor or by the value of the underlying collateral. Assets which do not currently expose the insured institution to sufficient risk to warrant classification as substandard or doubtful but possess certain identified weaknesses are required to be designated "special mention." If uncorrected, the potential weaknesses may result in deterioration of the repayment prospects. An asset is considered "substandard" if it is inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. “Substandard” assets include those characterized by the “distinct possibility” that the insured institution will sustain “some loss” if the deficiencies are not corrected. Assets classified as “doubtful” have all of the weaknesses inherent in those classified “substandard” with the added characteristic that the weaknesses present make “collection or liquidation in full,” on the basis of currently existing facts, conditions, and values, “highly questionable and improbable.”

*Residential Lending.* Residential mortgage originations are secured primarily by properties located in the Company’s primary market area and surrounding areas. We currently originate fixed-rate, fully amortizing mortgage loans with maturities of 10 to 30 years. We also offer adjustable rate mortgage (“ARM”) loans where the interest rate either adjusts on an annual basis or is fixed for the initial one, three or seven years and then adjusts annually.

We underwrite one- to four-family residential mortgage loans with loan-to-value ratios of up to 95%, provided that the borrower obtains private mortgage insurance on loans that exceed 80% of the appraised value or sales price, whichever is less, of the secured property. We also require that title insurance, hazard insurance and, if appropriate, flood insurance be maintained on all properties securing real estate loans. We require that a licensed appraiser from our list of approved appraisers perform and submit to us an appraisal on all properties secured by a first mortgage on one- to four-family first mortgage loans.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 2 - Summary of Significant Accounting Policies (Continued)**

In underwriting one- to four-family residential mortgage loans, the Company evaluates both the borrower's ability to make monthly payments and the value of the property securing the loan. Most properties securing real estate loans made by the Company are appraised by independent fee appraisers approved by the Board of Directors. The Company generally requires borrowers to obtain an attorney's title opinion or title insurance, and fire and property insurance (including flood insurance, if necessary) in an amount not less than the amount of the loan. Real estate loans originated by the Company generally contain a "due on sale" clause allowing the Company to declare the unpaid principal balance due and payable upon the sale of the security property. The Company has not engaged in sub-prime residential mortgage loan originations. Our single-family residential mortgage loans generally are underwritten on terms and documentation conforming to guidelines issued by Freddie Mac and Fannie Mae.

*Construction and Development Lending.* We originate construction loans for residential and, to a lesser extent, commercial uses within our market area. We generally limit construction loans to builders and developers with whom we have an established relationship, or who are otherwise known to officers of the Bank. Our construction and development loans currently in the portfolio typically have variable rates of interest tied to the prime rate which improves the interest rate sensitivity of our loan portfolio.

Construction and development loans generally are considered to involve a higher level of risk than one-to four-family residential lending, due to the concentration of principal in a limited number of loans and borrowers and the effect of economic conditions on developers, builders and projects. Additional risk is also associated with construction lending because of the inherent difficulty in estimating both a property's value at completion and the estimated cost (including interest) to complete a project. The nature of these loans is such that they are more difficult to evaluate and monitor. In addition, speculative construction loans to a builder are not pre-sold and thus pose a greater potential risk than construction loans to individuals on their personal residences. In order to mitigate some of the risks inherent in construction lending, we inspect properties under construction, review construction progress prior to advancing funds, work with builders with whom we have established relationships, require annual updating of tax returns and other financial data of developers and obtain personal guarantees from the principals.

*Commercial Lending.* Commercial and multi-family real estate loans generally present a higher level of risk than loans secured by one- to four-family residences. This greater risk is due to several factors, including the concentration of principal in a limited number of loans and borrowers, the effect of general economic conditions on income producing properties and the increased difficulty of evaluating and monitoring these types of loans. Furthermore, the repayment of loans secured by commercial and multi-family real estate is typically dependent upon the successful operation of the related real estate project. If the cash flow from the project is reduced (for example, if leases are not obtained or renewed, or a bankruptcy court modifies a lease term, or a major tenant is unable to fulfill its lease obligations), the borrower's ability to repay the loan may be impaired.

Most of the Company's commercial business loans have been extended to finance local and regional businesses and include short-term loans to finance machinery and equipment purchases, inventory and accounts receivable. The commercial business loans which we originate may be either a revolving line of credit or for a fixed term of generally 10 years or less. Interest rates are adjustable, indexed to a published prime rate of interest, or fixed. Generally, equipment, machinery, real property or other corporate assets secure such loans. Personal guarantees from the business principals are generally obtained as additional collateral.

*Consumer Lending.* The Company currently originates most of its consumer loans in its primary market area and surrounding areas. The Company originates consumer loans on both a direct and indirect basis. Consumer loans generally have higher interest rates and shorter terms than residential mortgage loans; however, they have additional credit risk due to the type of collateral securing the loan or in some case the absence of collateral. As a result of the declines in the market value of real estate and the deterioration in the overall economy, we are continuing to evaluate and monitor the credit conditions of our consumer loan borrowers and the real estate values of the properties securing our second mortgage loans as part of our on-going efforts to assess the overall credit quality of the portfolio in connection with our review of the allowance for loan losses.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 2 - Summary of Significant Accounting Policies (Continued)**

Consumer loans may entail greater credit risk than do residential mortgage loans, particularly in the case of consumer loans which are unsecured or are secured by rapidly depreciable assets, such as automobiles or recreational equipment. In such cases, any repossessed collateral for a defaulted consumer loan may not provide an adequate source of repayment of the outstanding loan balance as a result of the greater likelihood of damage, loss or depreciation. In addition, consumer loan collections are dependent on the borrower's continuing financial stability, and thus are more likely to be affected by adverse personal circumstances. Furthermore, the application of various federal and state laws, including bankruptcy and insolvency laws, may limit the amount which can be recovered on such loans.

Once all factor adjustments are applied, general reserve allocations for each segment are calculated, summarized and reported on the ALLL summary. ALLL final schedules, calculations and the resulting evaluation process are reviewed quarterly.

In addition, Federal bank regulatory agencies, as an integral part of their examination process, periodically review the Company's allowance for loan losses and may require the Company to recognize additions to the allowance based on their judgments about information available to them at the time of their examination. Based on management's comprehensive analysis of the loan portfolio, management believes the current level of the allowance for loan losses is adequate.

A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record and the amount of the shortfall in relation to the principal and interest owed.

An allowance for loan losses is established for an impaired loan if its carrying value exceeds its estimated fair value. The estimated fair values of substantially all of the Company's impaired loans are measured based on the estimated fair value of the loan's collateral.

For commercial loans secured by real estate, estimated fair values are determined primarily through third-party appraisals. When a real estate secured loan becomes impaired, a decision is made regarding whether an updated appraisal of the real estate is necessary. This decision is based on various considerations, including the age of the most recent appraisal, the loan-to-value ratio based on the original appraisal and the condition of the property. Appraised values are discounted to arrive at the estimated selling price of the collateral, which is considered to be the estimated fair value. The discounts also include estimated costs to sell the property.

For commercial and industrial loans secured by non-real estate collateral, such as accounts receivable, inventory and equipment, estimated fair values are determined based on the borrower's financial statements, inventory reports, accounts receivable aging or equipment appraisals or invoices. Indications of value from these sources are generally discounted based on the age of the financial information or the quality of the assets.

***Troubled Debt Restructurings***

Loans whose terms are modified are classified as troubled debt restructurings if the Company grants such borrowers concessions and it is deemed that those borrowers are experiencing financial difficulty. Concessions granted under a troubled debt restructuring may be modified by means of extending the maturity date of the loan, reducing the interest rate on the loan to a rate which is below market, a combination of rate adjustments and maturity extensions, or by other means including covenant modifications, forbearances or other concessions. However, the Company generally only restructures loans by modifying the payment structure to interest only or by reducing the actual interest rate.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 2 - Summary of Significant Accounting Policies (Continued)**

We do not accrue interest on loans that were non-accrual prior to the troubled debt restructuring until they have performed in accordance with their restructured terms for a period of at least six months. We continue to accrue interest on troubled debt restructurings which were performing in accordance with their terms prior to the restructure and continue to perform in accordance with their restructured terms. Management evaluates the ALLL with respect to TDRs under the same policy and guidelines as all other performing loans are evaluated with respect to the ALLL.

***Loan Servicing***

Servicing assets are recognized as separate assets when rights are acquired through purchase or through sale of financial assets. For sales of mortgage loans, a portion of the cost of originating the loan is allocated to the servicing right based on relative fair value. Fair value is based on market prices for comparable mortgage servicing contracts, when available, or alternatively is based on a valuation model that calculates the present value of estimated future net servicing income. The valuation model incorporates assumptions that market participants would use in estimating future net servicing income, such as the cost to service, the discount rate, the custodial earnings rate, an inflation rate, ancillary income, prepayment speeds and default rates and losses. Capitalized servicing rights are reported in other assets and are amortized into other expense in proportion to, and over the period of, the estimated future net servicing income of the underlying financial assets.

Servicing assets are evaluated for impairment based upon the fair value of the rights as compared to amortized cost. Impairment is determined by stratifying rights into tranches based on predominant risk characteristics, such as interest rate, loan type and investor type. Impairment is recognized through a valuation allowance for an individual tranche, to the extent that fair value is less than the capitalized amount for the tranche. If the Company later determines that all or a portion of the impairment no longer exists for a particular tranche, a reduction of the allowance may be recorded as an increase to income. The Company also sells loans in the secondary market with serving released.

***Other Real Estate Owned***

Assets acquired through, or in lieu of, loan foreclosure are held for sale and are initially recorded at fair value at the date of foreclosure, establishing a new cost basis. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of the previously established carrying amount or fair value less cost to sell. Revenue and expenses from operations and changes in the valuation allowance are included in other expenses from other real estate owned.

***Restricted Stock***

Restricted stock represents required investments in the common stock of a correspondent bank and is carried at cost. As of September 30, 2016, restricted stock consists of the common stock of the Federal Home Loan Bank of Pittsburgh (“FHLB”) and Atlantic Community Bankers Bank (“ACBB”). As of September 30, 2015, restricted stock consists solely of the common stock of the Federal Home Loan Bank of Pittsburgh (“FHLB”).

Management’s evaluation and determination of whether these investments are impaired is based on their assessment of the ultimate recoverability of their cost rather than by recognizing temporary declines in value. The determination of whether a decline affects the ultimate recoverability of an investment’s cost is influenced by criteria such as (1) the significance of the decline in net assets of the FHLB as compared to the capital stock amount for the FHLB and the length of time this situation has persisted, (2) commitments by the FHLB to make payments required by law or regulation and the level of such payments in relation to the operating performance of the FHLB, and (3) the impact of legislative and regulatory changes on institutions and, accordingly, on the customer base of the FHLB.

During the years ended September 30, 2016 and 2015, there were net repurchases of restricted stock of $659,000 and $1.3 million, respectively. Also as of September 30, 2016 and 2015 the number of FHLB shares was 53,441 and 47,651, respectively. There were approximately $250,000, $311,000 and $123,000 of dividends on FHLB stock received or recognized in income for fiscal years 2016, 2015 and 2014, respectively.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 2 - Summary of Significant Accounting Policies (Continued)**

***Property and Equipment***

Property and equipment is carried at cost. Depreciation is computed using the straight-line and accelerated methods over estimated useful lives ranging from 3 to 39 years beginning when assets are placed in service. When assets are retired or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts and any gain or loss is reflected in income for the period. The cost of maintenance and repairs is charged to income as incurred.

***Transfers of Financial Assets***

Transfers of financial assets are accounted for as sales when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the Company, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and (3) the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

***Bank-Owned Life Insurance***

The Company invests in bank owned life insurance (“BOLI”) as a source of funding for employee benefit expenses. BOLI involves the purchasing of life insurance by the Bank on a chosen group of employees. The Bank is the owner and beneficiary of the policies. This life insurance investment is carried at the cash surrender value of the underlying policies. Earnings from the increase in cash surrender value of the policies are included in other income on the statement of operations.

***Employee Benefit Plans***

The Bank’s 401(k) plan allows eligible participants to set aside a certain percentage of their salaries before taxes. The Company may elect to match employee contributions up to a specified percentage of their respective salaries in an amount determined annually by the Board of Directors. The Company’s matching contribution related to the plan resulted in expenses of $90,000, $64,000, and $118,000, for fiscal 2016, 2015, and 2014, respectively. There were no bonus matching contributions for fiscal years 2016, 2015 or 2014.

The Company also maintains an unfunded Supplemental Executive and a Director Retirement Plan (the “Plans”). The accrued amount for the Plans included in other liabilities was $1.1 million and $1.2 million at September 30, 2016 and 2015, respectively. Distributions made to directors for the fiscal year 2016 and 2015 were approximately $4,000 and $13,000, respectively. The (benefit)/expense associated with the Plans for the years ended September 30, 2016, 2015, and 2014 was $11,000, ($24,000), and $78,000, respectively. At fiscal 2015, the benefit associated with the Plans was due to the Plan being frozen at September 30, 2014 and the Company had to credit fiscal 2015 accruals for the first quarter of fiscal 2015.

***Derivatives and Hedging***

The Company records cash flow hedges at the inception of the derivative contract based on the Company’s intentions and belief as to likely effectiveness as a hedge. The Company documents the strategy for entering into the transactions and the method of assessing ongoing effectiveness. Cash flow hedges represent a hedge of a forecasted transaction or the variability of cash flows to be received or paid related to a recognized asset or liability. For a cash flow hedge, the gain or loss on the derivative is reported in other comprehensive income and is reclassified into earnings in the same periods during which the hedged transaction affects earnings. The changes in the fair value of derivatives that are not highly effective in hedging the changes in fair value or expected cash flows of the hedged item are recognized immediately in current earnings. Changes in the fair value of derivatives that do not qualify for hedge accounting are reported currently in earnings, as noninterest income.

Net cash settlements on derivatives that qualify for hedge accounting are recorded in interest income or interest expense, based on the item being hedged. Net cash settlements on derivatives that do not qualify for hedge accounting are reported in noninterest income. Cash flows on hedges are classified in the cash flow statement the same as the cash flows of the items being hedged. To determine fair value, the Company uses third party pricing models that incorporate assumptions about market conditions and risks that are current at the reporting date. The Company does not use derivative instruments for speculative purposes.

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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 2 - Summary of Significant Accounting Policies (Continued)**

The Company also formally assesses, both at the hedge's inception and on an ongoing basis, whether the derivative instruments that are used are highly effective in offsetting changes in fair values or cash flows of the hedged items. The Company discontinues hedge accounting when it determines that the derivative is no longer effective in offsetting changes in the fair value or cash flows of the hedged item, the derivative is settled or terminates, a hedged forecasted transaction is no longer probable, a hedged firm commitment is no longer firm, or treatment of the derivative as a hedge is no longer appropriate or intended.

When hedge accounting is discontinued, subsequent changes in fair value of the derivative are recorded as noninterest income. When a cash flow hedge is discontinued but the hedged cash flows or forecasted transactions are still expected to occur, gains or losses that were accumulated in other comprehensive income are amortized into earnings over the same periods which the hedged transactions will affect earnings.

***Advertising Costs***

The Company follows the policy of charging the costs of advertising to expense as incurred.

***Income Taxes***

Deferred tax assets and liabilities are recognized for the future tax consequences attributable to temporary differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax basis. 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. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. These calculations are based on many complex factors including estimates of the timing of reversals of temporary differences, the interpretation of federal income tax laws and a determination of the differences between the tax and the financial reporting basis of assets and liabilities. Actual results could differ significantly from the estimates and

interpretations used in determining the current and deferred income tax assets and liabilities.

A valuation allowance is required to be recognized if it is "more likely than not" that a portion of the deferred tax assets will not be realized. The Company's policy is to evaluate the deferred tax asset on a quarterly basis and record a valuation allowance for our deferred tax asset if we do not have sufficient positive evidence indicating that it is more likely than not that some or all of the deferred tax asset will be realized. The Company's policy is to account for interest and penalties as components of income tax expense.

***Commitments and Contingencies***

In the ordinary course of business, the Company has entered into off-balance sheet financial instruments consisting of commitments to extend credit and standby letters of credit. Such financial instruments are recorded in the statement of financial condition when they are funded.

***Segment Information***

The Company has one reportable segment, "Community Banking." All of the Company's activities are interrelated, and each activity is dependent and assessed based on how each of the activities of the Company supports the others. For example, lending is dependent upon the ability of the Company to fund itself with deposits and other borrowings and manage interest rate and credit risk. Accordingly, all significant operating decisions are based upon analysis of the Company as one segment or unit.

