TIMBERLAND BANCORP INC
Form 10-K
December 14, 2009

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

FORM 10-K

[X] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the Fiscal Year Ended September 30, 2009 OR

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

Commission File Number: 0-23333

TIMBERLAND BANCORP, INC.

(Exact name of registrant as specified in its charter)

Washington	91-1863696
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
624 Simpson Avenue, Hoquiam, Washington	98550
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (360) 533-4747

Securities registered pursuant to Section 12(b) of the Act:

Common Stock, par value $.01 per share	The Nasdaq Stock Market LLC
(Title of Each Class)	(Name of Each Exchange on Which Registered)

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the Registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. YES _____ NO X

Indicate by check mark if the Registrant is not required to file reports pursuant to Section 13 of Section 15(d) of the Act. YES _____ NO X

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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of the Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. X

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act:

Large accelerated filer	_____	Accelerated filer	_____
Non-accelerated filer	_____	Smaller reporting company	X

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Act). YES _____ NO X

As of November 30, 2009, the Registrant had 7,045,036 shares of Common Stock issued and outstanding. The aggregate market value of the Common Stock held by nonaffiliates of the Registrant, based on the closing sales price of the Registrant's common stock as quoted on the NASDAQ Global Select Market on March 31, 2009, was $36.4 million (7,045,036 shares at $5.16). For purposes of this calculation, Common Stock held by officers and directors of the Registrant and the Timberland Bank Employee Stock Ownership Plan and Trust are considered nonaffiliates.

DOCUMENTS INCORPORATED BY REFERENCE

1. Portions of Definitive Proxy Statement for the 2010 Annual Meeting of Stockholders (Part III).

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PART I

Item 1. Business

General

Timberland Bancorp, Inc. ("Company"), a Washington corporation, was organized on September 8, 1997 for the purpose of becoming the holding company for Timberland Savings Bank, SSB ("Bank") upon the Bank's conversion from a Washington-chartered mutual savings bank to a Washington-chartered stock savings bank ("Conversion"). The Conversion was completed on January 12, 1998 through the sale and issuance of 13,225,000 shares of common stock by the Company. At September 30, 2009, the Company had total assets of $701.7 million, total deposits of $505.7 million and total shareholders' equity of $87.2 million. The Company's business activities generally are limited to passive investment activities and oversight of its investment in the Bank. Accordingly, the information set forth in this report, including consolidated financial statements and related data, relates primarily to the Bank and its subsidiary.

The Bank was established in 1915 as "Southwest Washington Savings and Loan Association." In 1935, the Bank converted from a state-chartered mutual savings and loan association to a federally chartered mutual savings and loan association, and in 1972, changed its name to "Timberland Federal Savings and Loan Association." In 1990, the Bank converted to a federally chartered mutual savings bank under the name "Timberland Savings Bank, FSB." In 1991, the Bank converted to a Washington-chartered mutual savings bank and changed its name to "Timberland Savings Bank, SSB." On December 29, 2000, the Bank changed its name to "Timberland Bank." The Bank's deposits are insured up to applicable legal limits by the Federal Deposit Insurance Corporation ("FDIC"). The Bank has been a member of the Federal Home Loan Bank ("FHLB") System since 1937. The Bank is regulated by the Washington Department of Financial Institutions, Division of Banks ("Division" or "DFI") and the FDIC.

The Bank is a community-oriented bank which has traditionally offered a variety of savings products to its retail customers while concentrating its lending activities on real estate mortgage loans. Lending activities have been focused primarily on the origination of loans secured by real estate, including an emphasis on construction loans, one- to four-family residential loans, multi-family loans, commercial real estate loans and land loans. The Bank originates adjustable-rate residential mortgage loans that do not qualify for sale in the secondary market under Federal Home Loan Mortgage Corporation ("FHLMC") guidelines. The Bank also originates commercial business loans and in 1998 established a business banking division to increase the origination of these loans.

The Company maintains a website at www.timberlandbank.com. The information contained on that website is not included as a part of, or incorporated by reference into, this Annual Report on Form 10-K. Other than an investor's own internet access charges, the Company makes available free of charge through that website the Company's Annual Report on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K, and amendments to these reports, as soon as reasonably practicable after these materials have been electronically filed with, or furnished to, the Securities and Exchange Commission ("SEC").

Recent Developments

In December 2009, the FDIC determined that the Bank required supervisory attention and agreed to terms on a pending Memorandum of Understanding, or MOU, with the Bank. The terms of the MOU restrict the Bank from certain activities, and require that the Bank obtain the prior written approval, or nonobjection, of the FDIC and/or the DFI to engage in certain activities. For additional information regarding the MOU, see "Item 1A, Risk Factors -- Risks Related to Our Business -- We are required to comply with the terms of a pending memorandum of understanding issued by the FDIC and the Division and lack of compliance could result in additional regulatory actions."

Market Area

The Bank considers Grays Harbor, Thurston, Pierce, King, Kitsap and Lewis Counties, Washington as its primary market areas. The Bank conducts operations from:

* its main office in Hoquiam (Grays Harbor County);

* five branch offices in Grays Harbor County (Ocean Shores, Montesano, Elma, and two branches in Aberdeen);

* a branch office in King County (Auburn);

* five branch offices in Pierce County (Edgewood, Puyallup, Spanaway, Tacoma, and Gig Harbor);

* five branch offices in Thurston County (Olympia, Yelm, Tumwater, and two branches in Lacey);

* two branch offices in Kitsap County (Poulsbo and Silverdale); and

* three branch offices in Lewis County (Winlock, Toledo and Chehalis).

See "Item 2. Properties."

Hoquiam, with a population of approximately 9,000, is located in Grays Harbor County which is situated along Washington State's central Pacific coast. Hoquiam is located approximately 110 miles southwest of Seattle and 145 miles northwest of Portland, Oregon.

The Bank considers its primary market area to include six submarkets: primarily rural Grays Harbor County with its historical dependence on the timber and fishing industries; Pierce, Thurston and Kitsap Counties with their dependence on state and federal government; King County with its broadly diversified economic base; and Lewis County with its dependence on retail trade, manufacturing, industrial services and local government. Each of these markets presents operating risks to the Bank. The Bank's expansion into Pierce, Thurston, King, Kitsap and Lewis Counties represents the Bank's strategy to diversify its primary market area to become less reliant on the economy of Grays Harbor County.

Grays Harbor County has a population of 71,000 according to the U.S. Census Bureau 2008 estimates and a median family income of $54,500 according to 2009 HUD estimates. The economic base in Grays Harbor has been historically dependent on the timber and fishing industries. Other industries that support the economic base are tourism, agriculture, shipping, transportation and technology. According to the Washington State Employment Security Department, the unemployment rate in Grays Harbor County increased to 11.9% at September 30, 2009 from 7.5% at September 30, 2008. The median price of a resale home in Grays Harbor County for the quarter ended September 30, 2009 decreased 13.2% to $134,500 as compared to the quarter one year prior.

The number of home sales decreased 29.5% for the quarter ended September 30, 2009 compared the same quarter one year earlier. The Bank has six branches (including its home office) located throughout the county. The recent downturn in Grays Harbor County's economy and the decline in real estate values have had a negative effect on the Bank's profitability in this market area.

Pierce County is the second most populous county in the state and has a population of 786,000 according to the U.S. Census Bureau 2008 estimates. The county's median family income is $68,100 according to 2009 HUD estimates. The economy in Pierce County is diversified with the presence of military related government employment (Fort Lewis Army Base and McChord Air Force Base), transportation and shipping employment (Port of Tacoma), and aerospace related employment (Boeing). According to the Washington State Employment Security Department, the unemployment rate for the Pierce County area increased to 9.0% at September 30, 2009 from 5.9% at September 30, 2008. The median price of a resale home in Pierce County for the quarter ended September 30, 2009 decreased 9.6% to $230,000 as compared to the quarter one year prior. The number of home sales increased 11.6% for the quarter ended

September 30, 2009 compared the same quarter one year earlier. The Bank has five branches in Pierce County and these branches have historically been responsible for a substantial portion of the Bank's construction lending activities. The recent downturn in Pierce County's economy and the decline in real estate values have had a negative effect on the Bank's profitability in this market area.

