

HERITAGE FINANCIAL CORP /WA/
Form 10-Q
July 27, 2007
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2007

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
Commission File Number 0-29480

HERITAGE FINANCIAL CORPORATION

(Exact name of registrant as specified in its charter)

Washington
(State or other jurisdiction of incorporation or organization)

91-1857900
(I.R.S. Employer Identification No.)

201 Fifth Avenue SW, Olympia, WA
(Address of principal executive office)

(360) 943-1500

98501
(ZIP Code)

(Registrant's telephone number, including area code)

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

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

Large accelerated filer Accelerated filer Non-accelerated filer

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the last practicable date:

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As of July 12, 2007 there were 6,640,659 common shares outstanding, with no par value, of the registrant.

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(Dollars in thousands, except for per share data)

(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
INTEREST INCOME:				
Interest and fees on loans	\$ 15,131	\$ 12,927	\$ 29,550	\$ 24,836
Taxable interest on investment securities	411	431	826	840
Nontaxable interest on investment securities	44	41	88	80
Interest on federal funds sold and interest bearing deposits	36	13	80	26
Dividends on Federal Home Loan Bank stock	5		8	
Total interest income	15,627	13,412	30,552	25,782
INTEREST EXPENSE:				
Deposits	6,013	4,189	11,627	7,788
Other borrowings	512	439	925	725
Total interest expense	6,525	4,628	12,552	8,513
Net interest income	9,102	8,784	18,000	17,269
Provision for loan losses	180	100	360	240
Net interest income after provision for loan losses	8,922	8,684	17,640	17,029
NONINTEREST INCOME:				
Gains on sales of loans, net	11	30	13	90
Brokered mortgage income	221	101	402	227
Service charges on deposits	967	826	1,821	1,564
Rental income	81	79	160	156
Merchant visa income	709	613	1,364	1,186
Other income	240	268	502	465
Total noninterest income	2,229	1,917	4,262	3,688
NONINTEREST EXPENSE:				
Salaries and employee benefits	3,672	3,714	7,509	7,119
Occupancy and equipment	1,014	989	2,104	1,978
Data processing	388	327	768	644
Marketing	174	133	263	250
Office supplies and printing	101	99	200	203
Merchant visa	568	482	1,094	926
Professional services	210	181	381	321
State and local taxes	244	200	459	392
Other expense	805	691	1,584	1,267
Total noninterest expense	7,176	6,816	14,362	13,100
Income before federal income taxes	3,975	3,785	7,540	7,617
Federal income taxes	1,348	1,250	2,540	2,517

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Net income	\$ 2,627	\$ 2,535	\$ 5,000	\$ 5,100
Earnings per share:				
Basic	\$ 0.40	\$ 0.40	\$ 0.76	\$ 0.81
Diluted	\$ 0.39	\$ 0.39	\$ 0.75	\$ 0.79
Dividends declared per share:	\$ 0.210	\$ 0.200	\$ 0.420	\$ 0.395

See Notes to Condensed Consolidated Financial Statements.

Table of Contents**HERITAGE FINANCIAL CORPORATION****CONDENSED CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION**

(Dollars in thousands)

(Unaudited)

	June 30, 2007	December 31, 2006
Assets		
Cash on hand and in banks	\$ 33,738	\$ 23,713
Interest earning deposits	4,887	2,718
Federal funds sold	4,600	
Investment securities available for sale	35,866	39,124
Investment securities held to maturity (market value of \$3,704 and \$3,861)	3,757	3,858
Loans held for sale	380	
Loans receivable	789,813	749,701
Less: Allowance for loan losses	(10,232)	(10,105)
Loans receivable, net	779,581	739,596
Other real estate owned		225
Premises and equipment, at cost, net	15,359	15,681
Federal Home Loan Bank and Federal Reserve stock, at cost	3,227	3,227
Accrued interest receivable	4,451	4,298
Prepaid expenses and other assets	3,970	4,550
Deferred federal income taxes, net	2,143	2,242
Intangible assets, net	541	580
Goodwill	13,086	13,081
Total assets	\$ 905,586	\$ 852,893
Liabilities and Stockholders Equity		
Deposits	\$ 770,801	\$ 725,921
Advances from Federal Home Loan Bank	41,778	37,167
Other borrowings	2,559	3,371
Accrued expenses and other liabilities	8,878	7,795
Total liabilities	824,016	774,254
Stockholders equity:		
Common stock, no par value per share, 15,000,000 shares authorized; 6,639,671 and 6,558,206 shares outstanding at June 30, 2007 and December 31, 2006, respectively	24,781	24,053
Unearned compensation - ESOP	(491)	(535)
Retained earnings, substantially restricted	57,860	55,647
Accumulated other comprehensive loss, net	(580)	(526)
Total stockholders equity	81,570	78,639
Commitments and contingencies		
Total liabilities and stockholders equity	\$ 905,586	\$ 852,893

See Notes to Condensed Consolidated Financial Statements.

Table of Contents**HERITAGE FINANCIAL CORPORATION****CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY FOR THE SIX MONTHS ENDED****JUNE 30, 2007 AND COMPREHENSIVE INCOME FOR THE THREE AND SIX MONTHS ENDED****JUNE 30, 2007 AND 2006**

(In Thousands)

(Unaudited)

	Number of common shares	Common stock	Unearned Compensation- ESOP	Retained earnings	Accumulated other comprehensive loss, net	Total stockholders equity
Balance at December 31, 2006	6,558	\$ 24,053	\$ (535)	\$ 55,647	\$ (526)	\$ 78,639
Stock option compensation expense		146				146
Earned ESOP shares	5	68	44			112
Earned restricted stock shares		51				51
Tax benefit on vesting of restricted stock shares		100				100
Restricted stock awards granted	21					
Restricted stock awards cancelled	(5)					
Tax benefit on dividends paid on unallocated ESOP shares and restricted stock shares		16				16
Exercise of stock options (including tax benefits from nonqualified stock options)	104	1,358				1,358
Stock repurchase	(43)	(1,011)				(1,011)
Net income				5,000		5,000
Change in fair value of securities available for sale, net of tax					(54)	(54)
Cash dividends declared				(2,787)		(2,787)