***Comprehensive Income***

Accounting principles generally require that recognized revenue, expenses, gains and losses be included in net income. Although certain changes in assets and liabilities, such as unrealized gains and losses on available for sale investment securities, are reported as a separate component of the shareholders' equity section of the statement of financial condition, such items, along with net income, are components of comprehensive income.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 2 - Summary of Significant Accounting Policies (Continued)**

For securities transferred from available for sale to held to maturity, the Company records the amortization and/or accretion of unrealized holding losses on such investment securities, in accumulated other comprehensive income.

The Company also records changes in the fair value of interest rate derivatives used in its cash flow hedging activities, net of deferred income tax, in accumulated other comprehensive income.

***Reclassifications***

Certain reclassifications have been made to the previous years' consolidated financial statements to conform to the current year's presentation. These reclassifications had no effect on the Company's results of operations.

***Recent Accounting Pronouncements***

In October 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2016-16, "Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other Than Inventory". The ASU requires an entity to recognize the income tax consequences of intra-entity transfers of assets other than inventory at the time that the transfer occurs. Current guidance does not require recognition of tax consequences until the asset is eventually sold to a third party. ASU 2016-16 is effective for fiscal years, and interim periods within, beginning after December 15, 2017, with early adoption permitted as of the first interim period presented in a year. The Company does not expect the adoption of this guidance to have a material impact on its consolidated financial statements.

In August 2016, the FASB issued ASU No. 2016-15, "Statement of Cash Flows (Topic 230)". The ASU is intended to reduce the diversity in practice around how certain transactions are classified within the statement of cash flows. For public companies, this update will be effective for interim and annual periods beginning after December 15, 2017. The Company does not expect the adoption of this guidance to have a material impact on its consolidated financial statements.

In June 2016, the FASB issued ASU No. 2016-13, "Financial Instruments-Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments." The ASU requires an organization to measure all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts. Financial institutions and other organizations will now use forward-looking information to better inform their credit loss estimates. Many of the loss estimation techniques applied today will still be permitted, although the inputs to those techniques will change to reflect the full amount of expected credit losses. Organizations will continue to use judgment to determine which loss estimation method is appropriate for their circumstances. Additionally, the ASU amends the accounting for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. For public companies, this update will be effective for interim and annual periods beginning after December 15, 2019. The Company has not yet determined the impact the adoption of ASU 2016-13 will have on the consolidated financial statements and related disclosures.

In May 2016, the FASB issued ASU No. 2016-12 “Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients.” The guidance is intended to clarify the guidance previously issued in May 2014 related to the recognition of revenue from contracts with customers. The updated guidance includes narrow-scope improvements intended to address implementation issues and to provide additional practical expedients in the guidance. The updated guidance is effective for interim and annual reporting periods beginning after December 15, 2017, with early adoption permitted for interim and annual reporting periods beginning after December 15, 2016. The Company does not expect the adoption of this guidance to have a material impact on its consolidated financial statements.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 2 - Summary of Significant Accounting Policies (Continued)**

In April 2016, the FASB issued ASU No. 2016-10 “Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing.” The guidance is intended to clarify the guidance previously issued in May 2014 related to the recognition of revenue from contracts with customers. The updated guidance is intended to reduce the cost and complexity of applying the guidance on identifying promised goods or services in a contract and to improve the operability and understandability of the implementation guidance regarding the licensing of intellectual property. The updated guidance is effective for interim and annual reporting periods beginning after December 15, 2017, with early adoption permitted for interim and annual reporting periods beginning after December 15, 2016. The Company does not expect the adoption of this guidance to have a material impact on its consolidated financial statements.

In March 2016, the FASB issued ASU No. 2016-09, “Compensation - Stock Compensation (Topic 718): Improvements to Employee share-Based Payment Accounting.” The new guidance simplifies certain aspects related to income taxes, statement of cash flows, and forfeitures when accounting for share-based payment transactions. This new guidance will be effective for the Company for the first reporting period beginning after December 15, 2016, with earlier adoption permitted. Certain of the amendments related to timing of the recognition of tax benefits and tax withholding requirements should be applied using a modified retrospective transition method. Amendments related to the presentation of the statement of cash flows should be applied retrospectively. All other provisions may be applied on a prospective or modified retrospective basis. The Company does not expect the adoption of this guidance to have a material impact on its consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02, “Leases (Topic 842).” The guidance in this update supersedes the current lease accounting guidance for both the lessees and lessors under ASC 840, Leases. The new guidance requires lessees to evaluate whether a lease is a finance lease using criteria that are similar to what lessees use today to determine whether they have a capital lease. Leases not classified as finance leases are classified as operating leases. This classification will determine whether the lease expense is recognized based on an effective interest method or on a straight-line basis over the term of the lease. The lessee is also required to record a right-of-use asset and a lease liability for all leases with a term of greater than 12 months regardless of their classification. Leases with a term of 12 months or less will be accounted for similar to today’s guidance for operating leases. The new guidance will require lessors to account for leases using an approach that is substantially similar to the existing guidance for sales-type, direct financing leases and operating leases. This new guidance will be effective for the Company for the first reporting period beginning after December 15, 2018, with earlier adoption permitted. Adoption of the amendment must be applied on a modified retrospective approach. The Company is currently evaluating the effect that the standard will have on its consolidated financial statements and related disclosures.

In January 2016, the FASB issued ASU No. 2016-01, “Financial Instruments-Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities.” The new guidance is intended to improve the recognition and measurement of financial instruments. The ASU affects public and private companies, not-for-profit organizations, and employee benefit plans that hold financial assets or owe financial liabilities. ASU No. 2016-01 is effective for interim and annual reporting periods beginning after December 15, 2017. The Company is currently evaluating the effect that the standard will have on its consolidated financial statements and related disclosures.

In November 2015, the FASB issued ASU No. 2015-17, “Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes.” The FASB is issuing the amendments in this Update as part of its initiative to reduce complexity in accounting standards (the Simplification Initiative). The objective of the Simplification Initiative is to identify, evaluate, and improve areas of generally accepted accounting principles ("GAAP") for which cost and complexity can be reduced while maintaining or improving the usefulness of the information provided to users of financial statements. To simplify the presentation of deferred income taxes, the amendments in this Update require that deferred tax liabilities and assets be classified as noncurrent in a classified statement of financial position. The amendments in this Update apply to all entities that present a classified statement of financial position. The current requirement that deferred tax liabilities and assets of a tax-paying component of an entity be offset and presented as a single amount is not affected by the amendments in this Update. ASU No. 2015-17 is effective for interim and annual reporting periods beginning after December 15, 2016. Early adoption is permitted, including adoption in an interim period. All other amendments will be effective upon the issuance of this Update. The Company has evaluated the standard and determined that it has no effect on the Company's consolidated financial statements and related disclosures.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 3 - Correction of Error in Financial Statements**

Subsequent to the issuance of the Company's Annual Report on Form 10-K for the year ended September 30, 2016 and 2015, the Company determined to correct error in its historical financial statements, including for the years ended September 30, 2016 and 2015. Accordingly, the Company has restated the consolidated financial statements for the years ended September 30, 2016, 2015 and 2014 to reflect the error corrections, as mentioned below:

Item 8 of Part II of this Amendment No. 1 on Form 10-K/A includes audited consolidated financial statements for the year ended September 30, 2016 and 2015 that have been restated to correct the manner in which the Company originally accounted for the Bank's tax account balances. The audited annual financial statements as of September 30, 2016 and 2015, and for each of the years in the three year period ended September 30, 2016, as included in the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2016 (the "original Financial Statements"), which was originally filed on December 14, 2016 (the "Original 10-K Filling"), have been restated as set forth in this Amendment No. 1 on Form 10-K/A (this "Amendment"). The effect of these matters is to increase net income for fiscal 2016 by approximately $208,000, fiscal 2015 by approximately $970,000 and fiscal 2014 by approximately $388,000. The correction for 2014 represents the correction of an immaterial error. See the table below for an analysis of the impact on the consolidated balance sheets and income statements for the periods affected.

For the year ended September 30, 2016, the correction increased Net Income from $11.9 million as reported in the Consolidated Statement of Income that was included in the Original Financial Statements (the "Original Income Statements 2016") to $12.2 million. The correction also changed the amount reported under "Income tax benefit" in the Original Income Statement 2016 from $6.0 million to $6.2 million. Total Liabilities at September 30, 2016, as reported in the Consolidated Statement of Financial Condition included in the Original Financial Statements, decreased from $726.7 million to $725.1 million, due to the decrease in Other liabilities from $4.5 million to $3.0 million. Total Shareholders' Equity at September 30, 2016, as reported in the Consolidated Statement of Financial Condition included in the Original Financial Statements, increased from $94.6 million to $96.2 million due to the change in Retained Earnings from $35.7 million to $37.3 million.

For the year ended September 30, 2015, the correction increased Net Income from $3.7 million as reported in the Consolidated Statement of Income that was included in the Original Financial Statements (the "Original Income Statement 2015") to $4.7 million. The correction also changed the amount reported under "Income tax benefit" in the Original Income Statement 2015 from zero to $970,000. Total Liabilities at September 30, 2015, as reported in the Consolidated Statement of Financial Condition included in the Original Financial Statements, decreased from $574.3 million to $572.9 million, due to the decrease in Other liabilities from $3.6 million to $2.2 million. Total Shareholders' Equity at September 30, 2015, as reported in the Consolidated Statement of Financial Condition included in the Original Financial Statements, increased from $81.4 million to $82.7 million due to the change in Retained Earnings from $23.8 million to $25.2 million.

For the year ended September 30, 2014, the correction increased Net Income from \$323,000 to \$711,000 as reported in the Consolidated Statement of Income that was included in the Original Financial Statements 2014 (the "Original Income Statement 2014"). The correction also changed the amount reported under "Income tax expense (benefit)" in the Original Income Statement 2014 from an expense of 21,000 to an income tax benefit of \$367,000.

More detailed information regarding the correction is provided below.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 3 - Correction of Error in Financial Statements (Continued)**

In addition to the restatement of the Company's consolidated financial statements, certain information within the following notes to the consolidated financial statements has been restated to reflect the corrections of errors discussed above as well as other related changes and/or to add disclosure language as appropriate.

Note 4. Earnings Per Common Share

Note 13. Income Taxes

Note 16. Regulatory Capital Requirements

Note 19. Parent Company Only Financial Statements

Note 20. Quarterly Financial Information

**<u>Effects of the Restatement:</u>**

The following tables summarize the effect of the restatement on certain key items of the Original Financial Statements:

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 3 - Correction of Error in Financial Statements (Continued)**

**Item 8: Financial Statement- Balance Sheet**

| | For Year Ended September 30, | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | 2014 | | | 2015 | | | 2016 | | |
| | Original | Restated | Change | Original | Restated | Change | Original | Restated | Change |
| Other liabilities | $2,604 | $2,216 | $ (388 ) | $3,575 | $2,217 | $(1,358) | $4,549 | $2,983 | $(1,566) |
| Total Liabilities | 465,492 | 465,104 | (388 ) | 574,299 | 572,941 | (1,358) | 726,681 | 725,115 | (1,566) |
| Total Shareholders' Equity | 76,772 | 77,160 | 388 | 81,391 | 82,749 | 1,358 | 94,591 | 96,157 | 1,566 |

**Item 8: Financial Statement- Income Statement**

| | For Year Ended September 30, | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | 2014 | | | 2015 | | | 2016 | | |
| | Original | Restated | Change | Original | Restated | Change | Original | Restated | Change |
| Income tax (expense) benefit | $(21 ) | $ 367 | $ 388 | $— | $ 970 | $ 970 | $5,966 | $6,174 | $ 208 |
| Net Income (Loss) | 323 | 711 | 388 | 3,698 | 4,668 | 970 | 11,942 | 12,150 | 208 |
| Basic Earnings Per Share | 0.05 | 0.11 | 0.06 | 0.58 | 0.73 | 0.15 | 1.86 | 1.90 | 0.04 |
| Diluted Earnings Per Share | n/a | n/a | n/a | n/a | n/a | n/a | 1.86 | 1.90 | 0.04 |

**Item 8: Financial Statement - Comprehensive Income**

| | For Year Ended September 30, | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | 2014 | | | 2015 | | | 2016 | | |
| | Original | Restated | Change | Original | Restated | Change | Original | Restated | Change |
| Net Income (Loss) | $323 | $ 711 | $ 388 | $3,698 | $ 4,668 | $ 970 | $11,942 | $12,150 | 208 |
| Total comprehensive Income | 1,206 | 1,594 | 388 | 4,424 | 5,394 | 970 | 12,958 | 13,166 | 208 |

**Item 8: Financial Statement - Changes in Shareholders Equity**

| | For Year Ended September 30, | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | 2014 | | | 2015 | | | 2016 | | |
| | Original | Restated | Change | Original | Restated | Change | Original | Restated | Change |
| Net Income – Retained Earnings | $323 | $711 | $ 388 | $3,698 | $4,668 | $970 | $11,942 | $12,150 | $208 |
| | 323 | 711 | 388 | 3,698 | $4,668 | 970 | $11,942 | $12,150 | 208 |

| | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| Net Income – Total Shareholders' Equity | | | | | | | | | |
| Retained Earnings Balance at | 20,116 | 20,504 | (388 ) | 23,814 | 25,172 | (1,358) | 35,756 | 37,322 | (1,566) |
| Total Shareholders' Equity Balance at | 76,772 | 77,160 | (388 ) | 81,391 | 82,749 | (1,358) | 94,591 | 96,157 | (1,566) |

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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 3 - Correction of Error in Financial Statements (Continued)**

**Item 8: Financial Statement - Cash Flows**

| | For Year Ended September 30, | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | 2014 | | | 2015 | | | 2016 | | |
| | Original | Restated | Change | Original | Restated | Change | Original | Restated | Change |
| Net Income (Loss) | $323 | $ 711 | $ 388 | $3,698 | $4,668 | $ 970 | $11,942 | $12,150 | $ 208 |
| Increase in other liabilities | 309 | 21 | 388 | 1,319 | 349 | 970 | 974 | 766 | 208 |

**Note 4 – Earnings (Loss) Per Share (As Restated)**

Basic earnings per common share is computed based on the weighted average number of shares outstanding reduced by unearned ESOP shares. Diluted earnings per share is computed based on the weighted average number of shares outstanding and common stock equivalents (“CSEs”) that would arise from the exercise of dilutive securities reduced by unearned ESOP shares. For the fiscal year ended September 30, 2016, the Company issued stock options to purchase 5,000 shares of common stock, as well as 1,930 restricted shares, which are considered CSEs. At September 30, 2016, all restricted stocks were anti-dilutive. For the fiscal years ended September 30, 2015 and 2014, the Company did not issue and did not have any outstanding CSEs.

The following table sets forth the composition of the weighted average shares (denominator) used in the earnings per share computations.

| | Year Ended September 30, | | |
|---|---|---|---|
| (In thousands, except for share data) | 2016 | 2015 | 2014 |
| Net Income | $12,150 | $4,668 | $711 |
| Weighted average shares outstanding | 6,560,012 | 6,558,473 | 6,558,473 |
| Average unearned ESOP shares | (150,747 ) | (165,143 ) | (179,543 ) |
| Basic weighted average shares outstanding | 6,409,265 | 6,393,330 | 6,378,930 |
| Plus: effect of dilutive options | 60 | — | — |
| Diluted weighted average common shares outstanding | 6,409,325 | 6,393,330 | 6,378,930 |
| Earnings per share: | | | |
| Basic | $1.90 | $0.73 | $0.11 |
| Diluted | $1.90 | n/a | n/a |

**Note 5 – Employee Stock Ownership Plan**

The Company established an employee stock ownership plan ("ESOP") for substantially all of its full-time employees. As of September 30, 2016, the current ESOP trustee is Pentegra. Shares of the Company's common stock purchased by the ESOP are held until released for allocation to participants. Shares released are allocated to each eligible participant based on the ratio of each such participant's base compensation to the total base compensation of all eligible plan participants. As the unearned shares are committed to be released and allocated among participants, the Company recognizes compensation expense equal to the fair value of the ESOP shares during the periods in which they become committed to be released. To the extent that the fair value of the ESOP shares released differs from the cost of such shares, the difference is charged or credited to additional paid-in capital. During the period from May 20, 2008 to September 30, 2008, the ESOP purchased 241,178 shares of the common stock for approximately $2.6 million, an average price of $10.86 per share, which was funded by a loan from Malvern Federal Bancorp, Inc. (the Company's predecessor). The ESOP loan is being repaid principally from the Bank's contributions to the ESOP. The loan, which bears an interest rate of 5%, is being repaid in quarterly installments through 2026. Shares are released to participants proportionately as the loan is repaid. During years ended September 30, 2016, 2015 and 2014, there were 14,400, 14,400 and 14,400 shares, respectively, committed to be released. At September 30, 2016, there were 143,565 unallocated shares and 115,653 allocated shares held by the ESOP. The unallocated shares had an aggregate fair value of approximately $2.4 million at September 30, 2016.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 6 - Investment Securities**

The Company’s investment securities are classified as available-for-sale or held-to-maturity at September 30, 2016 and 2015. Investment securities available-for-sale are reported at fair value with unrealized gains or losses included in equity, net of tax. Accordingly, the carrying value of such securities reflects their fair value at the balance sheet date. Fair value is based upon either quoted market prices, or in certain cases where there is limited activity in the market for a particular instrument, assumptions are made to determine their fair value.