Thurston County has a population of 245,000 according to the U.S. Census Bureau 2008 estimates and a median family income of $70,000 according to 2009 HUD estimates. Thurston County is home of Washington State's capital (Olympia) and its economic base is largely driven by state government related employment. According to the Washington State Employment Security Department, the unemployment rate for the Thurston County area increased to 7.2% at September 30, 2009 from 5.2% at September 30, 2008. The median price of a resale home in Thurston County for the quarter ended September 30, 2009 decreased 3.0% to $243,100 as compared to the same quarter one year earlier. The number of home sales increased 1.5% for the quarter ended September 30, 2009 compared to the same quarter one year earlier. The Bank has five branches in Thurston County. This county has historically had a stable economic base primarily attributable to the state government presence; however the downturn in Thurston County's economy and the decline in real estate values have had a negative effect on the Bank's profitability in this market area.

Kitsap County has a population of 240,000 according to the U.S. Census Bureau 2008 estimates and a median family income of $70,900 according to 2009 HUD estimates. The Bank has two branches in Kitsap County. The economic base of Kitsap County is largely supported by military related government employment through the United States Navy. According to the Washington State Employment Security Department, the unemployment rate for the Kitsap County area increased to 7.3% at September 30, 2009 from 5.3% at September 30, 2008. The median price of a resale home in Kitsap County for the quarter ended September 30, 2009 decreased 7.4% to $249,900, as compared to the same quarter one year earlier. The number of home sales increased 14.2% for the quarter ended September 30, 2009 compared to the same quarter one year earlier. The recent downturn in Kitsap County's economy and the decline in real estate values have had a negative effect on the Bank's profitability in this market area.

King County is the most populous county in the state and has a population of 1.9 million according to the U.S. Census Bureau 2008 estimates. The Bank has one branch in King County. The county's median family income is $84,300 according to 2009 HUD estimates. King County's economic base is diversified with many industries including shipping, transportation, aerospace (Boeing), computer technology and biotech industries. According to the Washington State Employment Security Department, the unemployment rate for the King County area increased to 8.8% at September 30, 2009 from 4.6% at September 30, 2008. The median price of a resale home in King County for the quarter ended September 30, 2009 decreased 10.5% to $382,000, as compared to the same quarter one year earlier. The number of home sales increased 14.2% for the quarter ended September 30, 2009 compared to the same quarter one year earlier. The recent downturn in King County's economy and the decline in real estate values have had a negative effect on the Bank's profitability in this market area.

Lewis County has a population of 74,000 according to the U.S. Census Bureau 2008 estimates and a median family income of $54,000 according to 2009 HUD estimates. The economic base in Lewis County is supported by manufacturing, retail trade, local government and industrial services. According to the Washington State Employment Security Department, the unemployment rate in Lewis County increased to 12.1% at September 30, 2009 from 7.7% at September 30, 2008. The median price of a resale home in Lewis County for the quarter ended September 30, 2009 decreased 6.7% to $163,300, as compared to the same quarter one year earlier. The number of home sales increased 16.7% for the quarter ended September 30, 2009 compared to the same quarter one year earlier. The Bank currently has three branches located in Lewis County after it consolidated its loan production office into a new full service branch in May 2009. The recent downturn in Lewis County's economy and the decline in real estate values have had a negative effect on the Bank's profitability in this market area.

Lending Activities

General. Historically, the principal lending activity of the Bank has consisted of the origination of loans secured by first mortgages on owner-occupied, one- to four-family residences, loans secured by commercial real estate and loans for the construction of one- to four-family residences. The Bank's net loans receivable, including loans held

for sale, totaled $547.2 million at September 30, 2009, representing 77.9% of consolidated total assets, and at that date construction and land development loans (including undisbursed loans in process), and loans secured by commercial properties were $327.9 million, or 55.1%, of total loans. Construction and land development loans and commercial real estate loans typically have higher rates of return than one- to four-family loans; however, they also present a higher degree of risk. See "- Lending Activities - Construction and Land Development Lending" and "- Lending Activities - Commercial Real Estate Lending."

The Bank's internal loan policy limits the maximum amount of loans to one borrower to 25% of its Tier 1 capital. At September 30, 2009, the maximum amount which the Bank could have lent to any one borrower and the borrower's related entities was approximately $17.0 million under this policy. At

September 30, 2009, the largest amount outstanding to any one borrower and the borrower's related entities was $11.8 million (including $371,000 in undisbursed loans in process balance). These loans represent two condominium construction projects, several one- to four-family speculative construction projects, and commercial real estate holdings. All of the loans are secured by projects located in Grays Harbor County, except for one of the condominium construction projects which is located in Clatsop County, Oregon. These loans were performing according to the required loan repayment terms at September 30, 2009. The next largest amount outstanding to any one borrower and the borrower's related entities was $11.5 million (including $3.6 million in undisbursed loans in process balance.) These loans were secured by commercial buildings being constructed in Pierce County and a land parcel, all of which were performing according to loan repayment terms at September 30, 2009.

Loan Portfolio Analysis. The following table sets forth the composition of the Bank's loan portfolio by type of loan as of the dates indicated.

	At September 30,								
	2009		2008		2007		2006		
	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent	Amoun
	(Dollars in thousands)								
Mortgage Loans:									
One- to four-family(1)....	$110,556	18.58%	$112,299	18.35%	$102,434	17.40%	$ 98,709	20.11%	$101,7
Multi-family..	25,638	4.31	25,927	4.24	35,157	5.97	17,689	3.60	20,1
Commercial....	188,205	31.62	146,223	23.90	127,866	21.72	137,609	28.04	124,8
Construction and land..... development	139,728	23.48	186,344	30.46	186,261	31.64	146,855	29.92	112,4
Land..........	65,642	11.03	60,701	9.92	60,706	10.30	29,598	6.03	24,9
Total mortgage loans.......	529,769	89.02	531,494	86.87	512,424	87.03	430,460	87.70	384,2
Consumer Loans:									
Home equity and second mortgage.....	41,746	7.01	48,690	7.96	47,269	8.02	37,435	7.63	32,2
Other.........	9,827	1.66	10,635	1.73	10,922	1.86	11,127	2.27	9,3
Total consumer loans.......	51,573	8.67	59,325	9.69	58,191	9.88	48,562	9.90	41,6
Commercial business loans.........	13,775	2.31	21,018	3.44	18,164	3.09	11,803	2.40	12,0
Total loans..	595,117	100.00%	611,837	100.00%	588,779	100.00%	490,825	100.00%	437,8
Less:									
Undisbursed portion of construction									

loans in process......	(31,298)	(43,353)	(65,673)	(59,260)	(42,7
Deferred loan origination fees.........	(2,439)	(2,747)	(2,968)	(2,798)	(2,8
Allowance for loan losses..	(14,172)	(8,050)	(4,797)	(4,122)	(4,0
Total loans receivable, net...........	$547,208	$557,687	$515,341	$424,645	$388,1

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(1) Includes loans held-for-sale.

Residential One- to Four-Family Lending. At September 30, 2009, $110.6 million, or 18.6%, of the Bank's loan portfolio consisted of loans secured by one- to four-family residences. The Bank originates both fixed-rate loans and adjustable-rate loans.

Generally, one-to-four family fixed-rate loans and five and seven year balloon reset loans (which are loans that are originated with a fixed interest rate for the initial five or seven years, and thereafter incur one interest rate change in which the new rate remains in effect for the remainder of the loan term) are originated to meet the requirements for sale in the secondary market to the FHLMC. From time to time, however, a portion of these fixed-rate loans, which include five and seven year balloon reset loans, may be retained in the loan portfolio to meet the Bank's asset/liability management objectives. The Bank periodically retains some fixed rate loans including five and seven year balloon reset loans in its loan portfolio and classifies them as held-to-maturity. The Bank uses an automated underwriting program, which preliminarily qualifies a loan as conforming to FHLMC underwriting standards when the loan is originated. At September 30, 2009, $55.9 million, or 50.6%, of the Bank's one- to four-family loan portfolio consisted of fixed-rate mortgage loans.

The Bank also offers adjustable-rate mortgage ("ARM") loans. All of the Bank's ARM loans are retained in its loan portfolio and not sold. The Bank offers several ARM products which adjust annually after an initial period ranging from one to five years subject to a limitation on the annual increase of 2% and an overall limitation of 6%. These ARM products are priced utilizing the weekly average yield on one year U.S. Treasury securities adjusted to a constant maturity of one year plus a margin of 2.875% to 4.00%. Loans tied to the prime rate or to LIBOR indices typically do not have periodic, or lifetime adjustment limits. Loans tied to these indices normally have margins ranging up to 3.5%. ARM loans held in the Bank's portfolio do not permit negative amortization of principal. Borrower demand for ARM loans versus fixed-rate mortgage loans is a function of the level of interest rates, the expectations of changes in the level of interest rates and the difference between the initial interest rates and fees charged for each type of loan. The relative amount of fixed-rate mortgage loans and ARM loans that can be originated at any time is largely determined by the demand for each in a competitive environment. At September 30, 2009, $54.7 million, or 49.4%, of the Bank's one- to four- family loan portfolio consisted of ARM loans.

A portion of the Bank's ARM loans are "non-conforming" because they do not satisfy acreage limits, or various other requirements imposed by the FHLMC. Some of these loans are also originated to meet the needs of borrowers who cannot otherwise satisfy the FHLMC credit requirements because of personal and financial reasons (i.e., divorce, bankruptcy, length of time employed, etc.), and other aspects, which do not conform to the FHLMC's guidelines. Many of these borrowers have higher debt-to-income ratios, or the loans are secured by unique properties in rural markets for which there are no sales of comparable properties to support value according to secondary market requirements. These loans are known as non-conforming loans and the Bank may require additional collateral or lower loan-to-value ratios to reduce the risk of these loans. The Bank believes that these loans satisfy a need in its local market area. As a result, subject to market conditions, the Bank intends to continue to originate these types of loans.

The retention of ARM loans in the Bank's loan portfolio helps reduce the Bank's exposure to changes in interest rates. There are, however, unquantifiable credit risks resulting from the potential of increased interest to be paid by the customer as a result of increases in interest rates. It is possible that during periods of rising interest rates the risk of default on ARM loans may increase as a result of repricing and the increased costs to the borrower. Furthermore, because the ARM loans originated by the Bank generally provide, as a marketing incentive, for initial rates of interest below the rates which would apply were the adjustment index used for pricing initially, these loans are subject to increased risks of default or delinquency. The Bank attempts to reduce the potential for delinquencies and defaults on ARM loans by qualifying the borrower based on the borrower's ability to repay the ARM loan assuming that the maximum interest rate that could be charged at the first adjustment period remains constant during the loan term. Another consideration is that although ARM loans allow the Bank to increase the sensitivity of its asset base due to changes in the interest rates, the extent of this interest sensitivity is limited by the periodic and lifetime interest rate adjustment limits. Because of these considerations, the Bank has no assurance that yield increases on ARM loans will be sufficient to offset increases in the Bank's cost of funds.

While fixed-rate, single-family residential mortgage loans are normally originated with 15 to 30 year terms, these loans typically remain outstanding for substantially shorter periods because borrowers often prepay their loans in full upon sale of the property pledged as security or upon refinancing the original loan. In addition, substantially all mortgage loans in the Bank's loan portfolio contain due-on-sale clauses providing that the Bank may declare the unpaid amount due and payable upon the sale of the property securing the loan. Typically, the Bank enforces these due-on-sale

clauses to the extent permitted by law and as business judgment dictates. Thus, average loan maturity is a function of, among other factors, the level of purchase and sale activity in the real estate market, prevailing interest rates and the interest rates received on outstanding loans.

The Bank requires that fire and extended coverage casualty insurance be maintained on all of its real estate secured loans. Loans originated since

1994 also require flood insurance, if appropriate.

The Bank's lending policies generally limit the maximum loan-to-value ratio on mortgage loans secured by owner-occupied properties to 95% of the lesser of the appraised value or the purchase price. However, the Bank usually obtains private mortgage insurance ("PMI") on the portion of the principal amount that exceeds 80% of the appraised value of the security property. The maximum loan-to-value ratio on mortgage loans secured by non-owner-occupied properties is generally 80% (90% for loans originated for sale in the secondary market to the FHLMC). At September 30, 2009 seven single family loans totaling $1.34 million were not performing according to their terms. See "- Lending Activities - Non-performing Assets and Delinquencies."

Construction and Land Development Lending. Prompted by unfavorable economic conditions in its primary market area in the 1980s, the Bank sought to establish a market niche and, as a result, began originating construction loans outside of Grays Harbor County. In recent periods, construction lending activities have been primarily in the Pierce, King, Thurston, Grays Harbor, and Kitsap County markets.

The Bank currently originates three types of residential construction loans: (i) custom construction loans, (ii) owner/builder construction loans and (iii) speculative construction loans (on a very limited basis). The Bank believes that its computer tracking system has enabled it to establish processing and disbursement procedures to meet the needs of these borrowers. The Bank also originates construction loans for the development of multi-family and commercial properties.

At September 30, 2009 and 2008, the composition of the Bank's construction and land development loan portfolio was as follows:

	At September 30,			
	2009		2008	
	Outstanding Balance	Percent of Total	Outstanding Balance	Percent of Total
	(In thousands)			
Custom and owner/builder construction	$ 35,414	25.34%	$ 47,168	25.31%
Speculative construction	16,959	12.14	30,895	16.58
Multi-family (including condominium)	18,800	13.46	40,509	21.74
Land development	19,158	13.71	28,152	15.11
Commercial real estate	49,397	35.35	39,620	21.26
Total	$139,728	100.00%	$186,344	100.00%

Custom construction loans are made to home builders who, at the time of construction, have a signed contract with a home buyer who has a commitment to purchase the finished home. Custom construction loans are generally originated for a term of six to 12 months, with fixed interest rates currently ranging from 7.0% to 7.5% and with loan-to-value ratios of 80% of the appraised estimated value of the completed property or sales price, whichever is less. During the construction period, the borrower is required to make monthly payments of accrued interest on the outstanding loan balance, a portion, or all of which may be paid from an interest reserve.

Owner/builder construction loans are originated to the home owner rather than the home builder as a single loan that automatically converts to a permanent loan at the completion of construction. The construction phase of an owner/builder construction loan generally lasts up to 12 months with fixed interest rates currently ranging from 7.0%

to 7.5%, and with loan-to-value ratios of 80% (or up to 95% with PMI) of the appraised estimated value of the completed property. During the construction period, the borrower is required to make monthly payments of accrued interest on the outstanding loan balance, a portion, or all of which may be paid from an interest reserve. At the completion of construction, the loan converts automatically to either a fixed-rate mortgage loan, which conforms to secondary market standards, or an ARM loan for retention in the Bank's portfolio. At September 30, 2009, custom and owner/builder construction loans totaled $35.4 million, or 25.3%, of the total construction loan portfolio. At September 30, 2009, the largest outstanding custom and owner/builder construction loan had an outstanding balance of $1.1 million (including $71,000 of undisbursed loans in process balance) and was performing according to its repayment terms.

Speculative construction loans are made to home builders and are termed "speculative" because the home builder does not have, at the time of loan origination, a signed contract with a home buyer who has a commitment for permanent financing with either the Bank or another lender for the finished home. The home buyer may be identified either during or after the construction period, with the risk that the builder will have to debt service the speculative construction loan and finance real estate taxes and other carrying costs of the completed home for a significant time after the completion of construction until the home buyer is identified and a sale is consummated. Historically, the Bank has originated loans to approximately 50 builders located in the Bank's primary market area, each of which generally would have one to eight speculative loans outstanding from the Bank during a 12 month period. Rather than originating lines of credit to home builders to construct several homes at once, the Bank generally originates and underwrites a separate loan for each home. Speculative construction loans are generally originated for a term of 12 months, with current rates ranging from 6.5% to 7.5%, and with a loan-to-value ratio of no more than 80% of the appraised estimated value of the completed property. During this 12 month period, the borrower is required to make monthly payments of accrued interest on the outstanding loan balance, a portion, or all of which may be paid from an interest reserve. At September 30, 2009, speculative construction loans totaled $17.0 million, or 12.1%, of the total construction loan portfolio. At September 30, 2009, the Bank had nine borrowers each with aggregate outstanding speculative loan balances of more than $500,000. The largest aggregate outstanding balance to one borrower for speculative construction loans totaled $3.2 million (including $86,000 of undisbursed loans in process balance), all of which were performing according to the loan repayment terms. The largest outstanding balance for a single speculative loan was $746,000 and was performing according to its terms. At September 30, 2009, eight out of 53 speculative construction loans with an aggregate balance of $3.4 million were not performing according to their terms. These non-performing loans were located in Pierce County, Thurston County and King County. See "- Lending Activities - Non-performing Assets and Delinquencies."