Transfers of debt securities from the available-for-sale category to the held-to-maturity category are made at fair value at the date of transfer. The unrealized holding gain or loss at the date of transfer remains in accumulated other comprehensive income and in the carrying value of the held-to-maturity investment security. Premiums or discounts on investment securities are amortized or accreted using the effective interest method over the life of the security as an adjustment of yield. Unrealized holding gains or losses that remain in accumulated other comprehensive income are amortized or accreted over the remaining life of the security as an adjustment of yield, offsetting the related amortization of the premium or accretion of the discount.

The following tables present information related to the Company’s investment securities at September 30, 2016 and 2015.

| | September 30, 2016 | | | |
|---|---|---|---|---|
| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
| | (in thousands) | | | |
| Investment Securities Available-for-Sale: | | | | |
| State and municipal obligations | $24,751 | $ 557 | $ (1 ) | $25,307 |
| Single issuer trust preferred security | 1,000 | — | (122 ) | 878 |
| Corporate debt securities | 40,189 | 347 | (334 ) | 40,202 |
| Total | 65,940 | 904 | (457 ) | 66,387 |
| Investment Securities Held-to-Maturity: | | | | |
| U.S. government agencies | $2,999 | $ 16 | $ — | $3,015 |
| State and municipal obligations | 9,826 | 167 | (1 ) | 9,992 |
| Corporate debt securities | 3,916 | 77 | — | 3,993 |
| Mortgage-backed securities: | | | | |
| Collateralized mortgage obligations, fixed-rate | 23,810 | 102 | (95 ) | 23,817 |
| Total | $40,551 | $ 362 | $ (96 ) | $40,817 |
| Total investment securities | $106,491 | $ 1,266 | $ (553 ) | $107,204 |

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 6 - Investment Securities (Continued)**

| | September 30, 2015 | | | |
|---|---|---|---|---|
| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
| | (In thousands) | | | |
| Investment Securities Available-for-Sale: | | | | |
| U.S. government agencies | $816 | $ — | $ (1 ) | $815 |
| State and municipal obligations | 42,007 | 192 | (116 ) | 42,083 |
| Single issuer trust preferred security | 1,000 | — | (150 ) | 850 |
| Corporate debt securities | 70,874 | 34 | (926 ) | 69,982 |
| | 114,697 | 226 | (1,193 ) | 113,730 |
| Mortgage-backed securities: | | | | |
| Federal National Mortgage Association (FNMA), fixed-rate | 8,797 | — | (105 ) | 8,692 |
| Federal Home Loan Mortgage Company (FHLMC), fixed-rate | 5,986 | — | (54 ) | 5,932 |
| | 14,783 | — | (159 ) | 14,624 |
| Total | $129,480 | $ 226 | $ (1,352 ) | $128,354 |
| Investment Securities Held-to-Maturity: | | | | |
| U.S. government agencies | $14,301 | $ 8 | $ (13 ) | $14,296 |
| State and municipal obligations | 10,075 | 23 | (75 ) | 10,023 |
| Corporate debt securities | 4,011 | — | (55 ) | 3,956 |
| Mortgage-backed securities: | | | | |
| Collateralized mortgage obligations, fixed-rate | 28,834 | 55 | (339 ) | 28,550 |
| Total | $57,221 | $ 86 | $ (482 ) | $56,825 |
| Total investment securities | $186,701 | $ 312 | $ (1,834 ) | $185,179 |

During the year ended September 30, 2015, the Company transferred at fair value approximately $57.5 million in available-for-sale investment securities to the held-to-maturity category. The net unrealized loss at date of transfer amounted to $115,000. This will be amortized over the remaining life of the securities as an adjustment of yield, offsetting the related amortization of the premium or accretion of the discount on the transferred securities. No gains or losses were recognized at the time of transfer. Management considers the held-to-maturity classification of these investment securities to be appropriate as the Company has the positive intent and ability to hold these securities to maturity.

For fiscal 2016, proceeds of available-for-sale investment securities sold amounted to approximately $62.8 million. Gross realized gains on investment securities sold amounted to approximately $595,000, while gross realized losses amounted to approximately $30,000 for the period. For fiscal 2015, proceeds of available-for-sale investment securities sold amounted to approximately $70.4 million. Gross realized gains on investment securities sold amounted to approximately $610,000, while gross realized losses amounted to approximately $95,000 for the period. For fiscal 2014, proceeds of investment securities sold amounted to approximately $16.8 million. Gross realized gains on investment securities sold amounted to approximately $118,000, while gross realized losses amounted to approximately $35,000 for the period.

The varying amount of sales from the available-for-sale portfolio over the past few years, reflect the significant volatility present in the market. Given the historic low interest rates prevalent in the market, it is necessary for the Company to protect itself from interest rate exposure. Securities that once appeared to be sound investments can, after changes in the market, become securities that the Company has the flexibility to sell to avoid losses and mismatches of interest-earning assets and interest-bearing liabilities at a later time.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 6 - Investment Securities (Continued)**

The following tables indicate gross unrealized losses not recognized in income and fair value, aggregated by investment category and the length of time individual securities have been in a continuous unrealized loss position at September 30, 2016 and 2015.

| | September 30, 2016 | | | | | |
|---|---|---|---|---|---|---|
| | Less than 12 Months | | More than 12 Months | | Total | |
| | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses | Fair value | Unrealized Losses |
| | (In thousands) | | | | | |
| Investment Securities Available-for-Sale: | | | | | | |
| State and municipal obligations | $501 | $ (1) | $— | $ — | $501 | $ (1) |
| Single issuer trust preferred security | — | — | 878 | (122) | 878 | (122) |
| Corporate debt securities | 984 | (9) | 10,614 | (325) | 11,598 | (334) |
| Total | $1,485 | $ (10) | $11,492 | $ (447) | $12,977 | $ (457) |
| Investment Securities Held-to-Maturity: | | | | | | |
| State and municipal obligations | 1,193 | (1) | — | — | 1,193 | (1) |
| Mortgage-backed securities: | | | | | | |
| CMO, fixed-rate | 4,342 | (17) | 6,283 | (78) | 10,625 | (95) |
| Total | 5,535 | (18) | 6,283 | (78) | 11,818 | (96) |
| Total investment securities | $7,020 | $ (28) | $17,775 | $ (525) | $24,795 | $ (553) |

| | September 30, 2015 | | | | | |
|---|---|---|---|---|---|---|
| | Less than 12 Months | | More than 12 Months | | Total | |
| | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses | Fair value | Unrealized Losses |
| | (In thousands) | | | | | |
| Investment Securities Available-for-Sale: | | | | | | |
| U.S. government agencies | $— | $ — | $815 | $ (1) | $815 | $ (1) |
| State and municipal obligations | 18,223 | (116) | — | — | 18,223 | (116) |
| Single issuer trust preferred security | — | — | 850 | (150) | 850 | (150) |
| Corporate debt securities | 58,064 | (926) | — | — | 58,064 | (926) |
| Mortgage-backed securities: | | | | | | |
| FNMA, fixed-rate | 5,459 | (53) | 3,233 | (52) | 8,692 | (105) |
| FHLMC, fixed-rate | 3,280 | (25) | 2,652 | (29) | 5,932 | (54) |
| Total | $85,026 | $ (1,120) | $7,550 | $ (232) | $92,576 | $ (1,352) |
| Investment Securities Held-to-Maturity: | | | | | | |
| U.S. government agencies | 4,792 | (13) | — | — | 4,792 | (13) |
| State and municipal obligations | 6,917 | (75) | — | — | 6,917 | (75) |

| | | | | | | |
|---|---|---|---|---|---|---|
| Corporate debt securities | 3,957 | (55) | — | — | 3,957 | (55) |
| Mortgage-backed securities: | | | | | | |
| CMO, fixed-rate | 22,734 | (339) | — | — | 22,734 | (339) |
| Total | 38,400 | (482) | — | — | 38,400 | (482) |
| Total investment securities | $123,426 | $ (1,602) | $7,550 | $ (232) | $130,976 | $ (1,834) |

As of September 30, 2016, the estimated fair value of the securities disclosed above was primarily dependent upon the movement in market interest rates, particularly given the negligible inherent credit risk associated with these securities. These investment securities are comprised of securities that are rated investment grade by at least one bond credit rating service. Although the fair value will fluctuate as the market interest rates move, management believes that these fair values will recover as the underlying portfolios mature and are reinvested in market rate yielding investments. As of September 30, 2016, the Company held two municipal bonds, nine corporate securities, 15 mortgage-backed securities and one single issuer trust preferred security which were in an unrealized loss position. As of September 30, 2015, the Company held six U.S. government agency securities, 20 municipal bonds, 29 corporate securities, 37 mortgage-backed securities and one single issuer trust preferred security which were in an unrealized loss position. The Company does not intend to sell and expects that it is not more likely than not that it will be required to sell these securities until such time as the value recovers or the securities mature. Management does not believe any individual unrealized loss as of September 30, 2016 represents other-than-temporary impairment.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 6 - Investment Securities (Continued)**

Investment securities having a carrying value of approximately $552,000 at September 30, 2016 were pledged to secure public deposits. At September 30, 2015 the Company had no securities pledged to secure public deposits.

The following table presents information for investment securities at September 30, 2016, based on scheduled maturities. Actual maturities can be expected to differ from scheduled maturities due to prepayment or early call options of the issuer.

| | September 30, 2016 | |
|---|---|---|
| | Amortized Cost | Fair Value |
| | (In thousands) | |
| Investment Securities Available-for-Sale: | | |
| Due in one year or less | $— | $— |
| Due after one year through five years | 24,464 | 24,718 |
| Due after five years through ten years | 31,166 | 31,277 |
| Due after ten years | 10,310 | 10,392 |
| Total | $65,940 | $66,387 |
| Investment Securities Held-to-Maturity: | | |
| Due after one year through five years | $2,999 | $3,015 |
| Due after five years through ten years | 5,128 | 5,291 |
| Due after ten years | 32,424 | 32,511 |
| Total | $40,551 | $40,817 |
| Total investment securities | $106,491 | $107,204 |

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 7 - Loans Receivable and Related Allowance for Loan Losses**

Loans receivable in the Company's portfolio consisted of the following at the dates indicated:

| | September 30, | |
|---|---|---|
| | 2016 | 2015 |
| | (In thousands) | |
| Residential mortgage | $209,186 | $214,958 |
| Construction and Development: | | |
| Residential and commercial | 18,579 | 5,677 |
| Land | 10,013 | 2,142 |
| Total Construction and Development | 28,592 | 7,819 |
| Commercial: | | |
| Commercial real estate | 231,439 | 87,686 |
| Multi-family | 19,515 | 7,444 |
| Other | 38,779 | 13,380 |
| Total Commercial | 289,733 | 108,510 |
| Consumer: | | |
| Home equity lines of credit | 19,757 | 22,919 |
| Second mortgages | 29,204 | 37,633 |
| Other | 1,914 | 2,359 |
| Total Consumer | 50,875 | 62,911 |
| Total loans | 578,386 | 394,198 |
| Deferred loan fees and cost, net | 1,208 | 1,776 |
| Allowance for loan losses | (5,434) | (4,667) |
| Total loans receivable, net | $574,160 | $391,307 |

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 7 - Loans Receivable and Related Allowance for Loan Losses (Continued)**

The following table summarizes the primary classes of the allowance for loan losses, segregated into the amount required for loans individually evaluated for impairment and the amount required for loans collectively evaluated for impairment as of and for the years ended September 30, 2016, 2015 and 2014.

| | Year Ended September 30, 2016 | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | | Construction and Development | | Commercial | | | Consumer | | | | |
| | Residential Mortgage | Residential and Commercial | Land | **Commercial Real Estate** | Multi-family | Other | Home Equity Lines of Credit | Second Mortgages | Other | Unallocated | Total |
| | (In thousands) | | | | | | | | | | |
| **Allowance for loan losses:** | | | | | | | | | | | |
| Beginning balance | $1,486 | $30 | $35 | $1,235 | $104 | $108 | $139 | $761 | $24 | $745 | $4,667 |
| Charge-offs | (9) | (91) | — | (99) | — | — | — | (291) | (70) | — | (560 |
| Recoveries | 17 | 243 | — | 3 | — | 3 | 1 | 100 | 13 | — | 380 |
| Provision | (293) | 17 | 62 | 735 | 5 | 47 | (24) | (103) | 67 | 434 | 947 |
| Ending Balance | $1,201 | $199 | $97 | $1,874 | $109 | $158 | $116 | $467 | $34 | $1,179 | $5,434 |
| Ending balance: individually evaluated for impairment | $— | $— | $— | $— | $— | $— | $— | $23 | $— | $— | $23 |
| Ending balance: collectively evaluated for impairment | $1,201 | $199 | $97 | $1,874 | $109 | $158 | $116 | $444 | $34 | $1,179 | $5,411 |
| Loans receivable: | | | | | | | | | | | |
| Ending balance | $209,186 | $18,579 | $10,013 | $231,439 | $19,515 | $38,779 | $19,757 | $29,204 | $1,914 | | $578,386 |

| | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| Ending balance: individually evaluated for impairment | $1,159 | $109 | $— | $2,039 | $— | $— | $74 | $277 | $— | $3,658 |
| Ending balance: collectively evaluated for impairment | $208,027 | $18,470 | $10,013 | $229,400 | $19,515 | $38,779 | $19,683 | $28,927 | $1,914 | $574,728 |

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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 7 - Loans Receivable and Related Allowance for Loan Losses (Continued)**

| | Year Ended September 30, 2015 | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | | Construction and Development | | Commercial | | | Consumer | | | | |
| | Residential Mortgage | Residential and Commercial | Land | **Commercial Real Estate** | Multi-family | Other | Home Equity Lines of Credit | **Second Mortgages** | Other | Unallocated | Total |
| | (In thousands) | | | | | | | | | | |
| Allowance for loan losses: | | | | | | | | | | | |
| Beginning balance | $1,672 | $291 | $13 | $1,248 | $29 | $50 | $168 | $1,033 | $23 | $62 | $4,589 |
| Charge-offs | — | (1) | — | (48) | — | — | — | (138) | (34) | — | (221) |
| Recoveries | 17 | 98 | — | 9 | — | 3 | 2 | 69 | 11 | — | 209 |
| Provision | (203) | (358) | 22 | 26 | 75 | 55 | (31) | (203) | 24 | 683 | 90 |
| Ending Balance | $1,486 | $30 | $35 | $1,235 | $104 | $108 | $139 | $761 | $24 | $745 | $4,667 |
| Ending balance: individually evaluated for impairment | $— | $— | $— | $— | $— | $— | $— | $— | $— | $— | $— |
| Ending balance: collectively evaluated for impairment | $1,486 | $30 | $35 | $1,235 | $104 | $108 | $139 | $761 | $24 | $745 | $4,667 |
| Loans receivable: | | | | | | | | | | | |
| Ending balance | $214,958 | $5,677 | $2,142 | $87,686 | $7,444 | $13,380 | $22,919 | $37,633 | $2,359 | | $394,198 |
| Ending balance: individually evaluated for impairment | $599 | $121 | $— | $1,571 | $— | $— | $20 | $179 | $— | | $2,490 |
| Ending balance: collectively | $214,359 | $5,556 | $2,142 | $86,115 | $7,444 | $13,380 | $22,899 | $37,454 | $2,359 | | $391,708 |

evaluated
for
impairment

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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 7 - Loans Receivable and Related Allowance for Loan Losses (Continued)**

| | Year Ended September 30, 2014 | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | | Construction and Development | | Commercial | | | Consumer | | | | |
| | Residential Mortgage | Residential and Commercial | Land | **Commercial Real Estate** | Multi-family | Other | Home Equity Lines of Credit | **Second Mortgages** | Other | Unallocated | Total |
| | (In thousands) | | | | | | | | | | |
| Allowance for loan losses: | | | | | | | | | | | |
| Beginning balance | $1,414 | $164 | $56 | $1,726 | $40 | $59 | $137 | $1,393 | $22 | $79 | $5,090 |
| Charge-offs | (83) | (37) | — | (183) | — | — | (14) | (618) | (6) | — | (941) |
| Recoveries | 23 | 1 | — | 9 | — | 3 | 1 | 136 | 4 | — | 177 |
| Provision | 318 | 163 | (43) | (304) | (11) | (12) | 44 | 122 | 3 | (17) | 263 |
| Ending Balance | $1,672 | $291 | $13 | $1,248 | $29 | $50 | $168 | $1,033 | $23 | $62 | $4,589 |
| Ending balance: individually evaluated for impairment | $— | $— | $— | $— | $— | $— | $— | $— | $— | $— | $— |
| Ending balance: collectively evaluated for impairment | $1,672 | $291 | $13 | $1,248 | $29 | $50 | $168 | $1,033 | $23 | $62 | $4,589 |
| Loans receivable: | | | | | | | | | | | |
| Ending balance | $231,324 | $5,964 | $1,033 | $71,579 | $1,032 | $5,480 | $22,292 | $47,034 | $2,839 | | $388,577 |
| Ending balance: individually evaluated for impairment | $999 | $187 | $— | $504 | $— | $900 | $115 | $695 | $— | | $3,400 |
| | $230,325 | $5,777 | $1,033 | $71,075 | $1,032 | $4,580 | $22,177 | $46,339 | $2,839 | | $385,177 |

Ending
balance:
collectively
evaluated
for
impairment

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 7 - Loans Receivable and Related Allowance for Loan Losses (Continued)**

The following table presents impaired loans in portfolio by class, segregated by those for which a specific allowance was required and those for which a specific allowance was not necessary as of September 30, 2016 and 2015.

| | Impaired Loans With Specific Allowance | | Impaired Loans With No Specific Allowance | Total Impaired Loans | |
|---|---|---|---|---|---|
| | Recorded Investment | Related Allowance | Recorded Investment | Recorded Investment | Unpaid Principal Balance |
| | (In thousands) | | | | |
| September 30, 2016: | | | | | |
| Residential mortgage | $— | $ — | $ 1,159 | $1,159 | $ 1,225 |
| Construction and Development: | | | | | |
| Residential and commercial | — | — | 109 | 109 | 109 |
| Commercial: | | | | | |
| Commercial real estate | — | — | 2,039 | 2,039 | 2,039 |
| Consumer: | | | | | |
| Home equity lines of credit | — | — | 74 | 74 | 90 |
| Second mortgages | 31 | 23 | 246 | 277 | 451 |
| Total impaired loans | $31 | $ 23 | $ 3,627 | $3,658 | $ 3,914 |
| September 30, 2015: | | | | | |
| Residential mortgage | $— | $ — | $ 599 | $599 | $ 696 |
| Construction and Development: | | | | | |
| Residential and commercial | — | — | 121 | 121 | 253 |
| Commercial: | | | | | |
| Commercial real estate | — | — | 1,571 | 1,571 | 1,807 |
| Consumer: | | | | | |
| Home equity lines of credit | — | — | 20 | 20 | 36 |
| Second mortgages | — | — | 179 | 179 | 342 |
| Total impaired loans | $— | $ — | $ 2,490 | $2,490 | $ 3,134 |

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 7 - Loans Receivable and Related Allowance for Loan Losses (Continued)**

The following table presents the average recorded investment in impaired loans in portfolio and related interest income recognized year ended September 30, 2016, 2015 and 2014.

| | Average Impaired Loans | Interest Income Recognized on Impaired Loans |
|---|---|---|
| | (In thousands) | |
| Year Ended September 30, 2016: | | |
| Residential mortgages | $707 | $ — |
| Construction and Development: | | |
| Residential and commercial | 150 | 4 |
| Commercial: | | |
| Commercial real estate | 1,646 | 69 |
| Consumer: | | |
| Home equity lines of credit | 24 | — |
| Second mortgages | 214 | — |
| Total | $2,741 | $ 73 |
| | | |
| Year Ended September 30, 2015: | | |
| Residential mortgages | $729 | $ — |
| Construction and Development: | | |
| Residential and commercial | 144 | 5 |
| Commercial: | | |
| Commercial real estate | 690 | 4 |
| Other | 340 | 12 |
| Consumer: | | |
| Home equity lines of credit | 23 | — |
| Second mortgages | 537 | — |
| Total | $2,463 | $ 21 |
| | | |
| Year Ended September 30, 2014: | | |
| Residential mortgages | $1,731 | $ — |
| Construction and Development: | | |
| Residential and commercial | 609 | 17 |
| Land | 240 | 14 |
| Commercial: | | |
| Commercial real estate | 21 | — |
| Other | 900 | 32 |
| Consumer: | | |

| | | |
|---|---|---|
| Home equity lines of credit | 104 | — |
| Second mortgages | 622 | — |
| Total | $4,227 | $ 63 |

No additional funds are committed to be advanced in connection with impaired loans.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 7 - Loans Receivable and Related Allowance for Loan Losses (Continued)**

The following table presents the classes of the loan portfolio summarized by loans considered to be rated as pass and the categories of special mention, substandard and doubtful within the Company's internal risk rating system as of September 30, 2016 and 2015.

| | September 30, 2016 | | | | |
|---|---|---|---|---|---|
| | Pass | Special Mention | Substandard | Doubtful | Total |
| | (In thousands) | | | | |
| Residential mortgage | $207,880 | $ 122 | $ 1,184 | $ — | $209,186 |
| Construction and Development: | | | | | |
| Residential and commercial | 18,470 | — | 109 | — | 18,579 |
| Land | 10,013 | — | — | — | 10,013 |
| Commercial: | | | | | |
| Commercial real estate | 221,742 | 4,990 | 4,707 | — | 231,439 |
| Multi-family | 19,303 | 212 | — | — | 19,515 |
| Other | 37,848 | 259 | 672 | — | 38,779 |
| Consumer: | | | | | |
| Home equity lines of credit | 19,584 | — | 173 | — | 19,757 |
| Second mortgages | 27,843 | 119 | 1,242 | — | 29,204 |
| Other | 1,903 | 11 | — | — | 1,914 |
| Total | $564,586 | $ 5,713 | $ 8,087 | $ — | $578,386 |

| | September 30, 2015 | | | | |
|---|---|---|---|---|---|
| | Pass | Special Mention | Substandard | Doubtful | Total |
| | (In thousands) | | | | |
| Residential mortgage | $214,146 | $ 130 | $ 682 | $ — | $214,958 |
| Construction and Development: | | | | | |
| Residential and commercial | 5,450 | 106 | 121 | — | 5,677 |
| Land | 2,142 | — | — | — | 2,142 |
| Commercial: | | | | | |
| Commercial real estate | 78,207 | 4,791 | 4,688 | — | 87,686 |
| Multi-family | 7,166 | 278 | — | — | 7,444 |
| Other | 12,387 | 272 | 721 | — | 13,380 |
| Consumer: | | | | | |
| Home equity lines of credit | 22,801 | — | 118 | — | 22,919 |
| Second mortgages | 36,834 | 133 | 666 | — | 37,633 |
| Other | 2,345 | 14 | — | — | 2,359 |
| Total | $381,478 | $ 5,724 | $ 6,996 | $ — | $394,198 |

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 7 - Loans Receivable and Related Allowance for Loan Losses (Continued)**

The following table presents loans on which we are no longer accruing interest by portfolio class at the dates indicated.

| | September 30, 2016 | September 30, 2015 |
|---|---|---|
| | (In thousands) | |
| Residential mortgage | $1,072 | $599 |
| Construction and Development: | | |
| Residential and commercial | — | 12 |
| Commercial: | | |
| Commercial real estate | 193 | 589 |
| Consumer: | | |
| Home equity lines of credit | 74 | 20 |
| Second mortgages | 278 | 179 |
| Total non-accrual loans | $1,617 | $1,399 |

Under the Bank’s loan policy, once a loan has been placed on non-accrual status, we do not resume interest accruals until the loan has been brought current and has maintained a current payment status for not less than six consecutive months. Interest income that would have been recognized on nonaccrual loans had they been current in accordance with their original terms was $48,000, $84,000 and $121,000 for fiscal 2016, 2015 and 2014, respectively. At September 30, 2016 there were approximately $696,000 loans past due 90 days or more and still accruing interest. There were no loans past due 90 days or more and still accruing interest at September 30, 2015.

Management further monitors the performance and credit quality of the loan portfolio by analyzing the age of the portfolio as determined by whether a loan payment is “current,” that is, it is received from a borrower by the scheduled due date, or the length of time a scheduled payment is past due. The following table presents the classes of the loan portfolio summarized by the aging categories as of September 30, 2016 and 2015.

| | Current | 30-59 Days Past Due | 60-89 Days Past Due | 90 Days or More Past Due | Total Past Due | Total Loans Receivable | Accruing 90 Days or More Past Due |
|---|---|---|---|---|---|---|---|
| | (in thousands) | | | | | | |
| September 30, 2016: | | | | | | | |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Residential mortgage | $204,816 | $1,750 | $1,345 | $1,275 | $4,370 | $ 209,186 | $ 509 |
| Construction and Development: | | | | | | | |
| Residential and commercial | 18,579 | — | — | — | — | 18,579 | — |
| Land | 10,013 | — | — | — | — | 10,013 | — |
| Commercial: | | | | | | | |
| Commercial real estate | 231,059 | — | — | 380 | 380 | 231,439 | 187 |
| Multi-family | 19,515 | — | — | — | — | 19,515 | — |
| Other | 38,433 | 346 | — | — | 346 | 38,779 | — |
| Consumer: | | | | | | | |
| Home equity lines of credit | 19,513 | 170 | 43 | 31 | 244 | 19,757 | — |
| Second mortgages | 27,933 | 473 | 566 | 232 | 1,271 | 29,204 | — |
| Other | 1,913 | 1 | — | — | 1 | 1,914 | — |
| Total | $571,774 | $2,740 | $1,954 | $1,918 | $6,612 | $ 578,386 | $ 696 |

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 7 - Loans Receivable and Related Allowance for Loan Losses (Continued)**

| | Current | 30 - 59 Days Past Due | 60 - 89 Days Past Due | 90 Days or More Past Due | Total Past Due | Total Loans Receivable |
|---|---|---|---|---|---|---|
| | (in thousands) | | | | | |
| September 30, 2015: | | | | | | |
| Residential mortgage | $213,253 | $913 | $193 | $599 | $1,705 | $ 214,958 |
| Construction and Development: | | | | | | |
| Residential and commercial | 5,665 | — | — | 12 | 12 | 5,677 |
| Land | 2,142 | — | — | — | — | 2,142 |
| Commercial: | | | | | | |
| Commercial real estate | 86,119 | 485 | 493 | 589 | 1,567 | 87,686 |
| Multi-family | 7,444 | — | — | — | — | 7,444 |
| Other | 13,380 | — | — | — | — | 13,380 |
| Consumer: | | | | | | |
| Home equity lines of credit | 22,899 | — | — | 20 | 20 | 22,919 |
| Second mortgages | 37,010 | 345 | 99 | 179 | 623 | 37,633 |
| Other | 2,329 | 30 | — | — | 30 | 2,359 |
| Total | $390,241 | $1,773 | $785 | $1,399 | $3,957 | $ 394,198 |

Restructured loans deemed to be TDRs are typically the result of extension of the loan maturity date or a reduction of the interest rate of the loan to a rate that is below market, a combination of rate and maturity extension, or by other means including covenant modifications, forbearance and other concessions. However, the Company generally only restructures loans by modifying the payment structure to require payments of interest only for a specified period or by reducing the actual interest rate. Once a loan becomes a TDR, it will continue to be reported as a TDR during the term of the restructure.

The Company had seven and five loans classified as TDRs with an aggregate outstanding balance of $2.2 million and $1.6 million at September 30, 2016 and 2015, respectively. At September 30, 2016, these loans were also classified as impaired. All of the TDR loans continue to perform under the restructured terms through September 30, 2016 and we continued to accrue interest on such loan through such date. Two commercial loans to one borrower, with an aggregate balance of $477,000 at September 30, 2016, were returned to accruing status and consolidated into one loan during fiscal 2016. The increase in TDRs of approximately $600,000 during fiscal 2016 was due to the addition of one residential mortgage loan with an outstanding balance of $85,000 and a commercial loan with an outstanding balance of $386,000 were classified as a performing TDR and impaired loan. As well as, one residential mortgage loan with a balance of $139,000 was classified as a non-performing TDR and impaired loan at September 30, 2016. At September 30, 2015, the two commercial loans to one borrower with a balance of $492,000 were non-accruing. All of such loans have been classified as TDRs since we modified the payment terms and in some cases interest rate from the original agreements and allowed the borrowers, who were experiencing financial difficulty, to make interest only payments for a period of time in order to relieve some of their overall cash flow burden. Some loan modifications classified as TDRs may not ultimately result in the full collection of principal and interest, as modified, and result in potential incremental losses. These potential incremental losses have been factored into our overall estimate of the allowance for loan losses. The level of any defaults will likely be affected by future economic conditions. A default on a troubled debt restructured loan for purposes of this disclosure occurs when the borrower is 90 days past due or a foreclosure or repossession of the applicable collateral has occurred.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 7 - Loans Receivable and Related Allowance for Loan Losses (Continued)**

TDRs may arise in which, due to financial difficulties experienced by the borrower, the Company obtains through physical possession one or more collateral assets in satisfaction of all or part of an existing credit. Once possession is obtained, the Company reclassifies the appropriate portion of the remaining balance of the credit from loans to OREO, which is included within other assets in the Consolidated Statements of Condition. For any residential real estate property collateralizing a consumer mortgage loan, the Company is considered to possess the related collateral only if legal title is obtained upon completion of foreclosure, or the borrower conveys all interest in the residential real estate property to the Company through completion of a deed in lieu of foreclosure or similar legal agreement. Excluding OREO, the Company had $141,000 and $1.2 million of residential real estate properties in the process of foreclosure at September 30, 2016 and 2015, respectively.

| | Total Troubled Debt Restructurings | | Troubled Debt Restructured Loans That Have Defaulted on Modified Terms Within The Past 12 Months | |
|---|---|---|---|---|
| | Number of Loans | Recorded Investment | Number of Loans | Recorded Investment |
| | (Dollars in thousands) | | | |
| At September 30, 2016: | | | | |
| Residential mortgage | 2 | $ 224 | 1 | $ 139 |
| Construction and Development: | | | | |
| Residential and commercial | 1 | 109 | — | — |
| Commercial: | | | | |
| Commercial real estate | 4 | 1,845 | — | — |
| Total | 7 | $ 2,178 | 1 | $ 139 |
| At September 30, 2015: | | | | |
| Construction and Development: | | | | |
| Residential and commercial | 1 | $ 109 | — | $ — |
| Commercial: | | | | |
| Commercial real estate | 4 | 1,474 | 2 | 492 |
| Total | 5 | $ 1,583 | 2 | $ 492 |

The following table reports the performing status of all TDR loans. The performing status is determined by the loan's compliance with the modified terms.

| | September 30, | | | |
|---|---|---|---|---|
| | 2016 | | 2015 | |
| | Performing | Non-Performing | Performing | Non-Performing |
| | (In thousands) | | | |
| Residential mortgage | $85 | $ 139 | $— | $ — |
| Construction and Development: | | | | |
| Residential and commercial | 109 | — | 109 | — |
| Commercial: | | | | |
| Commercial real estate | 1,845 | — | 982 | 492 |
| Total | $2,039 | $ 139 | $1,091 | $ 492 |

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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 7 - Loans Receivable and Related Allowance for Loan Losses (Continued)**

The following table shows the new TDR's for the twelve months ended September 30, 2016 and 2015.

| | September 30, 2016 | | | 2015 | | |
|---|---|---|---|---|---|---|
| | Restructured During Period | | | | | |
| | Number of Loans | Pre-Modifications Outstanding Recorded Investments | Post-Modifications Outstanding Recorded Investments | Number of Loans | Pre-Modifications Outstanding Recorded Investments | Post-Modifications Outstanding Recorded Investments |
| | (In thousands) | | | | | |
| **Troubled Debt Restructurings:** | | | | | | |
| Residential mortgage | 2 | $ 245 | $ 245 | — | $ — | $ — |
| Commercial: | | | | | | |
| Commercial real estate | 1 | 386 | 386 | 4 | 1,485 | 1,485 |
| Total | 3 | $ 631 | $ 631 | 4 | $ 1,485 | $ 1,485 |

The following table sets forth the aggregate dollar amount of loans to principal officers, directors and their affiliates in the normal course of business of the Company.

| (In thousands) | Year Ended September 30, 2016 | 2015 |
|---|---|---|
| Balance at beginning of year | $5,635 | $252 |
| New loans | 12,249 | 8,474 |
| Repayments | (9,892 ) | (3,091) |
| Balance at end of year | $7,992 | $5,635 |

At September 30, 2016, 2015 and 2014, the Company was servicing loans for the benefit of others in the amounts of $45.4 million, $54.1 million and $59.9 million, respectively. A summary of mortgage servicing rights included in other assets and the activity therein follows for the periods indicated:

| | September 30, 2016 | 2015 | 2014 |
|---|---|---|---|
| | (In thousands) | | |
| Balance at beginning of year | $401 | $453 | $271 |

| | | | |
|---|---|---|---|
| Amortization | (73 ) | (82 ) | 22 |
| Addition | — | 30 | 160 |
| Balance at end of year | $328 | $401 | $453 |

For the fiscal year ended September 30, 2016, 2015 and 2014, the fair value of servicing rights was determined using a base discount rate between 11% and 12%. The fair market value is evaluated by a third party vendor on a quarterly basis for impairment purposes only. For the fiscal year ended September 30, 2016, we sold $6.4 million of long-term, fixed-rate residential mortgage loans with servicing released. This transaction resulted in a gain of $116,000. For the year ended September 30, 2016, the Company only sold loans with servicing released. For the fiscal year ended September 30, 2015, we sold $4.1 million of long-term, fixed-rate residential mortgage loans with the servicing retained. This transaction resulted in a gain of $102,000. For the fiscal year ended September 30, 2014, we sold $7.7 million of long-term, fixed-rate residential mortgage loans with the servicing retained. This transaction resulted in a gain of $71,000.