The Bank historically originated loans to real estate developers with whom it has established relationships for the purpose of developing residential subdivisions (i.e., installing roads, sewers, water and other utilities) (generally with ten to 50 lots). The Bank is not currently originating any new land development loans. At September 30, 2009, the Bank had 18 land development loans totaling $19.2 million, or 13.7% of construction and land development loans receivable. Land development loans are secured by a lien on the property and typically made for a period of two to five years with fixed or variable interest rates, and are made with loan-to-value ratios generally not exceeding 75%. Monthly interest payments are required during the term of the loan. Land development loans are generally structured so that the Bank is repaid in full upon the sale by the borrower of approximately 80% of the subdivision lots. A majority of the Bank's land development loans are secured by property located in its primary market area. In addition, in the case of a corporate borrower, the Bank also generally obtains personal guarantees from corporate principals and reviews their personal financial statements. At September 30, 2009, the Bank had seven land development loans totaling $8.8 million that were non-performing. The non-performing loans consisted of:

* Four loans totaling $5.5 million secured by land development projects in King County;
* Two loans totaling $1.6 million secured by land development projects in Pierce County;
* One loan with a balance of $876,000 secured by a land development project in Thurston County; and
* An $804,000 participation interest in a loan secured by a land development project in Clark County.

Land development loans secured by land under development involve greater risks than one- to four-family residential mortgage loans because these loans are advanced upon the predicted future value of the developed property upon completion. If the estimate of the future value proves to be inaccurate, in the event of default and foreclosure the Bank may be confronted with a property the value of which is insufficient to assure full repayment. The Bank has

historically attempted to minimize this risk by generally limiting the maximum loan-to-value ratio on land loans to 75% of the estimated developed value of the secured property. The Bank is not currently originating any new land development loans.

The Bank also provides construction financing for multi-family and commercial properties. At September 30, 2009, these loans amounted to $18.8 million, or 13.5% of construction loans. These loans are secured by condominiums, apartment buildings, mini-storage facilities, office buildings and retail rental space predominantly located in the Bank's primary market area. At September 30, 2009, the largest outstanding multi-family construction loan was secured by a condominium project and had a balance of $4.1 million (including $12,000 of undisbursed loans in process balance) and was performing according to its repayment terms. At September 30, 2009, the largest outstanding commercial real estate construction loan had a balance of $6.3 million (including $2.0 million of undisbursed loans in process balance). This loan was secured by a medical office facility being constructed in Pierce County and was performing according to its repayment terms.

All construction loans must be approved by a member of one of the Bank's Loan Committees or the Bank's Board of Directors, or in the case of one- to four-family construction loans meeting FHLMC guidelines, by a qualified underwriter. See "- Lending Activities - Loan Solicitation and Processing."

Prior to preliminary approval of any construction loan application, an independent fee appraiser inspects the site and the Bank reviews the existing or proposed improvements, identifies the market for the proposed project and analyzes the pro forma data and assumptions on the project. In the case of a speculative or custom construction loan, the Bank reviews the experience and expertise of the builder. After preliminary approval has been given, the application is processed, which includes obtaining credit reports, financial statements and tax returns on the borrowers and guarantors, an independent appraisal of the project, and any other expert reports necessary to evaluate the proposed project. In the event of cost overruns, the Bank generally requires that the borrower increase the funds available for construction by depositing its own funds into a secured savings account, the proceeds of which are used to pay construction costs.

Loan disbursements during the construction period are made to the builder, materials' supplier or subcontractor, based on a line item budget. Periodic on-site inspections are made by qualified inspectors to document the reasonableness of draw requests. For most builders, the Bank disburses loan funds by providing vouchers to suppliers, which when used by the builder to purchase supplies are submitted by the supplier to the Bank for payment.

The Bank regularly monitors the construction loan disbursements using an internal monitoring system which the Bank believes reduces many of the risks inherent with construction lending.

The Bank originates construction loan applications primarily through customer referrals, contacts in the business community and occasionally real estate brokers seeking financing for their clients.

Construction lending affords the Bank the opportunity to achieve higher interest rates and fees with shorter terms to maturity than does its single-family permanent mortgage lending. Construction lending, however, is generally considered to involve a higher degree of risk than single-family permanent mortgage lending because of the inherent difficulty in estimating both a property's value at completion of the project and the estimated cost of the project. The nature of these loans is such that they are generally more difficult to evaluate and monitor. If the estimate of construction cost proves to be inaccurate, the Bank may be required to advance funds beyond the amount originally committed to permit completion of the project. If the estimate of value upon completion proves to be inaccurate, the Bank may be confronted with a project whose value is insufficient to assure full repayment and it may incur a loss. Projects may also be jeopardized by disagreements between borrowers and builders and by the failure of builders to pay subcontractors. Loans to builders to construct homes for which no purchaser has been identified carry more risk because the payoff for the loan depends on the builder's ability to sell the property prior to the time that the construction loan is due. The Bank has sought to address these risks by adhering to strict underwriting policies, disbursement procedures, and monitoring practices. The Bank's construction loans are primarily secured by properties in its primary market area, and changes in the local and state economies and real estate markets have adversely affected the Bank's construction loan portfolio.

Multi-Family Lending. At September 30, 2009, the Bank had $25.6 million, or 4.3% of the Bank's total loan portfolio, secured by multi-family dwelling units (more than four units) located primarily in the Bank's primary market area. Multi-family loans are generally originated with variable rates of interest ranging from 2.00% to 3.50% over the one-year constant maturity U.S. Treasury Bill Index or a matched term FHLB advance, with principal and interest payments fully amortizing over terms of up to 30 years. At September 30, 2009, the largest multi-family loan had an outstanding principal balance of $5.0 million and was secured by an apartment building located in the Bank's primary market area. At September 30, 2009, this loan was performing according to its terms.

The maximum loan-to-value ratio for multi-family loans is generally limited to not more than 80%. The Bank generally requests its multi-family loan borrowers with loan balances in excess of $750,000 to submit financial statements and rent rolls on the subject property annually. The Bank also inspects the subject property annually. The Bank generally imposes a minimum debt coverage ratio of approximately 1.20 times for loans secured by multi-family properties.

Multi-family mortgage lending affords the Bank an opportunity to receive interest at rates higher than those generally available from one- to four-family residential lending. However, loans secured by multi-family properties usually are greater in amount, more difficult to evaluate and monitor and, therefore, involve a greater degree of risk than one- to four-family residential mortgage loans. Because payments on loans secured by multi-family properties are often dependent on the successful operation and management of the properties, repayment of such loans may be affected by adverse conditions in the real estate market or the economy. The Bank seeks to minimize these risks by scrutinizing the financial condition of the borrower, the quality of the collateral and the management of the property securing the loan. If the borrower is other than an individual, the Bank also generally obtains personal guarantees from the principals based on a review of personal financial statements.

Commercial Real Estate Lending. Commercial real estate loans totaled $188.2 million, or 31.6% of the total loan portfolio at September 30, 2009. The Bank originated $43.8 million of commercial real-estate loans during the year ended September 30, 2009 compared to $29.3 million originated during the year ended September 30, 2008. The Bank originates commercial real estate loans generally at variable interest rates and these loans are secured by properties, such as restaurants, motels, mini-storage facilities, office buildings and retail/wholesale facilities, located in the Bank's primary market area. At September 30, 2009, the largest commercial real estate loan was secured by a mini-storage facility in Pierce County, had a balance of $4.5 million and was 60 days past due. At September 30, 2009, seven commercial real estate loans totaling $5.0 million were not performing according to their terms. See "- Lending Activities - Non-performing Assets and Delinquencies."

The Bank typically requires appraisals of properties securing commercial real estate loans. For loans that are less than $250,000, the Bank may use the tax assessed value and a property inspection in lieu of an appraisal. Appraisals are performed by independent appraisers designated by the Bank, all of which are reviewed by management. The Bank considers the quality and location of the real estate, the credit history of the borrower, the cash flow of the project and the quality of management involved with the property. The Bank generally imposes a minimum debt coverage ratio of approximately 1.20 for originated loans secured by income producing commercial properties. Loan-to-value ratios on commercial real estate loans are generally limited to not more than 80%. If the borrower is other than an individual, the Bank also generally obtains personal guarantees from the principals based on a review of personal financial statements.

Commercial real estate lending affords the Bank an opportunity to receive interest at rates higher than those generally available from one- to four-family residential lending. However, loans secured by such properties usually are greater in amount, more difficult to evaluate and monitor and, therefore, involve a greater degree of risk than one- to four-family residential mortgage loans. Because payments on loans secured by commercial properties often depend upon the successful operation and management of the properties, repayment of these loans may be affected by adverse conditions in the real estate market or the economy. The Bank seeks to minimize these risks by generally limiting the maximum loan-to-value ratio to 80% and strictly scrutinizing the financial condition of the borrower, the quality of the collateral and the management of the property securing the loan. The Bank also requests annual financial information and rent rolls on the subject property from the borrowers on loans over $750,000.

Land Lending. The Bank originates loans for the acquisition of land upon which the purchaser can then build or make improvements necessary to build or to sell as improved lots. At September 30, 2009, land loans totaled $65.6 million, or 11.0% of the Bank's total loan portfolio as compared to $60.7 million, or 9.9% of the Bank's total loan portfolio at September 30, 2008. Land loans originated by the Bank are generally fixed-rate loans and have maturities of five to ten years. The largest land loan had an outstanding balance of $3.0 million at September 30, 2009 and was performing according to its repayment terms. At September 30, 2009, 16 land loans totaling $5.0 million were not performing according to their terms. See "- Lending Activities - Non-performing Assets and Delinquencies."

Loans secured by undeveloped land or improved lots involve greater risks than one- to four-family residential mortgage loans because these loans are more difficult to evaluate. If the estimate of value proves to be inaccurate, in the event of default and foreclosure the Bank may be confronted with a property the value of which is insufficient to assure full repayment. The Bank attempts to minimize this risk by generally limiting the maximum loan-to-value ratio on land loans to 75%.

Consumer Lending. Consumer loans generally have shorter terms to maturity and higher interest rates than mortgage loans. Consumer loans include home equity lines of credit, second mortgage loans, savings account loans, automobile loans, boat loans, motorcycle loans, recreational vehicle loans and unsecured loans. Consumer loans are made with both fixed and variable interest rates and with varying terms. At September 30, 2009, consumer loans amounted to $51.6 million, or 8.7%, of the total loan portfolio.

At September 30, 2009, the largest component of the consumer loan portfolio consisted of second mortgage loans and home equity lines of credit, which totaled $41.7 million, or 7.0%, of the total loan portfolio. Home equity lines of credit and second mortgage loans are made for purposes such as the improvement of residential properties, debt consolidation and education expenses, among others. The majority of these loans are made to existing customers and are secured by a first or second mortgage on residential property. The Bank occasionally solicits these loans. The loan- to-value ratio is typically 80% or less, when taking into account both the first and second mortgage loans. Second mortgage loans typically carry fixed interest rates with a fixed payment over a term between five and 15 years. Home equity lines of credit are generally made at interest rates tied to the prime rate or the 26 week Treasury Bill. Second mortgage loans and home equity lines of credit have greater credit risk than one- to four-family residential mortgage loans because they are secured by mortgages subordinated to the existing first mortgage on the property, which may or may not be held by the Bank.

Consumer loans entail greater risk than do residential mortgage loans, particularly in the case of consumer loans that are unsecured or secured by rapidly depreciating assets such as automobiles. 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. The remaining deficiency often does not warrant further substantial collection efforts against the borrower beyond obtaining a deficiency judgment. In addition, consumer loan collections are dependent on the borrower's continuing financial stability, and are more likely to be adversely affected by job loss, divorce, illness or personal bankruptcy. Furthermore, the application of various federal and state laws, including federal and state bankruptcy and insolvency laws, may limit the amount that can be recovered on such loans. The Bank believes that these risks are not as prevalent in the case of the Bank's consumer loan portfolio because a large percentage of the portfolio consists of second mortgage loans and home equity lines of credit that are underwritten in a manner such that they result in credit risk that is substantially similar to one- to four-family residential mortgage loans. At September 30, 2009, nine consumer loans totaling $258,000 were delinquent in excess of 90 days. See "- Lending Activities - Non-performing Assets and Delinquencies."

Commercial Business Lending. Commercial business loans totaled $13.8 million, or 2.3% of the loan portfolio at September 30, 2009, and consisted of 117 loans. Commercial business loans are generally secured by business equipment, accounts receivable, inventory or other property and are made at variable rates of interest equal to a negotiated margin above the prime rate. The Bank also generally obtains personal guarantees from the principals based on a review of personal financial statements. The largest commercial business loan had an outstanding balance of $1.1 million at September 30, 2009 and was performing according to its terms. At September 30, 2009, two commercial

business loans totaling $65,000 were not performing according to their repayment terms. See "- Lending Activities - Non-performing Assets and Delinquencies."

Commercial business lending generally involves greater risk than residential mortgage lending and involves risks that are different from those associated with residential and commercial real estate lending. Real estate lending is generally considered to be collateral based lending with loan amounts based on predetermined loan to collateral values and liquidation of the underlying real estate collateral is viewed as the primary source of repayment in the event of borrower default. Although commercial business loans are often collateralized by equipment, inventory, accounts receivable or other business assets, the liquidation of collateral in the event of a borrower default is often an insufficient source of repayment because accounts receivable may be uncollectible and inventories and equipment may be obsolete or of limited use, among other things. Accordingly, the repayment of a commercial business loan depends primarily on the creditworthiness of the borrower (and any guarantors), while liquidation of collateral is a secondary and often insufficient source of repayment.

Loan Maturity. The following table sets forth certain information at September 30, 2009 regarding the dollar amount of loans maturing in the Bank's portfolio based on their contractual terms to maturity, but does not include scheduled payments or potential prepayments. Loans having no stated maturity and overdrafts are reported as due in one year or less.

	Within 1 Year	After 1 Year Through 3 Years	After 3 Years Through 5 Years	After 5 Years Through 10 Years	After 10 Years	Total
			(In thousands)			
Mortgage loans:						
One- to four-family (1)	$ 1,835	$ 2,941	$ 3,544	$ 8,381	$ 93,855	$110,556
Multi-family	4,672	1,817	689	17,386	1,074	25,638
Commercial	14,878	10,127	28,531	122,766	11,903	188,205
Construction and land development(2)	139,265	114	349	--	--	139,728
Land	35,889	12,553	12,524	2,980	1,696	65,642
Consumer loans:						
Home equity and second mortgage	11,539	1,578	910	5,782	21,937	41,746
Other	2,693	1,330	1,242	509	4,053	9,827
Commercial business loans	5,427	4,128	695	2,087	1,438	13,775
Total	$216,198	$34,588	$48,484	$159,891	$135,956	595,117
Less:						
Undisbursed portion of construction loans in process						(31,298)
Deferred loan origination fees						(2,439)
Allowance for loan losses						(14,172)
Loans receivable, net						$547,208

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(1) Includes $630,000 of loans held-for-sale.
(2) Includes construction/permanent loans that convert to permanent mortgage loans once construction is completed.

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The following table sets forth the dollar amount of all loans due after one year from September 30, 2009, which have fixed interest rates and have floating or adjustable interest rates.