No valuation allowance on servicing rights has been recorded at September 30, 2016, 2015, or 2014.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 8 - Property and Equipment**

Property and equipment, net consisted of the following at September 30, 2016 and 2015:

| | Estimated Useful Life (years) | September 30, 2016 | 2015 |
|---|---|---|---|
| | | (In thousands) | |
| Land | — | $711 | $711 |
| Building and improvements | 10-39 | 11,400 | 11,124 |
| Construction in process | — | 222 | 154 |
| Furniture, fixtures and equipment | 3-7 | 4,722 | 4,317 |
| | | 17,055 | 16,306 |
| Accumulated depreciation | | (10,418) | (9,771) |
| | | $6,637 | $6,535 |

Depreciation expense was approximately $650,000, $646,000 and $638,000 for the years ended September 30, 2016, 2015 and 2014, respectively. We also had a $41,000 loss on disposal of fixed assets related to the closure of our Westtown branch in June 2014.

**Note 9 - Deposits**

Deposits classified by interest rates with percentages to total deposits at September 30, 2016 and 2015 consisted of the following:

| | September 30, 2016 Amount | Percent of Total Deposits | 2015 Amount | Percent of Total Deposits |
|---|---|---|---|---|
| | (Dollars in thousands) | | | |
| Balances by types of deposit: | | | | |
| Savings | $44,714 | 7.43 % | $45,189 | 9.71 % |
| Money market accounts | 177,486 | 29.48 | 108,706 | 23.35 |
| Interest bearing demand | 95,041 | 15.78 | 82,897 | 17.81 |
| Non-interest bearing demand | 34,547 | 5.74 | 27,010 | 5.80 |
| | 351,788 | 58.43 | 263,802 | 56.67 |
| Certificates of deposit | 250,258 | 41.57 | 201,720 | 43.33 |
| Total | $602,046 | 100.00 % | $465,522 | 100.00 % |

The total amount of certificates of deposit of $250,000 and greater at September 30, 2016 and 2015 was $13.7 million and $12.2 million, respectively. We had brokered deposits totaling $58.8 million at September 30, 2016. We had no brokered deposits at September 30, 2015.

Interest expense on deposits consisted of the following for the years:

| | September 30, | | |
|---|---|---|---|
| | 2016 | 2015 | 2014 |
| | (In thousands) | | |
| Savings accounts | $33 | $29 | $27 |
| Money market accounts | 874 | 271 | 164 |
| Interest bearing demand | 139 | 83 | 85 |
| Certificates of deposit | 3,491 | 3,048 | 3,693 |
| Total deposits | $4,537 | $3,431 | $3,969 |

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 9 - Deposits (Continued)**

The following is a schedule of certificates of deposit maturities.

| | September 30, 2016 (In thousands) |
|---|---|
| Maturing in the Fiscal Year Ending September 30, | |
| 2017 | $150,614 |
| 2018 | 48,906 |
| 2019 | 16,981 |
| 2020 | 8,218 |
| 2021 | 16,551 |
| Thereafter | 8,988 |
| | $250,258 |

Deposits from related parties held by the Company at September 30, 2016 and 2015 amounted to $6.4 million and $5.5 million, respectively.

**Note 10 - Borrowings**

Under terms of its collateral agreement with the Federal Home Loan Bank of Pittsburgh ("FHLB"), the Company maintains otherwise unencumbered qualifying assets in an amount at least equal to its borrowings.

Under an agreement with the FHLB, the Company has a line of credit available in the amount of $127.8 million and $108.5 million, respectively, of which none was outstanding at September 30, 2016 or 2015. The interest rate on the line of credit at September 30, 2016 and 2015 was 0.46% and 0.34%, respectively.

The summary of long-term borrowings as of September 30, 2016 and 2015 are as follows:

| | September 30, 2016 | | 2015 | |
|---|---|---|---|---|
| | Amount | Weighted Average Rate | Amount | Weighted Average Rate |
| | (Dollars in thousands) | | | |
| Due by September 30: | | | | |
| 2016 | $— | — % | $20,000 | 0.61 % |

| | | | | | | |
|---|---|---|---|---|---|---|
| 2017 | 35,000 | 0.22 | | — | — | |
| 2018 | — | — | | 30,000 | 3.38 | |
| 2019 | 55,000 | 1.62 | | 25,000 | 2.12 | |
| 2020 | 28,000 | 2.83 | | 28,000 | 2.51 | |
| Total FHLB Advances | $118,000 | 1.65 | % | $103,000 | 2.48 | % |

At September 30, 2016, the Company had $118.0 million in outstanding long-term fixed rate FHLB advances and $223.0 million in potential FHLB advances available to us, which is based on the amount of FHLB stock held or levels of other assets, including U.S. government securities, and certain mortgage loans which are available for collateral.

**Note 11- Derivatives**

The Company is exposed to certain risks arising from both its business operations and economic conditions. The Company principally manages its exposures to a wide variety of business and operational risks through management of its core business activities. The Company manages economic risks, including interest rate, liquidity, and credit risk primarily by managing the amount, sources, and duration of its debt funding and the use of derivative financial instruments. Specifically, the Company enters into derivative financial instruments to manage exposures that arise from business activities that result in the payment of future uncertain cash amounts, the value of which are determined by interest rates.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 11 - Derivatives (Continued)**

The Company's objectives in using interest rate derivatives are to add stability to interest expense and to manage its exposure to interest rate movements. To accomplish this objective, the Company primarily uses interest rate swaps as part of its interest rate risk management strategy. Interest rate swaps designated as cash flow hedges involve the receipt of variable amounts from a counterparty in exchange for the Company making fixed-rate payments over the life of the agreements without exchange of the underlying notional amount.

The effective portion of changes in the fair value of derivatives designated and that qualify as cash flow hedges is recorded in Accumulated Other Comprehensive Income and is subsequently reclassified into earnings in the period that the hedged forecasted transaction affects earnings. At September 30, 2016, such derivatives were used to hedge the variable cash flows associated with FHLB advances. The ineffective portion of the change in fair value of the derivatives is recognized directly in earnings. The Company's derivatives did not have any hedge ineffectiveness recognized in earnings during fiscal 2016 and 2015.

Amounts reported in accumulated other comprehensive income related to derivatives will be reclassified to interest expense as interest payments are made on the Company's variable-rate debt. During the next twelve months, the Company estimates approximately $203,000 to be reclassified to earnings in interest expense. The Company is hedging its exposure to the variability in future cash flows for forecasted transactions over a maximum period of twenty months (excluding forecasted transactions related to the payment of variable interest on existing financial instruments).

The table below presents the fair value of the Company's derivative financial instruments as well as their classification on the Balance Sheet as of September 30, 2016 and 2015:

| | September 30, 2016 | | | |
|---|---|---|---|---|
| | Notional Amount | Fair Value | Balance Sheet Location | Expiration Date |
| | **(dollars in thousand)** | | | |
| **Derivatives designated as hedging instruments** | | | | |
| **Interest rate swaps by effective date:** | | | | |
| August 3, 2015 | $15,000 | $ 394 | Other liabilities | August 3, 2020 |
| February 5, 2016 | 20,000 | 148 | Other liabilities | February 1, 2021 |

| | **September 30, 2015** | | | |
|---|---|---|---|---|
| | **Notional Amount** | Fair Value | Balance Sheet Location | Expiration Date |
| | (Dollars in thousand) | | | |

**Derivatives designated as hedging instruments**

Interest rate swaps by effective date:

| | | | | |
|---|---|---|---|---|
| August 3, 2015 | $ 15,000 | $ 348 | Other liabilities | August 3, 2020 |

Interest expense recorded on these swaps transactions totaled approximately $272,000 and $36,000 for the years ended September 30, 2016 and 2015, respectively, and is reported as a component of interest expense on FHLB Advances. There are no related expenses for the year ended September 30, 2014.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 11 – Derivatives (Continued)**

**Cash Flow Hedge**

The following table presents the net gains (losses) recorded in accumulated other comprehensive income and the Consolidated Statements of Income relating to the cash flow derivative instruments for the year ended September 30:

| | For the Year Ended September 30, 2016 | | |
|---|---|---|---|
| | Amount of Gain (Loss) Recognized in OCI (Effective Portion) | Amount of Gain (Loss) Reclassified from OCI to Interest Expense | Amount of Gain (Loss) Recognized in Other Non-Interest Income (Ineffective Portion) |
| | (in thousands) | | |
| August 3, 2015 | $(270) | $ (188) | $ — |
| February 5, 2016 | (231) | (84) | — |

| | **For the Year Ended September 30, 2015** | | |
|---|---|---|---|
| | **Amount of Gain (Loss) Recognized in OCI (Effective Portion)** | Amount of Gain (Loss) Reclassified from OCI to Interest Expense | Amount of Gain (Loss) Recognized in Other Non-Interest Income (Ineffective Portion) |
| | (in thousands) | | |
| Interest Rate Contracts | $348 | $ 36 | $ — |

The Company has agreements with each of its derivative counterparties that contain a provision where if the Company defaults on any of its indebtedness, including default where repayment of the indebtedness has not been accelerated by the lender, then the Company could also be declared in default on its derivative obligations.

At September 30, 2016 and 2015, the fair value of derivatives in a net liability position, which includes accrued interest but excludes any adjustment for nonperformance risk, related to these agreements was $586,000 and $195,000, respectively. As of September 30, 2016 and 2015, the Company has minimum collateral posting thresholds with certain of its derivative counterparties and has posted collateral of $800,000 and $600,000, respectively, against its obligations under these agreements. If the Company had breached any of these provisions at September 30, 2016, it could have been required to settle its obligations under the agreements at the termination value and would have been required to pay any additional amounts due in excess of amounts previously posted as collateral with the respective counterparty.

**Note 12 - Fair Value Measurements**

The Company follows FASB ASC Topic 820 "Fair Value Measurement," to record fair value adjustments to certain assets and to determine fair value disclosures for the Company's financial instruments. Investment and mortgage-backed securities available for sale are recorded at fair value on a recurring basis. Additionally, from time to time, the Company may be required to record at fair value other assets on a nonrecurring basis, such as impaired loans, real estate owned and certain other assets. These nonrecurring fair value adjustments typically involve application of lower-of-cost-or-market accounting or write-downs of individual assets.

The Company groups its assets at fair value in three levels, based on the markets in which the assets are traded and the reliability of the assumptions used to determine fair value. These levels are:

Level 1—Valuation is based upon quoted prices for identical instruments traded in active markets.

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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 12 - Fair Value Measurements (Continued)**

Level 2—Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market.

Level 3—Valuation is generated from model-based techniques that use significant assumptions not observable in the market. These unobservable assumptions reflect the Company's own estimates of assumptions that market participants would use in pricing the asset.

The Company bases its fair values on the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. It is our policy to maximize the use of observable inputs and minimize the use of unobservable inputs when developing fair value measurements, in accordance with the fair value hierarchy.

Fair value measurements for assets where there exists limited or no observable market data and, therefore, are based primarily upon the Company's or other third-party's estimates, are often calculated based on the characteristics of the asset, the economic and competitive environment and other factors. Therefore, the results cannot be determined with precision and may not be realized in an actual sale or immediate settlement of the asset. Additionally, there may be inherent weaknesses in any calculation technique, and changes in the underlying assumptions used, including discount rates and estimates of future cash flows, could significantly affect the results of current or future valuations.

FASB ASC Topic 825 "Financial Instruments" provides an option to elect fair value as an alternative measurement for selected financial assets and financial liabilities not previously recorded at fair value. The fair value of a financial instrument is the current amount that would be exchanged between willing parties, other than in a forced liquidation.

The Company monitors and evaluates available data to perform fair value measurements on an ongoing basis and recognizes transfers among the levels of the fair value hierarchy as of the date event or a change in circumstances that affects the valuation method chosen. There were no changes in valuation technique or transfers between levels as of and for the years ended September 30, 2016 and 2015.

The tables below present the balances of assets measured at fair value on a recurring basis at September 30, 2016 and 2015:

| | **September 30, 2016** | | | |
|---|---|---|---|---|
| | Total | Level 1 | Level 2 | Level 3 |

| | (in thousands) | | | | | |
|---|---|---|---|---|---|---|
| Assets: | | | | | | |
| Investment securities available-for-sale: | | | | | | |
| Debt securities: | | | | | | |
| State and municipal obligations | $25,307 | $ | — | $25,307 | $ | — |
| Single issuer trust preferred security | 878 | | — | 878 | | — |
| Corporate debt securities | 40,202 | | — | 40,202 | | — |
| Total investment securities available-for-sale | 66,387 | | — | 66,387 | | — |
| Liabilities: | | | | | | |
| Derivative instruments | $542 | $ | — | $542 | $ | — |

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 12 - Fair Value Measurements (Continued)**

| | **September 30, 2015** | | | |
|---|---|---|---|---|
| | **Total** | **Level 1** | **Level 2** | **Level 3** |
| | **(in thousands)** | | | |
| **Assets:** | | | | |
| **Investment securities available-for-sale:** | | | | |
| Debt securities: | | | | |
| U.S. government agencies | $815 | $ — | $815 | $ — |
| State and municipal obligations | 42,083 | — | 42,083 | — |
| Single issuer trust preferred security | 850 | — | 850 | — |
| Corporate debt securities | 69,982 | — | 69,982 | — |
| Total investment securities available-for-sale | 113,730 | — | 113,730 | — |
| **Mortgage-backed securities available-for-sale:** | | | | |
| FNMA, fixed-rate | 8,692 | — | 8,692 | — |
| FHLMC, fixed-rate | 5,932 | — | 5,932 | — |
| Total mortgage-backed securities available-for-sale | 14,624 | — | 14,624 | — |
| Total investments securities available for sale | $128,354 | $ — | $128,354 | $ — |
| **Liabilities:** | | | | |
| Derivative instruments | $348 | $ — | $348 | $ — |

For assets measured at fair value on a nonrecurring basis in fiscal 2016 and fiscal 2015 that were still held at the end of the period, the following table provides the level of valuation assumptions used to determine each adjustment and the carrying value of the related individual assets or portfolios at September 30, 2016 and 2015:

| | September 30, 2016 | | | |
|---|---|---|---|---|
| | Total | Level 1 | Level 2 | Level 3 |
| | **(in thousands)** | | | |
| Impaired loans[1] | $8 | $ — | $ — | $ 8 |
| Total | $8 | $ — | $ — | $ 8 |

| September 30, 2016 | | | |
|---|---|---|---|
| Fair Value at September 30, 2016 | Valuation Technique | Unobservable Input | Range/(Weighted Average) |
| **(dollars in thousands)** | | | |

| | | | | | |
|---|---|---|---|---|---|
| Impaired loans[1] | $8 | Appraisal of collateral[2] | Collateral discounts[3] | 0%/(0% | ) |
| Total | $8 | | | | |

(1) At September 30, 2016, consisted of one loan with an aggregate balance of $31,000 and with $23,000 in specific loan loss allowance.

(2) Fair value is generally determined through independent appraisals of the underlying collateral primarily using comparable sales.

(3) Appraisals may be adjusted by management for qualitative factors such as time, changes in economic conditions and estimated liquidation expense.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 12 - Fair Value Measurements (Continued)**

| | September 30, 2015 | | | |
|---|---|---|---|---|
| | Total | Level 1 | Level 2 | Level 3 |
| | (In thousands) | | | |
| Impaired loans(1) (2) | $48 | $ — | $ — | $ 48 |
| Mortgage servicing rights | 30 | — | 30 | — |
| Total | $78 | $ — | $ 30 | $ 48 |

| | September 30, 2015 | | | |
|---|---|---|---|---|
| | Fair Value at September 30, 2015 | Valuation Technique | Unobservable Input | Range/(Weighted Average) |
| | (Dollars in thousands) | | | |
| Impaired loans(1) (2) | $ 48 | Appraisal of collateral(3) | Collateral discounts(4) | 65 – 80%/(74%) |
| Total | $48 | | | |

(1) At September 30, 2015, consisted of two loans with an aggregate balance of $48,000 and there were no specific loan loss allowance.
(2) Includes assets directly charged-down to fair value during the year-to-date period.
(3) Fair value is generally determined through independent appraisals of the underlying collateral primarily using comparable sales.
(4) Appraisals may be adjusted by management for qualitative factors such as time, changes in economic conditions and estimated liquidation expense.

For the year ended September 30, 2016, the Company did not have any additions to our mortgage servicing assets. For the fiscal year end 2016, the Company only sold loans with servicing released. The following table shows active information regarding significant techniques and inputs used at September 30, 2015 for measures in a non-recurring basis using unobservable inputs (Level 2):

| Fair Value at September 30, 2015 | Valuation Technique | Unobservable Input | Method or Value as of September 30, 2015 |
|---|---|---|---|

| | (In thousands) | | | | |
|---|---|---|---|---|---|
| Mortgage servicing rights | $30 | Discounted rate | Discount rate | 11.00 – 12.00% | Rate used through modeling period |
| | | | Loan prepayment speeds | 14.73% | Weighted-average conditional prepayment rate |
| | | | Servicing fees | 0.25% | Of loan balance |
| | | | Servicing costs | $6.25 | Monthly servicing cost per account |
| | | | | $300 – 500 | Additional monthly servicing cost per loan on loans more than 30 days delinquent |

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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 12 - Fair Value Measurements (Continued)**

The following disclosure of the estimated fair value of financial instruments is made in accordance with the requirements of FASB ASC 825. The estimated fair value amounts have been determined by the Company using available market information and appropriate valuation methods. However, considerable judgment is necessarily required to interpret market data to develop the estimates of fair value. Accordingly, the estimates presented herein are not necessarily indicative of the amounts the Company would realize in a current market exchange. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts. FASB ASC 825 excludes certain financial instruments and all non-financial instruments from its disclosure requirements. Accordingly, the aggregate fair value amounts presented may not necessarily represent the underlying fair value of the Company.

The fair value estimates presented herein are based on pertinent information available to management as of September 30, 2016 and 2015. Although management is not aware of any factors that would significantly affect the estimated fair value amounts, such amounts have not been comprehensively revalued for purposes of these financial statements since September 30, 2016 and 2015 and, therefore, current estimates of fair value may differ significantly from the amounts presented herein.

The following assumptions were used to estimate the fair value of the Company's financial instruments:

***Cash and Cash Equivalents***—These assets are carried at historical cost. The carrying amount is a reasonable estimate of fair value because of the relatively short time between the origination of the instrument and its expected realization.

***Investment Securities***—Investment and mortgage-backed securities available for sale (carried at fair value) and held to maturity (carried at amortized cost) are measured at fair value on a recurring basis. Fair value measurements for these securities are typically obtained from independent pricing services that we have engaged for this purpose. When available, we, or our independent pricing service, use quoted market prices to measure fair value. If market prices are not available, fair value measurement is based upon models that incorporate available trade, bid and other market information and for structured securities, cash flow and, when available, loan performance data. Because many fixed income securities do not trade on a daily basis, our independent pricing service's applications apply available information through processes such as benchmark curves, benchmarking of like securities, sector groupings and matrix pricing to prepare evaluations. For each asset class, pricing applications and models are based on information from market sources and integrate relevant credit information. All of our securities available for sale are valued using either of the foregoing methodologies to determine fair value adjustments recorded to our financial statements. The Company had no Level 1 or Level 3 securities as of September 30, 2016 or 2015.

***Loans Receivable***—We do not record loans at fair value on a recurring basis. As such, valuation techniques discussed herein for loans are primarily for estimating fair value for FASB ASC 825 disclosure purposes. However, from time to time, we record nonrecurring fair value adjustments to loans to reflect partial write-downs for impairment or the full charge-off of the loan carrying value. The valuation of impaired loans is discussed below. The fair value estimate for FASB ASC 825 purposes differentiates loans based on their financial characteristics, such as product classification, loan category, pricing features and remaining maturity. Prepayment and credit loss estimates are evaluated by loan type and rate. The fair value of loans is estimated by discounting contractual cash flows using discount rates based on current industry pricing, adjusted for prepayment and credit loss estimates.

***Impaired Loans***—Impaired loans are valued utilizing independent appraisals that rely upon quoted market prices for similar assets in active markets. These appraisals include adjustments to comparable assets based on the appraisers' market knowledge and experience. The appraisals are adjusted downward by management, as necessary, for changes in relevant valuation factors subsequent to the appraisal date and are considered level 3 inputs.

***Accrued Interest Receivable***—This asset is carried at historical cost. The carrying amount is a reasonable estimate of fair value because of the relatively short time between the origination of the instrument and its expected realization.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 12 - Fair Value Measurements (Continued)**

***Restricted Stock***—Although restricted stock is an equity interest in the FHLB, it is carried at cost because it does not have a readily determinable fair value as its ownership is restricted and it lacks a market. The estimated fair value approximates the carrying amount.

***Other Real Estate Owned***—Assets acquired through foreclosure or deed in lieu of foreclosure are recorded at estimated fair value less estimated selling costs when acquired, thus establishing a new cost basis. Fair value is generally based on independent appraisals. These appraisals include adjustments to comparable assets based on the appraisers' market knowledge and experience, and are considered level 3 inputs. When an asset is acquired, the excess of the loan balance over fair value, less estimated selling costs, is charged to the allowance for loan losses. If the estimated fair value of the asset declines, a write-down is recorded through expense. The valuation of foreclosed assets is subjective in nature and may be adjusted in the future because of, among other factors, changes in the economic conditions.

***Deposits***—Deposit liabilities are carried at cost. As such, valuation techniques discussed herein for deposits are primarily for estimating fair value for FASB ASC 825 disclosure purposes. The fair value of deposits is discounted based on rates available for borrowings of similar maturities. A decay rate is estimated for non-time deposits. The discount rate for non-time deposits is adjusted for servicing costs based on industry estimates.

***Long-Term Borrowings***—Advances from the FHLB are carried at amortized cost. However, we are required to estimate the fair value of long-term debt under FASB ASC 825. The fair value is based on the contractual cash flows discounted using rates currently offered for new notes with similar remaining maturities.

***Derivatives***—The fair value of derivatives are based on valuation models using observable market data as of the measurement date (level 2). Our derivatives are traded in an over-the-counter market where quoted market prices are not always available. Therefore, the fair values of derivatives are determined using quantitative models that utilize multiple market inputs. The inputs will vary based on the type of derivative, but could include interest rates, prices and indices to generate continuous yield or pricing curves, prepayment rate, and volatility factors to value the position. The majority of market inputs is actively quoted and can be validated through external sources, including brokers, market transactions and third-party pricing services.

***Accrued Interest Payable***—This liability is carried at historical cost. The carrying amount is a reasonable estimate of fair value because of the relatively short time between the origination of the instrument and its expected realization.

***Commitments to Extend Credit and Letters of Credit***—The majority of the Company's commitments to extend credit and letters of credit carry current market interest rates if converted to loans. Because commitments to extend credit and letters of credit are generally unassignable by either the Bank or the borrower, they only have value to the Company and the borrower. The estimated fair value approximates the recorded deferred fee amounts, which are not significant.

***Mortgage Servicing Rights***—The fair value of mortgage servicing rights is based on observable market prices when available or the present value of expected future cash flows when not available. Assumptions, such as loan default rates, costs to service, and prepayment speeds significantly affect the estimate of future cash flows.

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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 12 - Fair Value Measurements (Continued)**

The carrying amount and estimated fair value of the Company's financial instruments as of September 30, 2016 and 2015 were as follows:

| | Carrying Amount (in thousands) | Fair Value | Level 1 | Level 2 | Level 3 |
|---|---|---|---|---|---|
| **September 30, 2016:** | | | | | |
| Financial assets: | | | | | |
| Cash and cash equivalents | $96,762 | $96,762 | $96,762 | $— | $— |
| Investment securities available-for-sale | 66,387 | 66,387 | — | 66,387 | — |
| Investment securities held-to-maturity | 40,551 | 40,817 | — | 40,817 | — |
| Loans receivable, net (including impaired loans) | 574,160 | 589,844 | — | — | 589,844 |
| Accrued interest receivable | 2,558 | 2,558 | — | 2,558 | — |
| Restricted stock | 5,424 | 5,424 | — | 5,424 | — |
| Mortgage servicing rights (included in Other Assets) | 328 | 308 | — | 308 | — |
| Financial liabilities: | | | | | |
| Savings accounts | 44,714 | 44,714 | — | 44,714 | — |
| Checking and NOW accounts | 129,588 | 129,588 | — | 129,588 | — |
| Money market accounts | 177,486 | 177,486 | — | 177,486 | — |
| Certificates of deposit | 250,258 | 252,232 | — | 252,232 | — |
| FHLB advances | 118,000 | 119,946 | — | 119,946 | — |
| Derivatives (included in Other Liabilities) | 542 | 542 | — | 542 | — |
| Accrued interest payable | 427 | 427 | — | 427 | — |
| **September 30, 2015:** | | | | | |
| Financial assets: | | | | | |
| Cash and cash equivalents | $40,263 | $40,263 | $40,263 | $— | $— |
| Investment securities available-for-sale | 128,354 | 128,354 | — | 128,354 | — |
| Investment securities held-to-maturity | 57,221 | 56,825 | — | 56,825 | — |
| Loans receivable, net | 391,307 | 400,305 | — | — | 400,305 |
| Accrued interest receivable | 2,484 | 2,484 | — | 2,484 | — |
| Restricted stock | 4,765 | 4,765 | — | 4,765 | — |
| Mortgage servicing rights | 401 | 416 | — | 416 | — |
| Financial liabilities: | | | | | |
| Savings accounts | 45,189 | 45,189 | — | 45,189 | |
| Checking and NOW accounts | 109,907 | 109,907 | — | 109,907 | — |
| Money market accounts | 108,706 | 108,706 | — | 108,706 | — |
| Certificates of deposit | 201,720 | 203,257 | — | 203,257 | — |
| FHLB advances | 103,000 | 104,889 | — | 104,889 | — |

| | | | | | |
|---|---|---|---|---|---|
| Derivatives | 348 | 348 | — | 348 | — |
| Accrued interest payable | 396 | 396 | — | 396 | — |

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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 13 - Income Taxes (As Restated)**

In accordance with ASC Topic 740, the Company evaluates on a quarterly basis, all evidence, both positive and negative, to determine whether, based on the weight of that evidence, a valuation allowance for DTAs is needed. In conducting this evaluation, management explores all possible sources of taxable income available under existing tax laws to realize the net deferred tax asset beginning with the most objectively verifiable evidence first, including available carry back claims and viable tax planning strategies. If needed, management will look to future taxable income as a potential source. Management reviews the Company's current financial position and its results of operations for the current and preceding years. That historical information is supplemented by all currently available information about future years. The Company understands that projections about future performance are subjective.

In accordance with ASC Topic 740, the Company considered prudent and feasible tax-planning strategies available at September 30, 2016 that, if implemented, could prevent an operating loss or tax credit carry-forward from expiring unused and could result in realization of the existing DTA. The Company has no present intention to implement such strategies; however, in the event that the Company determined future earnings would not be sufficient to realize the deferred tax asset, the Company has the ability to realize a portion of DTA through tax strategies such as: selling available-for-sale securities in a gain position from the investment portfolio, surrendering BOLI policies, and selling loans in a gain position from the loan portfolio, as well as sales or sale/leaseback of branch offices/office buildings to recognize built-in gains.

Deferred income taxes at September 30, 2016 and 2015 were as follows:

| | September 30, | |
|---|---|---|
| | 2016 | 2015 |
| | (In thousands) | |
| Deferred Tax Assets: | | |
| Unrealized loss on investments available for sale | $— | $383 |
| Allowance for loan losses | 3,299 | 2,985 |
| Non-accrual interest | 56 | 98 |
| Write-down of real estate owned | — | 106 |
| Alternative minimum tax (AMT) credit carryover | 287 | 128 |
| Low-income housing tax credit carryover | 217 | 337 |
| Supplement Employer Retirement Plan | 412 | 455 |
| Charitable contributions | 61 | 36 |
| Depreciation | 60 | 205 |
| Federal net operating loss | 4,344 | 6,375 |
| Other | 651 | 338 |
| Total Deferred Tax Assets | 9,387 | 11,446 |
| Valuation allowance for DTA | (61 ) | (8,043 ) |
| Total Deferred Tax Assets, Net of Valuation Allowance | $9,326 | $3,403 |
| Deferred Tax Liabilities: | | |

| | | |
|---|---|---|
| State net operating income | — | (187 ) |
| Unrealized gain on investments available-for-sale | (152 ) | — |
| Mortgage servicing rights | (112 ) | (136 ) |
| Other | (235 ) | (206 ) |
| Total Deferred Tax Liabilities | (499 ) | (529 ) |
| Deferred Tax Assets, Net | $8,827 | $2,874 |

Of these DTA, the carryforward periods for certain tax attributes are as follows:

Gross federal net operating loss carryforwards of $12.7 million (net DTA of $4.3 million) to expire in the fiscal year ending September 30, 2031;

Low income housing credit carryforwards of $217,000 to expire in the fiscal years ending September 30, 2030 and 2031;

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 13 – Income Taxes (Continued) (As Restated)**

AMT credit carryforward has no expiration date; and

Gross charitable contributions carryforwards of $180,000 (net DTA of $61,000) to expire in the fiscal year ending September 30, 2018.

Income tax expense for the years ended September 30, 2016, 2015 and 2014 was comprised of the following:

| | September 30, | | |
|---|---|---|---|
| | 2016 | 2015 | 2014 |
| | (In thousands) | | |
| Federal: | | | |
| Current | $142 | $65 | $— |
| Deferred | (6,316) | (1,035) | (367) |
| | (6,174) | (970) | (367) |
| State, current | — | — | — |
| | $(6,174) | $(970) | $(367) |

The following reconciliation between federal income tax at the statutory rate of 34% and the actual income tax expense (benefit) recorded on income (loss) before income taxes for the years ended September 30, 2016, 2015 and 2014:

| | September 30, | | |
|---|---|---|---|
| | 2016 | 2015 | 2014 |
| | (Dollars in thousands) | | |
| At federal statutory rate at 34% | $2,032 | $1,257 | $— |
| Adjustments resulting from: | | | |
| Tax-exempt interest | (265) | (186) | — |
| Earnings on bank-owned life insurance | (176) | (231) | — |
| Federal tax on cash surrender of BOLI | — | — | 21 |
| DTA valuation allowance | (8,007) | (2,031) | (388) |
| Other | 242 | 221 | — |
| | $(6,174) | $(970) | $(367) |
| Effective tax rate | (103.3)% | (26.2)% | (106.7)% |

It is the Company’s policy to provide for uncertain tax positions and the related interest and penalties based upon management’s assessment of whether a tax benefit is more like than not to be sustained upon examination by tax authorities. As of September 30, 2016 and 2015, there were no material uncertain tax positions related to federal and state income tax matters. The Company is currently open to audit under the statute of limitation by the Internal Revenue Service and state taxing authorities for the years ended September 30, 2013 to September 30, 2016.