	Fixed Rates	Floating or Adjustable Rates	Total
		(In thousands)	
Mortgage loans:			
One- to four-family(1)	$ 54,083	$ 54,638	$108,721
Multi-family	2,455	18,512	20,967
Commercial	22,916	150,411	173,327
Construction and land development	348	114	462
Land	24,300	5,453	29,753
Consumer loans:			
Home equity and second mortgage	20,428	9,779	30,207

Other	6,972	162	7,134
Commercial business loans	4,223	4,125	8,348
Total	$135,725	$243,194	$378,919

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(1) Includes loans held-for-sale.

Scheduled contractual principal repayments of loans do not reflect the actual life of these assets. The average life of loans is substantially less than their contractual terms because of prepayments. In addition, due-on-sale clauses on loans generally give the Bank the right to declare loans immediately due and payable in the event, among other things, that the borrower sells the real property subject to the mortgage and the loan is not repaid. The average life of mortgage loans tends to increase, however, when current mortgage loan interest rates are substantially higher than interest rates on existing mortgage loans and, conversely, decrease when interest rates on existing mortgage loans are substantially higher than current mortgage loan interest rates.

Loan Solicitation and Processing. Loan originations are obtained from a variety of sources, including walk-in customers, and referrals from builders and realtors. Upon receipt of a loan application from a prospective borrower, a credit report and other data are obtained to verify specific information relating to the loan applicant's employment, income and credit standing. An appraisal of the real estate offered as collateral generally is undertaken by an appraiser retained by the Bank and certified by the State of Washington.

Loan applications are initiated by loan officers and are required to be approved by an authorized loan underwriter, one of the Bank's Loan Committees or the Bank's Board of Directors. The Bank's Consumer Loan Committee, which consists of three underwriters, each of whom can approve one-to four-family mortgage loans and other consumer loans up to and including the current FHLMC single-family limit. Certain consumer loans up to and including $25,000 may be approved by individual loan officers and the Bank's Consumer Lending Department Manager may approve consumer loans up to and including $75,000. The Bank's Regional Manager of Commercial Lending has individual lending authority for loans up to and including $250,000, excluding speculative construction loans and unsecured loans. The Bank's Commercial Loan Committee, which consists of the Bank's President, Chief Credit Administrator, Executive Vice President of Commercial Lending, Executive Vice President of Community Lending, and Regional Manager of Commercial Lending, may approve commercial real estate loans and commercial business loans up to and including $1.5 million. The Bank's President, Executive Vice President of Commercial Lending and Executive Vice President of Community Lending also have individual lending authority for loans up to and including $750,000. The Bank's Board Loan Committee, which consists of two rotating non-employee Directors and the Bank's President, may approve loans up to and including $3.0 million. Loans in excess of $3.0 million, as well as loans of any amount granted to a single borrower whose aggregate loans exceed $3.0 million, must be approved by the Bank's Board of Directors.

Loan Originations, Purchases and Sales. During the years ended September 30, 2009 and 2008, the Bank's total gross loan originations were $295.3 million and $258.6 million, respectively. Periodically, the Bank purchases participation interests in construction and land development loans, commercial real estate loans, and multi-family loans, secured by properties generally located in Washington State, from other lenders. These purchases are underwritten to the Bank's underwriting guidelines and are without recourse to the seller other than for fraud. During the years ended September 30, 2009 and 2008, the Bank purchased loan participation interests of $1.6 million and $2.9 million, respectively. See "- Lending Activities - Construction and Land Development Lending" and "- Lending Activities - Multi-Family Lending."

Consistent with its asset/liability management strategy, the Bank's policy generally is to retain in its portfolio all ARM loans originated and to sell fixed rate one-to four-family mortgage loans in the secondary market to the FHLMC; however, from time to time, a portion of fixed-rate loans may be retained in the Bank's portfolio to meet its asset-liability objectives. Loans sold in the secondary market are generally sold on a servicing retained basis. At September 30, 2009, the Bank's loan servicing portfolio totaled $251.8 million.

The Bank also periodically sells participation interests in construction and land development loans, commercial real estate loans, and land loans to other lenders. These sales are usually made to avoid concentrations in a particular loan type or concentrations to a particular borrower. The Bank did not sell any loan participation interests to other lenders during the year ended September 30, 2009.

The following table shows total loans originated, purchased, sold and repaid during the periods indicated.

	Year Ended September 30,		
	2009	2008	2007
	(In thousands)		
Loans originated:			
Mortgage loans:			
One- to four-family	$ 165,972	$ 45,844	$ 33,252
Multi-family	1,036	4,710	4,397
Commercial	43,821	29,306	35,886
Construction and land development	56,287	118,186	127,082
Land	6,519	25,858	35,066
Consumer	14,080	22,411	32,354
Commercial business loans	7,601	12,268	11,020
Total loans originated	295,316	258,583	279,057
Loans purchased:			
Mortgage loans:			
One- to four-family	--	--	--
Multi-family	--	--	5,200
Commercial	1,606	--	--
Construction and land development	--	2,862	15,175
Land	--	--	--
Total loans purchased	1,606	2,862	20,375
Total loans originated and purchased	296,922	261,445	299,432
Loans sold:			
Whole loans sold	(162,913)	(45,269)	(29,893)
Participation loans sold	--	(17,035)	(6,650)
Total loans sold	(162,913)	(62,304)	(36,543)

Loan principal repayments	(150,729)	(176,083)	(164,935)
Decrease (increase) in other items, net	6,241	19,288	(7,258)
Net increase (decrease) in loans receivable	$ (10,479)	$ 42,346	$ 90,696

Loan Origination Fees. The Bank receives loan origination fees on many of its mortgage loans and commercial business loans. Loan fees are a percentage of the loan which are charged to the borrower for funding the loan. The amount of fees charged by the Bank is generally 0.0% to 2.0% of the loan amount. Current accounting principles generally accepted in the United States of America require fees received and certain loan origination costs for originating loans to be deferred and amortized into interest income over the contractual life of the loan. Net deferred fees or costs associated with loans that are prepaid are recognized as income at the time of prepayment. Unamortized deferred loan origination fees totaled $2.4 million at September 30, 2009.

Non-performing Loans and Delinquencies. The Bank assesses late fees or penalty charges on delinquent loans of approximately 5% of the monthly loan payment amount. A majority of loan payments are due on the first day of the month; however, the borrower is given a 15 day grace period to make the loan payment. When a mortgage loan borrower fails to make a required payment when due, the Bank institutes collection procedures. A notice is mailed to the borrower 16 days after the date the payment is due. Attempts to contact the borrower by telephone generally begin on or before the 30th day of delinquency. If a satisfactory response is not obtained, continuous follow-up contacts are attempted until the loan has been brought current. Before the 90th day of delinquency, attempts are made to establish (i) the cause of the delinquency, (ii) whether the cause is temporary, (iii) the attitude of the borrower toward the debt, and (iv) a mutually satisfactory arrangement for curing the default.

If the borrower is chronically delinquent and all reasonable means of obtaining payment on time have been exhausted, foreclosure is initiated according to the terms of the security instrument and applicable law. Interest income on loans in foreclosure is reduced by the full amount of accrued and uncollected interest.

When a consumer loan borrower or commercial business borrower fails to make a required payment on a loan by the payment due date, the Bank institutes similar collection procedures as for its mortgage loan borrowers. Loans becoming 90 days or more past due are placed on non-accrual status, with any accrued interest reversed against interest income, unless they are well secured and in the process of collection.

The Bank's Board of Directors is informed monthly as to the status of loans that are delinquent by more than 30 days, and the status of all foreclosed and repossessed property owned by the Bank.

The following table sets forth information with respect to the Company's non-performing assets at the dates indicated.

	At September 30,				
	2009	2008	2007	2006	2005
Loans accounted for on a non-accrual basis:	(In thousands)				
Mortgage loans:					
One- to four-family........	$ 1,343	$ 300	$ 252	$ 80	$ 2,208
Commercial................	5,004	714	90	--	261
Construction and land development..............	17,594	9,840	1,000	--	--
Land......................	5,023	726	28	--	23
Consumer loans............	258	160	--	--	133
Commercial business loans..	65	250	120	--	301
Total....................	29,287	11,990	1,490	80	2,926
Accruing loans which are contractually past due 90 days or more...............	796	--	--	--	--
Total of non-accrual and 90 days past due loans........	30,083	11,990	1,490	80	2,926
Non-accrual investment securities................	477	--	--	--	--
Other real estate owned and other repossessed assets...	8,185	511	--	15	509
Total non-performing assets (1)..............	$ 37,949	$ 12,501	$ 1,490	$ 95	$ 3,435
Troubled debt restructured loans (2)..................	$ 9,492	$ 272	$ --	$ --	$ --
Non-accrual and 90 days or more past due loans as a percentage of loans receivable, net...........	5.36%	2.12%	0.29%	0.02%	0.75%
Non-accrual and 90 days or more past due loans as a percentage of total assets.	4.28%	1.76%	0.23%	0.01%	0.53%
Non-performing assets as a percentage of total assets.	5.41%	1.83%	0.23%	0.02%	0.62%
Loans receivable, net (3)...	$561,380	$565,737	$520,138	$428,767	$392,208
Total assets................	$702,547	$681,883	$644,848	$577,087	$552,765

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(1) Includes non-accrual loans, non-accrual investment securities, other real estate owned and other repossessed assets. Loans considered impaired are not included if they are still on accrual status. Loans classified as troubled debt restructurings are not included if they are on accrual status.
(2) At September 30, 2009, troubled debt restructured loans totaling $9,492 were on non-accrual status and included in total non-performing assets.
(3) Includes loans held-for-sale and is before the allowance for loan losses.

The Bank's non-accrual loans increased by $17.3 million to $29.3 million at September 30, 2009 from $12.0 million at September 30, 2008, primarily as a result of a $7.8 million increase in construction and land development loans on non-accrual status, a $4.3 million increase in land loans on non-accrual status and a $4.3 million increase in commercial real estate loans on non-accrual status. The largest non-performing loan was secured by a condominium construction project in King County and had a balance of $3.7 million at September 30, 2009. Management's evaluation of the collateral determined no impairment existed at September 30, 2009. A discussion of our largest non-performing loans is set forth below under "Asset Classification."

Additional interest income which would have been recorded for the year ended September 30, 2009 had non-accruing loans been current in accordance with their original terms totaled $2.1 million.

Other Real Estate Owned and Other Repossessed Items. Real estate acquired by the Bank as a result of foreclosure or by deed-in-lieu of foreclosure is classified as other real estate owned until sold. When property is acquired, it is recorded at the lower of its cost, which is the unpaid principal balance of the related loan plus foreclosure costs, or fair market value less estimated costs to sell, which becomes the new cost. Subsequent to foreclosure, the property is recorded at the lower of the cost or fair value, less estimated selling costs. At September 30, 2009, the Bank had $8.2 million of other real estate owned and other repossessed items consisting of 26 individual properties representing 14 relationships. The properties consisted of 12 single family homes totaling $3.5 million, one land development project with a balance of $2.3 million, a multi-family property with a balance of $1.1 million, ten land parcels totaling $734,000 and two commercial real estate properties totaling $612,000.

Restructured Loans. Under accounting principles generally accepted in the United States of America, the Bank is required to account for certain loan modifications or restructuring as a "troubled debt restructuring." In general, the modification or restructuring of a debt constitutes a troubled debt restructuring if the Bank for economic or legal reasons related to the borrower's financial difficulties grants a concession to the borrowers that the Bank would not otherwise consider. Debt restructuring or loan modifications for a borrower does not necessarily always constitute troubled debt restructuring, however, and troubled debt restructurings do not necessarily result in non-accrual loans. The Bank had restructured loans totaling $9.5 million at September 30, 2009, all of which were on non-accrual status.

Impaired Loans. A loan is considered impaired when it is probable the Bank will be unable to collect all contractual principal and interest payments due in accordance with the original or modified terms of the loan agreement. Impaired loans are measured based on the estimated fair value of the collateral less estimated cost to sell if the loan is considered collateral dependent. Impaired loans not considered to be collateral dependent are measured based on the present value of expected future cash flows.

The categories of non-accrual loans and impaired loans overlap, although they are not coextensive. The Bank considers all circumstances regarding the loan and borrower on an individual basis when determining whether an impaired loan should be placed on non-accrual status, such as the financial strength of the borrower, the collateral value, reasons for delay, payment record, the amount of past due and the number of days past due. At September 30, 2009, the Bank had $47.6 million in impaired loans. For additional information on impaired loans, see Note 4 of the Notes to the Consolidated Financial Statements included in Item 8 of this Annual Report on Form 10-K.

Other Loans of Concern. Loans not reflected in the table above, but where known information about possible credit problems of borrowers causes management to have doubts as to the ability of the borrower to comply with present repayment terms and that may result in disclosure of such loans as non-performing assets in the future are commonly referred to as "other loans of concern" or "potential problem loans." The amount included in potential problem loans results from an evaluation, on a loan-by-loan basis, of loans classified as "substandard" and "special mention," as those terms are defined under "Asset Classification" below. The amount of potential problem loans and non-performing loans was $84.9 million at September 30, 2009 and $42.8 million at September 30, 2008. The vast majority of these loans are collateralized by real estate. See "- Asset Classification" below for additional information regarding our problem loans.

Asset Classification. Applicable regulations require that each insured institution review and classify its assets on a regular basis. In addition, in connection with examinations of insured institutions, regulatory examiners have authority to identify problem assets and, if appropriate, require them to be classified. There are three classifications for problem assets: substandard, doubtful and loss. Substandard assets have one or more defined weaknesses and are characterized by the distinct possibility that the insured institution will sustain some loss if the deficiencies are not corrected. Doubtful assets have the weaknesses of substandard assets with the additional characteristic that the weaknesses make collection or liquidation in full on the basis of currently existing facts, conditions and values questionable, and there is a high possibility of loss. An asset classified as loss is considered uncollectible and of such little value that continuance as an asset of the institution is not warranted. When an insured institution classifies problem assets as either substandard or doubtful, it is required to establish general allowances for loan losses in an amount deemed prudent by management. These allowances represent loss allowances which have been established to recognize the inherent risk associated with lending activities and the risks associated with particular problem assets. When an insured institution classifies problem assets as loss, it charges off the balance of the asset against the allowance for loan losses.

Assets which do not currently expose the insured institution to sufficient risk to warrant classification in one of the aforementioned categories but possess weaknesses are required to be designated as special mention. The Bank's determination of the classification of its assets and the amount of its valuation allowances is subject to review by the FDIC and the Division which can order the establishment of additional loss allowances.

The aggregate amounts of the Bank's classified and special mention loans (as determined by the Bank), and of the Bank's allowances for loan losses at the dates indicated, were as follows:

	At September 30,		
	2009	2008	2007
	(In thousands)		
Loss	$ --	$ --	$ --
Doubtful	--	--	--
Substandard(1)(2)	63,188	24,603	8,812
Special mention(1)	21,711	18,225	6,917
Total classified and special mention loans	$84,899	$42,828	$15,729
Allowance for loan losses	$14,172	$ 8,050	$ 4,797

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(1) For further information concerning the change in classified assets, see "- Lending Activities - Non-performing Assets and Delinquencies."
(2) Includes non-performing loans.

The Bank's classified and special mention loans increased by $42.1 million from September 30, 2008 to September 30, 2009, primarily as a result of a $38.6 million increase in loans classified as substandard and a $3.5 million increase in loans classified as special mention.

Special mention loan are defined as those credits deemed by management to have some potential weakness that deserve management's close attention. If left uncorrected these potential weaknesses may result in the deterioration of the payment prospects of the loan. Assets in this category are not adversely classified and currently do not expose the Bank to sufficient risk to warrant a substandard classification. Seven individual loans comprise $14.3 million, or 65.8%, of the $21.7 million in loans classified as special mention. They include a $4.3 million loan secured by a multi-family building in King County, a $3.2 million loan secured by a mixed-use building in Thurston County, a $2.5 million loan secured by a multi-family construction project in Grays Harbor County, a $1.2 million loan secured by land in Thurston County, a $1.1 million commercial business loan to a mini-storage facility business in Pierce County, a $1.1 million loan secured by a commercial building in Grays Harbor County, and a $945,000 loan secured by a motel in Grays Harbor County. At September 30, 2009 these loans were current and paying in accordance with their required terms.