The Small Business Job Protection Act of 1996 provides for the repeal of the tax bad debt deduction computed under the percentage-of-taxable-income method. Upon repeal, the Company was required to recapture into income, over a six-year period, the portion of its tax bad debt reserves that exceeds its base year reserves (i.e., tax reserves for tax years beginning before 1988). The base year tax reserves, which may be subject to recapture if the Company ceases to qualify as a bank for federal income tax purposes, are restricted with respect to certain distributions and have been treated as a permanent tax difference.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 14 - Leases**

Pursuant to the terms of non-cancelable operating lease agreements expiring in September 2030, pertaining to Company property, future minimum rent commitments are (In thousands):

| | |
|---|---|
| Years ending September 30: | |
| 2017 | $385 |
| 2018 | 429 |
| 2019 | 431 |
| 2020 | 434 |
| 2021 | 466 |
| Thereafter | 2,225 |
| | $4,370 |

The Company receives rents from the lease of office and residential space owned by the Company. Future minimum rental commitments under these leases are (In thousands):

| | |
|---|---|
| Years ending September 30: | |
| 2017 | $133 |
| 2018 | 22 |
| 2019 | — |
| 2020 | — |
| 2021 | — |
| | $155 |

**Note 15 - Commitments and Contingencies**

The Company is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit, unused lines of credit and standby letters of credit. Such commitments involve, to varying degrees, elements of credit, and interest rate risk in excess of the amount recognized in the statements of financial condition.

The Company's 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. The Company uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments.

Letters of credit are conditional commitments issued by the Company guaranteeing payments of drafts in accordance with the terms of the letter of credit agreements. Standby letters of credit are conditional commitments issued by the Company to guarantee the performance of a customer to a third party. Collateral may be required to support letters of credit based upon management's evaluation of the creditworthiness of each customer. The credit risk involved in issuing letters of credit is substantially the same as that involved in extending loan facilities to customers. Most letters of credit expire within one year. At September 30, 2016 and 2015, the uncollateralized portion of the letters of credit extended by the Company was approximately $1.9 million and $566,000, respectively. The current amount of the liability for guarantees under letters of credit was not material as of September 30, 2016 or 2015.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 15 – Commitments and Contingencies (Continued)**

At September 30, 2016 and 2015, the following financial instruments were outstanding whose contract amounts represent credit risk:

| | September 30, | |
|---|---|---|
| | 2016 | 2015 |
| | (In thousands) | |
| Commitments to extend credit: | | |
| Future loan commitments | $97,566 | $26,849 |
| Undisbursed construction loans | 33,135 | 14,187 |
| Undisbursed home equity lines of credit | 25,270 | 27,074 |
| Undisbursed commercial lines of credit | 22,272 | 20,325 |
| Undisbursed commercial unsecured lines of credit | 26,395 | 5,275 |
| Overdraft protection lines | 850 | 840 |
| Standby letters of credit | 1,927 | 566 |
| Total Commitments | $207,415 | $95,116 |

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. The Company evaluates each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Company upon extension of credit, is based on management's credit evaluation. Collateral held varies but generally includes personal or commercial real estate.

Unfunded commitments under commercial lines of credit are collateralized except for the overdraft protection lines of credit and commercial unsecured lines of credit. The amount of collateral obtained is based on management's credit evaluation, and generally includes personal or commercial real estate.

Various legal claims arise from time to time in the normal course of business which, in the opinion of management, will have no material effect on the Company's consolidated financial statements.

**Note 16 - Regulatory Matters (As Restated)**

The Bank is subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of the Bank's assets, liabilities and certain off-balance sheet items as calculated under regulatory accounting practices. The Bank's capital amounts and classifications are also subject to qualitative judgments by the regulators about components, risk-weightings and other factors.

In July of 2013, the respective U.S. federal banking agencies issued final rules implementing Basel III and the Dodd-Frank Act capital requirements to be fully phased in on a global basis on January 1, 2019. The new regulations establish a new tangible common equity capital requirement, increase the minimum requirement for the current Tier 1 risk-weighted asset ("RWA") ratio, phase out certain kinds of intangibles treated as capital and certain types of instruments and change the risk weightings of certain assets used to determine required capital ratios. The new common equity Tier 1 capital component requires capital of the highest quality – predominantly composed of retained earnings and common stock instruments. For community banks such as Malvern Federal Savings Bank, a common equity Tier 1 capital ratio of 4.5% became effective on January 1, 2015. The new capital rules also increased the minimum Tier 1 capital ratio from 4.0% to 6.0% beginning on January 1, 2015. The rules also establish a capital conservation buffer of 2.5% above the new regulatory minimum capital requirements, which must consist entirely of common equity Tier 1 capital and would result in the following minimum ratios: (1) a common equity Tier 1 capital ratio of 7.0%, (2) a Tier 1 capital ratio of 8.5%, and (3) a total capital ratio of 10.5%. The new capital conservation buffer requirement was phased in beginning in January 2016 at 0.625% of risk-weighted assets and will increase by that amount each year until fully implemented in January 2019. An institution is also subject to limitations on paying dividends, engaging in share repurchases, and paying discretionary bonuses if its capital level falls below the buffer amount. These limitations establish a maximum percentage of eligible retained income that could be utilized for such actions.

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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 16 - Regulatory Matters – (continued) (As Restated)**

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the table below) of tangible and core capital (as defined in the regulations) to total adjusted tangible assets (as defined) and of risk-based capital (as defined) to risk-weighted assets (as defined).

As of September 30, 2016, the Company's and the Bank's current capital levels exceed the required capital amounts to be considered "well capitalized" and we believe they also meet the fully-phased in minimum capital requirements, including the related capital conservation buffers, as required by the Basel III capital rules.

The following table summarizes the Company's compliance with applicable regulatory capital requirements as of September 30, 2016:

| | **Actual** | | **For Capital Adequacy Purposes** | | **To Be Well Capitalized Under Prompt Corrective Action Provisions** | |
|---|---|---|---|---|---|---|
| **(Dollars in thousands)** | **Capital Amount** | **Ratio** | **Capital Amount** | **Ratio** | **Capital Amount** | **Ratio** |
| **As of September 30, 2016:** | | | | | | |
| Tier 1 Leverage (Core) Capital (to average assets) | $91,876 | 11.64 % | $ 31,561 | 4.00 % | $ 39,452 | 5.00 % |
| Common Equity Tier 1 Capital (to risk weighted assets) | 91,876 | 15.37 % | 26,894 | 4.50 % | 38,847 | 6.50 % |
| Tier 1 Capital (to risk weighted assets) | 91,876 | 15.37 % | 35,859 | 6.00 % | 47,812 | 8.00 % |
| Total Risk Based Capital (to risk weighted assets) | 97,372 | 16.29 % | 47,812 | 8.00 % | 59,765 | 10.00 % |

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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 16 - Regulatory Matters – (continued) (As Restated)**

The following table summarizes the Bank's compliance with applicable regulatory capital requirements as of September 30, 2016 and 2015:

| (Dollars in thousands) | Actual | | For Capital Adequacy Purposes | | To Be Well Capitalized Under Prompt Corrective Action Provisions | |
|---|---|---|---|---|---|---|
| | Capital Amount | Ratio | Capital Amount | Ratio | Capital Amount | Ratio |
| As of September 30, 2016: | | | | | | |
| Tier 1 Leverage (to average assets) | $86,596 | 10.98% | $ 31,533 | 4.00 % | $39,417 | 5.00 % |
| Common Equity Tier 1 Capital (to risk weighted assets) | 86,596 | 14.50% | 26,875 | 4.50 % | 38,820 | 6.50 % |
| Tier 1 Capital (to risk weighted assets) | 86,596 | 14.50% | 35,834 | 6.00 % | 47,779 | 8.00 % |
| Total Capital (to risk weighted assets) | 92,092 | 15.42% | 47,779 | 8.00 % | 59,723 | 10.00 % |
| As of September 30, 2015: | | | | | | |
| Tier 1 Leverage (to average assets) | $70,388 | 11.01% | $ 25,573 | 4.00 % | $31,966 | 5.00 % |
| Common Equity Tier 1 Capital (to risk weighted assets) | 70,388 | 16.21% | 19,538 | 4.50 % | 28,222 | 6.50 % |
| Tier 1 Capital (to risk weighted assets) | 70,388 | 16.21% | 26,051 | 6.00 % | 34,734 | 8.00 % |
| Total Capital (to risk weighted assets) | 75,117 | 17.30% | 34,734 | 8.00 % | 43,418 | 10.00 % |

The following table presents a reconciliation of the Bank's equity determined using accounting principles generally accepted in the United States of America ("US GAAP") and its regulatory capital amounts as of September 30, 2016 and 2015:

| September 30, 2016 | 2015 |
|---|---|
| (In thousands) | |

| | | | | | |
|---|---|---|---|---|---|
| Bank GAAP equity | $ | 90,877 | | $ | 69,309 |
| Disallowed portion of deferred tax asset | | (4,344 | ) | | — |
| Net unrealized gain on securities available for sale, net of income taxes | | (294 | ) | | 743 |
| Net unrealized gain on derivatives, net of income taxes | | 357 | | | 336 |
| Tangible Capital, Core Capital and Tier 1 Capital | | 86,596 | | | 70,388 |
| Allowance for loan losses | | 5,496 | | | 4,729 |
| Total Risk-Based Capital | $ | 92,092 | | $ | 75,117 |

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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 17 – Comprehensive Income (Loss)**

The components of accumulated other comprehensive (loss) included in shareholders' equity are as follows:

| | September 30, | | |
|---|---|---|---|
| | 2016 | 2015 | 2014 |
| | (In thousands) | | |
| Net unrealized holding gains (losses) on available-for-sale securities | $447 | $(1,011) | $(2,736) |
| Tax effect | (152) | 344 | 931 |
| Net of tax amount | 295 | (667) | (1,805) |
| Net unrealized holding losses on securities available-for-sale transferred to held-to-maturity | — | (115) | — |
| Tax effect | — | 39 | — |
| Net of tax amount | — | (76) | — |
| Fair value adjustment on derivatives | (542) | (348) | — |
| Tax effect | 184 | 12 | — |
| Net of tax amount | (358) | (336) | — |
| Total accumulated other comprehensive loss | $(63) | $(1,079) | $(1,805) |

Other comprehensive income and related tax effects are presented in the following table:

| | Year Ended September 30, | | |
|---|---|---|---|
| | 2016 | 2015 | 2014 |
| | (In thousands) | | |
| Net unrealized holding gains (losses) on available-for-sale securities | $2,128 | $2,120 | $1,419 |
| Net realized gain on securities available-for-sale | (565) | (515) | (83) |
| Amortization of unrealized holding losses on securities available-for-sale transferred to held-to-maturity | 9 | 5 | — |
| Fair value adjustment on derivatives | (194) | (348) | — |
| Other comprehensive income before taxes | 1,378 | 1,262 | 1,336 |

| | | | |
|---|---|---|---|
| Tax effect | (362 ) | (536 ) | (453 ) |
| Total comprehensive income | $1,016 | $726 | $883 |

**Note 18 – Equity Based Incentive Compensation Plan**

The Company maintains the Malvern Bancorp, Inc. 2014 Long-Term Incentive Compensation Plan (the “2014 Plan”), which permits the grant of long-term incentive and other stock and cash awards. The purpose of the 2014 Plan is to promote the success of the Company and the Bank by providing incentives to officers, employees and directors of the Company and the Bank that will link their personal interests to the financial success of the Company and to growth in shareholder value. The maximum total number of shares of the Company’s common stock available for grants under the 2014 Plan is 400,000. As of September 30, 2016, there were 393,070 remaining shares available for future grants.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 18 - Equity Based Incentive Compensation Plan – (continued)**

Restricted stock and option awards granted during fiscal 2016 vest in 20% increments beginning on the one year anniversary of the grant date, and accelerate upon a change in control of the Company. The options generally expire ten years from the date of grant. All issuances are subject to forfeiture if the recipient leaves or is terminated prior to the awards vesting. Shares of restricted stock have the same dividend and voting rights as common stock while options do not.

All awards are issued at fair value of the underlying shares at the grant date. The Company expenses the cost of the awards, which is determined to be the fair market value of the awards at the date of grant.

No options were granted in fiscal 2015 or 2014. In fiscal 2016, stock options covering 5,000 shares of common stock were granted. Total compensation expense related to options granted under the 2014 Plan was $3,000 for fiscal 2016 and zero for fiscal 2015 and 2014, respectively.

During fiscal 2016, 2,240 shares of restricted stock were awarded and 310 of those shares were forfeited. During fiscal 2015 and 2014 no shares of restricted stock were awarded. The compensation expense related to restricted stock awards was approximately $5,000 for fiscal 2016 and zero in fiscal 2015 and 2014, respectively.

Stock-based compensation expense for the cost of the awards granted is based on the grant-date fair value. For stock option awards, the fair value is estimated at the date of grant using the Black-Scholes option-pricing model. This model requires the input of highly subjective assumptions, changes to which can materially affect the fair value estimate. Additionally, there may be other factors that would otherwise have a significant effect on the value of employee stock options granted but are not considered by the model. Accordingly, while management believes that the Black-Scholes option-pricing model provides a reasonable estimate of fair value, the model does not necessarily provide the best single measure of fair value for the Company’s employee stock options.

The assumptions used in determining the fair value of stock option grants for the year ended September 30, 2016 are as follows:

| | |
|---|---|
| Weighted average fair value of awards | $5.15 |

| | | |
|---|---|---|
| Risk-free rate | 1.45 | % |
| Dividend yield | — | % |
| Volatility | 28.88 | % |
| Expected life | 6.5 years | |

The following is a summary of currently outstanding options at September 30, 2016:

| | Shares | Weighted Average Exercise Price | **Weighted Average Remaining Contractual Term (In Years)** | **Aggregate Intrinsic Value** |
|---|---|---|---|---|
| Outstanding, beginning of year | — | | | |
| Granted | 5,000 | $ 16.02 | | |
| Exercised | — | — | | |
| Forfeited/cancelled/expired | — | — | | |
| Outstanding, end of year | 5,000 | $ 16.02 | 9.498 | $ 1,900 |
| Vested and expected to vest, end of year | 5,000 | $ 16.02 | 9.498 | $ 1,900 |

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 18 - Equity Based Incentive Compensation Plan – (continued)**

The table below summarizes the activity for the Company's restricted stock outstanding at September 30, 2016:

| | Shares | Weighted Average Fair Value |
|---|---|---|
| Outstanding, beginning of year | — | |
| Granted | 2,240 | $ 17.40 |
| Vested | — | — |
| Forfeited/cancelled/expired | (310 ) | 17.40 |
| Outstanding, end of year | 1,930 | $ 17.40 |

As of September 30, 2016, there was $29,000 of total unrecognized compensation cost related to nonvested shares of restricted stock granted under the Plan. The cost is expected to be recognized over a weighted average period of 9.25 years.

**Note 19 – Condensed Financial Information - Parent Company Only (As Restated)**

**Condensed Statements of Financial Condition**

| | September 30, | |
|---|---|---|
| | 2016 | 2015 |
| | (In thousands) | |
| Assets | | |
| Cash and Cash Equivalents | $3,192 | $5,325 |
| Investment in subsidiaries | 90,877 | 69,309 |
| Investment securities held to maturity, (fair value at $5,666) | — | 5,762 |
| Loans receivable, net | 1,709 | 1,842 |
| Other assets | 418 | 532 |
| Total Assets | $96,196 | $82,770 |
| Liabilities | | |
| Accounts payable | $39 | $21 |

| | | |
|---|---|---|
| Shareholders' Equity | 96,157 | 82,749 |
| Total Liabilities and Shareholders' Equity | $96,196 | $82,770 |

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 19 – Condensed Financial Information - Parent Company Only (Continued) (As Restated)**

**Condensed Statements of Operations**

| | Year Ended September 30, | | |
|---|---|---|---|
| | 2016 | 2015 | 2014 |
| | (In thousands) | | |
| Income | | | |
| Interest income | $116 | $196 | $254 |
| Total Interest Income | 116 | 196 | 254 |
| Expense | | | |
| Other operating expenses | 189 | 251 | 331 |
| Total Other Expenses | 189 | 251 | 331 |
| Loss before Equity in Undistributed Net Income of Subsidiaries and Income Tax Expense | (73) | (55) | (77) |
| Equity in Undistributed Net Income of Subsidiaries | 12,334 | 4,723 | 788 |
| Income tax expense | 111 | — | — |
| Net Income | $12,150 | $4,668 | $711 |

**Condensed Statements of Comprehensive Income**

| | Year Ended September 30, | | |
|---|---|---|---|
| (In thousands) | 2016 | 2015 | 2014 |
| Net Income | $12,150 | $4,668 | $711 |
| Other Comprehensive Income, Net of Tax: | | | |
| Unrealized holding gains (losses) on available-for-sale securities | 2,128 | 2,120 | 1,419 |
| Tax effect | (723) | (721) | (482) |
| Net of tax amount | 1,405 | 1,399 | 937 |
| Reclassification adjustment for net gains arising during the period(1) | (565) | (515) | (83) |
| Tax effect | 192 | 175 | 29 |
| Net of tax amount | (373) | (340) | (54) |
| Accretion of unrealized holding losses on securities transferred from available-for-sale to held-to-maturity(2) | 9 | 5 | — |
| Tax effect | (3) | (2) | — |
| Net of tax amount | 6 | 3 | — |
| Fair value adjustment on derivatives | (194) | (348) | — |
| Tax effect | 172 | 12 | — |

| | | | |
|---|---|---|---|
| Net of tax amount | (22 ) | (336 ) | — |
| Total other comprehensive income | 1,016 | 726 | 883 |
| Total comprehensive income | $13,166 | $5,394 | $1,594 |

(1) Amounts are included in net gain on sales of securities on the Consolidated Statements of Operations in total other income.

(2) Amounts are included in interest and dividends on investment securities on the Consolidated Statements of Operations.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 19 – Condensed Financial Information - Parent Company Only (Continued) (As Restated)**

**Condensed Statements of Cash Flows**

| | Year Ended September 30, | | |
|---|---|---|---|
| | 2016 | 2015 | 2014 |
| | (In thousands) | | |
| Cash Flows from Operating Activities | | | |
| Net income | $12,150 | $4,668 | $711 |
| Undistributed net income of subsidiaries | (12,334) | (4,722) | (788) |
| Deferred income taxes, net | — | 84 | 197 |
| ESOP shares committed to be released | 242 | 195 | 160 |
| Increase (decrease) in accounts payable | 18 | (27) | (14) |
| (Increase) decrease in other assets | (2,629) | 239 | 227 |
| Net Cash (Used in) Provided by Operating Activities | (2,553) | 437 | 493 |
| Cash Flows from Investing Activities | | | |
| Proceeds from maturities and principal collection on investments available for sale, net | — | — | 422 |
| Proceeds from maturities and principal collection on investments held to maturity | 287 | 511 | — |
| Purchases of investment securities | — | — | (992) |
| Calls, sales of investment securities | — | 1,812 | — |
| Loan originations and principal collections, net | 133 | 127 | 121 |
| Net Cash Provided by (Used in) Investing Activities | 420 | 2,450 | (449) |
| Net (Decrease) Increase in Cash and Cash Equivalents | (2,133) | 2,887 | 44 |
| Cash and Cash Equivalents - Beginning | 5,325 | 2,438 | 2,394 |
| Cash and Cash Equivalents - Ending | $3,192 | $5,325 | $2,438 |
| | | | |
| Supplementary Cash Flows Information | | | |
| Non-cash transfer of investment securities from Parent Company to Bank | $5,475 | $— | $— |

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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 20 – Quarterly Financial Information of Malvern Bancorp Inc. (Unuadited) (As Restated)**

The following tables are a summary of certain quarterly financial data for the fiscal years ended September 30, 2016 and 2015.

| | 2016 | | | |
|---|---|---|---|---|
| | **4th Quarter** | **3rd Quarter** | **2nd Quarter** | **1st Quarter** |
| | (Dollars in thousands, except per share data) | | | |
| Total Interest and Dividend Income | 6,817 | $6,530 | $6,210 | $5,687 |
| Total Interest Expense | 1,796 | 1,750 | 1,710 | 1,476 |
| Net Interest Income | 5,021 | 4,780 | 4,500 | 4,211 |
| Provision for Loan Losses | 100 | 472 | 375 | — |
| Total Other Income | 615 | 659 | 501 | 558 |
| Total Other Expenses | 3,759 | 3,378 | 3,360 | 3,425 |
| Income before income tax benefit | 1,777 | 1,589 | 1,266 | 1,344 |
| Income tax benefit | (6,174) | — | — | — |
| Net Income | $7,951 | $1,589 | $1,266 | $1,344 |
| | | | | |
| Earnings Per Common Share: | | | | |
| Basic | $1.24 | $0.25 | $0.20 | $0.21 |
| Diluted | $1.24 | $0.25 | $0.20 | n/a |
| | | | | |
| Weighted Average Common Shares Outstanding | | | | |
| Basic | 6,415,049 | 6,411,766 | 6,408,167 | 6,402,332 |
| Diluted | 6,415,207 | 6,411,804 | 6,408,167 | n/a |

| | 2015 | | | |
|---|---|---|---|---|
| | **4th Quarter** | **3rd Quarter** | **2nd Quarter** | **1st Quarter** |
| | (Dollars in thousands, except per share data) | | | |
| Total Interest and Dividend Income | 5,344 | $5,139 | $5,166 | $4,813 |
| Total Interest Expense | 1,365 | 1,301 | 1,330 | 1,252 |
| Net Interest Income | 3,979 | 3,838 | 3,836 | 3,561 |
| Provision for Loan Losses | — | — | — | 90 |
| Total Other Income | 639 | 640 | 745 | 511 |
| Total Other Expenses | 3,454 | 3,273 | 3,573 | 3,661 |
| Income before income tax benefit | 1,164 | 1,205 | 1,008 | 321 |
| Income tax benefit | (341) | 882 | (1,081) | (430) |
| Net Income | $1,505 | $323 | $2,089 | $751 |
| | | | | |
| Earnings Per Common Share: | | | | |

| | | | | |
|---|---|---|---|---|
| Basic | $0.23 | $0.05 | $0.33 | $0.12 |
| Diluted | n/a | n/a | n/a | n/a |
| | | | | |
| Weighted Average Common Shares Outstanding | | | | |
| Basic | 6,398,720 | 6,395,126 | 6,391,521 | 6,387,932 |
| Diluted | n/a | n/a | n/a | n/a |

**Item 9A. Controls and Procedures.**

**Evaluation of Disclosure Controls and Procedures**

Our management evaluated, with the participation of our Chief Executive Officer and Chief Financial Officer, the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) as of September 30, 2016. Based on such evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures were not effective as of September 30, 2016 because of the material weakness described below.

**Management's Annual Report on Internal Control over Financial Reporting**

Management of the Company is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Securities and Exchange Act of 1934 Rules 13(a)-15(f). The Company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with U.S. generally accepted accounting principles. An adequate system of internal control encompasses the processes and procedures that have been established by management to, among other things:

Maintain records that accurately reflect the Company's transactions;

Prepare financial statements and footnote disclosures in accordance with GAAP that can be relied upon by external users;

Prevent and detect unauthorized acquisition, use or disposition of the Company's assets that could have a material effect of the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, the application of any evaluation of effectiveness to future periods is subject to the risk that controls may become inadequate because of changes in conditions, or that compliance with the policies or procedures may deteriorate.

As we previously disclosed, in November 21, 2017, we were advised by BDO USA, LLP ("BDO"), our independent registered public accounting firm, that BDO had concluded that a material weakness in our internal controls over financial reporting existed, and that BDO's report on the effectiveness of the Company's internal control over financial reporting as of September 30, 2016 in Item 9A of the Company's fiscal 2016 10-K that the Company' internal control over financial reporting was effective as of September 30, 2016, should no longer be relied upon. BDO also informed us at that time that BDO's audit report on the Company's consolidated financial statements as of September 30, 2016 and 2015, and for each of the years in the two year period ended September 30, 2016, and BDO's completed interim reviews of the Company's consolidated interim financial statements as of and for the periods ended December 31, 2016, March 31, 2017 and June 30, 2017 (collectively, the "Specified Financial Statements"), should no longer be relied upon. In this Amendment to our fiscal 2016 Annual Report on Form 10-K we are restating the annual consolidated financial statements referred to above. We will also amend our 10-Qs for the first three quarters of fiscal 2017, which will contain the restated consolidated interim financial statements referred to above.

The matters described above related to our income tax account balances. Management has implemented a more formal review and documentation process around the accounting for income tax which management believes will strengthen the Company's overall internal control over financial reporting.

Management, including the Chief Executive Officer and Chief Financial Officer, conducted a review, evaluation and testing of the effectiveness of the Company's controls over financial reporting based on the 2013 framework in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO"). Management concluded that because of the matters described above, the Company's internal control over financial reporting was not effective as of September 30, 2016. Management believes that the material weakness described above has been remediated as of the filing of this Amendment to our fiscal 2016 Annual Report on Form 10-K.

The effectiveness of our internal control over financial reporting as of September 30, 2016, has been audited by BDO, our independent registered public accounting firm as stated in their report which appears herein.

**Remediation of Prior Material Weakness**

Item 9A of the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2015, indicated that management's review of the Company's internal control over financial reporting identified certain deficiencies which, in the aggregate, constituted a material weakness at September 30, 2015, and described the Company's remediation plan to address such deficiencies. An internal control material weakness is a significant deficiency, or combination of significant deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the annual or interim financial statements will not be prevented or detected on a timely basis. The Company's remediation efforts included: enhancement of the Company's procedures with respect to documentation and identification of troubled debt restructurings; enhancement of the Company's analysis and review process with respect to impaired loans; and re-evaluation of its policies and procedures regarding use of real estate appraisers who are not on the Company's list of approved appraisers. During the quarter ended December 31, 2015, the Company commenced the remediation efforts described in Item 9A of the fiscal 2015 Annual Report on Form 10-K and such efforts continued through the quarter ended September 30, 2016. As indicated above, after completing its assessment of the Company's internal control over financial reporting as of September 30, 2016, management concluded that the Company had remediated the previously identified weaknesses.

**Changes in Internal Control over Financial Reporting**

Other than the changes described above, no change in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15(d)-15(f) under the Securities Exchange Act of 1934) occurred during the fourth quarter of fiscal 2016 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

**Report of Independent Registered Public Accounting Firm**

To the Board of Directors and Shareholders

Malvern Bancorp, Inc. and Subsidiaries

Paoli, Pennsylvania

We have audited Malvern Bancorp Inc. and subsidiaries (the "Company") internal control over financial reporting as of September 30, 2016, based on criteria established in *Internal Control – Integrated Framework (2013)* issued by the

Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). Malvern Bancorp Inc.'s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Item 9A, "Management's Annual Report on Internal Control over Financial Reporting". Our responsibility is to express an opinion on the company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our report dated December 13, 2016, we expressed an unqualified opinion on the effectiveness of internal control over financial reporting as of September 30, 2016. Subsequent to December 13, 2016, Malvern Bancorp, Inc. identified an error in its annual financial statements for 2016 and 2015, requiring restatement of such financial statements. Management revised its assessment of internal control over financial reporting due to the identification of a material weakness, described in the following paragraph, in connection with the financial statement restatement. Accordingly, our opinion on the effectiveness of Malvern Bancorp, Inc.'s internal control over financial reporting as of September 30, 2016 expressed herein is different from that expressed in our previous report.

A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the Company's annual or interim financial statements will not be prevented or detected on a timely basis. A material weakness regarding accounting for income taxes has been identified and described in management's revised assessment. This material weakness was considered in determining the nature, timing, and extent of audit tests applied in our audit of the 2016 and 2015 financial statements (as restated).

In our opinion, Malvern Bancorp, Inc. did not maintain, in all material respects, effective internal control over financial reporting as of September 30, 2016, based on the COSO criteria.

We do not express an opinion or any other form of assurance on management's statements referring to any corrective actions to be taken by the Company after the date of management's assessment.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated statement of financial condition of Malvern Bancorp, Inc. as of September 30, 2016 and 2015, and the related consolidated statements of operations, comprehensive income, changes in shareholders' equity, and cash flows for each of the three years in the period ended September 30, 2016 and our report dated December 13, 2016, except for Note 3 as to which the date is December 15, 2017 expressed an unqualified opinion thereon.

/s/ BDO USA, LLP

Philadelphia, Pennsylvania

December 13, 2016, except as to the effect of the material weakness which is dated as of December 15, 2017.

**PART IV.**

**Item 15. Exhibits and Financial Statement Schedules**.

(a)(1) The following financial statements are incorporated by reference from Item 8 hereof:

Report of Independent Registered Public Accounting Firm
Consolidated Statements of Financial Condition
Consolidated Statements of Operations
Consolidated Statements of Comprehensive Income (Loss)
Consolidated Statements of Changes in Shareholders' Equity
Consolidated Statements of Cash Flows
Notes to Consolidated Financial Statements

(2) All schedules are omitted because they are not required or applicable, or the required information is shown in the consolidated financial statements or the notes thereto.

(3) Exhibits

The following exhibits are filed as part of this Form 10-K and this list includes the Exhibit Index.

| No. | Description | Location |
|---|---|---|
| 3.1 | Articles of Incorporation of Malvern Bancorp, Inc. | (1) |
| 3.2 | Amended and Restated Bylaws of Malvern Bancorp, Inc. | (2) |
| 4.0 | Form of Stock Certificate of Malvern Bancorp, Inc. | (1) |
| 10.1 | Malvern Bancorp 2014 Long Term Incentive Plan* | (3) |
| 10.2 | Employment Agreement with Anthony C. Weagley* | (4) |
| 10.3 | Change of Control Agreement with Joseph D. Gangemi* | (5) |

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| No. | Description | Location |
|---|---|---|
| 10.4 | Change of Control Agreement with William Woolworth* | (6) |
| 10.5 | Change of Control Agreement with William Boylan | (7) |
| 23.0 | Consent of BDO USA, LLP | Filed herewith |
| 31.1 | Rule 13(a)-14(a) Certification of the Chief Executive Officer | Filed herewith |
| 31.2 | Rule 13(a)-14(a) Certification of the Chief Financial Officer | Filed herewith |
| 32.0 | Section 1350 Certification | Filed herewith |
| 101.INS | XBRL Instance Document. ** | Filed herewith |
| 101.SCH | XBRL Taxonomy Extension Schema Document.** | Filed herewith |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase Document.** | Filed herewith |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase Document.** | Filed herewith |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase Document.** | Filed herewith |
| 101.DEF | XBRL Taxonomy Extension Definitions Linkbase Document.** | Filed herewith |

* Denotes a management contract or compensatory plan or arrangement.

** Attached as Exhibit 101 to this report are the following documents formatted in XBRL (Extensible Business Reporting Language): (i) the Consolidated Statement of Financial Condition at September 30, 2016 and 2015, (ii) the Consolidated Statement of Operations for the years ended September 30, 2016, 2015 and 2014, (iii) the Consolidated Statement of Comprehensive Income (Loss) for the years ended September 30, 2016, 2015 and 2014, (iv) the Consolidated Statement of Changes in Shareholders' Equity for the years ended September 30, 2016, 2015 and 2014, (v) the Consolidated Statement of Cash Flows for the years ended September 30, 2016, 2015 and 2014 and (vi) the Notes to Condensed Consolidated Financial Statements, tagged as detailed footnote tagging.

(1) Incorporated by reference from the like-numbered exhibit included in Malvern Bancorp's registration statement on Form S-1, filed May 31, 2012 (SEC File No. 333-181798).

(2) Incorporated by reference from Exhibit 3.2 included in the Current Report on Form 8-K of Malvern Bancorp, Inc. dated as of February 17, 2016 and filed February 19, 2016 (SEC File No. 000-54835).

(3) Incorporated by reference to Appendix A of the definitive proxy statement filed by Malvern Bancorp, Inc. with the SEC on January 2, 2015 (SEC File No. 000-54835).

(4) Incorporated by reference to Exhibit 10.1 included in the Current Report on Form 8-K of Malvern Bancorp, Inc., dated as of June 23, 2016, and filed on June 24, 2016 (SEC File No. 000-54835).

(5)

Incorporated by reference to Exhibit 10.1 included in the Current Report on Form 8-K of Malvern Bancorp, Inc., dated as of May 23, 2016, and filed on May 27, 2016 (SEC File No. 000-54835).

(6) Incorporated by reference to Exhibit 10.2 included in the Current Report on Form 8-K of Malvern Bancorp, Inc., dated as of May 23, 2016, and filed on May 27, 2016 (SEC File No. 000-54835).

(b) Exhibits

The exhibits listed under (a)(3) of this Item 15 are filed herewith.

(c) Reference is made to (a)(2) of this Item 15.

(7) Filed as exhibit 10.5 to the Annual Report on Form 10-K of Malvern Bancorp, Inc., for the fiscal year ended September 30, 2016, filed with the SEC on December 14, 2016.

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**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) 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.

| | |
|---|---|
| | **MALVERN BANCORP, INC.** |
| December 15, 2017 By: | /s/ Joseph D. Gangemi |
| | Joseph D. Gangemi |
| | Senior Vice President and CFO |