Substandard loans are classified as those loans that are inadequately protected by the current net worth, and paying capacity of the obligor, or of the collateral pledged. Assets classified as substandard have a well-defined weakness, or weaknesses that jeopardize the repayment of the debt. If the weakness, or weaknesses are not corrected there is the distinct possibility that some loss will be sustained. The aggregate amount of loans classified as substandard at September 30, 2009 increased by $38.6 million to $63.1 million from $24.6 million at September 30, 2008. At September 30, 2009, 121 loans were classified as substandard compared to 68 at September 30, 2008.

Fifteen credit relationships comprise $42.4 million, or 67.1%, of the $63.2 million in loans classified as substandard (including non-performing loans). These credit relationships classified as substandard are summarized below.

* $8.5 million in loans secured by two mini-storage facilities and a commercial building site. One of the facilities is located in King County and one is located in Pierce County. The commercial building

lot is located in Pierce County adjacent to the mini-storage facility. These three loans were considered impaired at September 30, 2009. Management's evaluation of the collateral determined that there was no principal impairment.

* $5.9 million in loans secured by three land parcels and two land development projects in King County. These loans were considered impaired at September 30, 2009, primarily due to decreased appraisal valuations. Management's evaluation of the collateral determined a potential principal impairment of $1.9 million existed at September 30, 2009 which was factored into the Bank's allowance for loan loss analysis.

* $2.1 million in loans secured by two land development projects in King County. Management's evaluation of the collateral supporting the two loans determined that a potential impairment of $1.0 million existed at September 30, 2009 which was factored into the Bank's allowance for loan loss analysis. This borrower is also a guarantor on two of the loans noted in the bullet point directly above in the amount of $2.0 million.

* $3.7 million loan secured by condominium units located in King County. At September 30, 2009 the loan was not performing in accordance with its terms and was considered impaired. Management's evaluation of the collateral determined that there was no principal impairment.

* $2.7 million loan secured by commercial building lots in Kitsap County. The loan was considered impaired at September 30, 2009. Management's evaluation of the collateral determined that there was no principal impairment.

* $3.2 million participation interest in a condominium conversion loan in King County. The loan was considered impaired at September 30, 2009. Management's evaluation of the collateral and the guarantors' financial capacity determined that there was no principal impairment.

* $2.5 million loan secured by commercial/industrial land in Lewis County. The loan was considered impaired at September 30, 2009. Management's evaluation of the collateral determined that there was no principal impairment.

* $2.4 million loan secured by condominium units in King County that was performing in accordance with its repayment terms at September 30, 2009.

* $2.3 million in loans secured by two speculative single family residential houses and seven building lots in King County. These loans were considered impaired at September 30, 2009 primarily due to decreased appraisal valuations. Management's evaluation of the collateral determined a potential principal impairment of $465,000

existed at September 30, 2009 which was factored into the Bank's allowance for loan loss analysis.

* $1.7 million in loans secured by a residential plat and a completed single family dwelling in Pierce County which were not performing in accordance with their terms at September 30, 2009. Management's evaluation of the collateral determined that there was no principal impairment.

* $1.7 million loan secured by a motel and recreational vehicle park in Grays Harbor County. The loan was considered impaired at September 30, 2009. Management's evaluation of the collateral determined that there was no principal impairment.

* $1.6 million loan secured by residential condominiums and excess land in Oregon which was performing in accordance with its terms at September 30, 2009.

* $1.4 million loan secured by a commercial building in Pierce County. The loan was considered impaired at September 30, 2009. Management's evaluation of the collateral determined that there was no principal impairment.

* $1.4 million loan secured by commercial building lots in Lewis County that was performing in accordance with its repayment terms at September 30, 2009.

* $1.3 million in loans secured by a single family house nearing completion and three commercial condominium units in Pierce County that were performing in accordance with their repayment terms at September 30, 2009.

Allowance for Loan Losses. The allowance for loan losses is maintained to cover estimated losses in the loan portfolio. The Bank has established a comprehensive methodology for the determination of provisions for loan losses that takes into consideration the need for an overall general valuation allowance. The Bank's methodology for assessing the adequacy of its allowance for loan losses is based on its historic loss experience for various loan segments; adjusted for changes in economic conditions, delinquency rates, and other factors. Using these loss estimate factors, management develops a range of probable loss for each loan category. Certain individual loans for which full collectibility may not be assured are evaluated individually with loss exposure based on estimated discounted cash flows or collateral values. The total estimated range of loss based on these two components of the analysis is compared to the loan loss allowance balance. Based on this review, management will adjust the allowance as necessary to maintain directional consistency with trends in the loan portfolio.

In originating loans, the Bank recognizes that losses will be experienced and that the risk of loss will vary with, among other things, the type of loan being made, the creditworthiness of the borrower over the term of the loan, general economic conditions and, in the case of a secured loan, the quality of the security for the loan. The Bank increases its allowance for loan losses by charging provisions for loan losses against the Bank's income.

The Board of Directors reviews the adequacy of the allowance for loan losses at least quarterly based on management's assessment of current economic conditions, past loss and collection experience, and risk characteristics of the loan portfolio.

At September 30, 2009, the Bank's allowance for loan losses totaled $14.2 million. This represents 2.52% of the total loans receivable and 48.39% of non-performing loans. The Bank's allowance for loan losses as a percentage of total loans receivable has increased to 2.52% at September 30, 2009 from 1.42% at September 30, 2008 primarily due to uncertainties in the housing market and the economy, and an increased level of charge-offs (which has translated into higher loss factors assigned to certain loan categories), increased levels of non-performing loans, and increased levels of classified loans.

Management believes that the amount maintained in the allowance is adequate to absorb probable losses in the portfolio. Although management believes that it uses the best information available to make its determinations, future adjustments to the allowance for loan losses may be necessary and results of operations could be significantly and adversely affected if circumstances differ substantially from the assumptions used in making the determinations.

While the Bank believes it has established its existing allowance for loan losses in accordance with accounting principles generally accepted in the United States of America, there can be no assurance that regulators, in reviewing the Bank's loan portfolio, will not request the Bank to increase significantly its allowance for loan losses. In addition, because future events affecting borrowers and collateral cannot be predicted with certainty, there can be no assurance that the existing allowance for loan losses is adequate or that substantial increases will not be necessary should the quality of any loans deteriorate as a result of the factors discussed above. Any material increase in the allowance for loan losses may adversely affect the Bank's financial condition and results of operations.

The following table sets forth an analysis of the Bank's allowance for loan losses for the periods indicated.

	Year Ended September 30,				
	2009	2008	2007	2006	2005
	(Dollars in thousands)				
Allowance at beginning of year...	$ 8,050	$4,797	$4,122	$4,099	$3,991
Provision for loan losses........	10,734	3,900	686	--	141
Allocated to loan commitments....	(169)	--	--	--	--
Recoveries:					
Mortgage loans:					
Land...........................	83	--	--	--	--
Consumer loans:					
Home equity and second mortgage.	--	--	--	--	5
Other..........................	5	1	1	5	3
Commercial business loans........	--	--	--	20	9

Total recoveries	88	1	1	25	17
Charge-offs:					
Mortgage loans:					
One- to four-family............	46	--	--	--	--
Multi-family...................	--	--	--	--	1
Construction...................	3,108	648	--	--	--
Commercial.....................	235	--	--	--	--
Land...........................	705	--	--	--	1
Consumer loans:					
Home equity and second mortgage.	162	--	--	--	--
Other..........................	25	--	12	2	12
Commercial business loans........	250	--	--	--	36
Total charge-offs..............	4,531	648	12	2	50
Net charge-offs (recoveries)....	4,443	647	11	(23)	33
Balance at end of year..........	$14,172	$8,050	$4,797	$4,122	$4,099
Allowance for loan losses as a percentage of total loans receivable (net)(1) outstanding at the end of the year.........	2.52%	1.42%	0.92%	0.96%	1.05%
Net charge-offs (recoveries) as a percentage of average loans outstanding during the year.....	0.79%	0.12%	0.00%	(0.01%)	0.01%
Allowance for loan losses as a percentage of non-performing loans at end of year excluding troubled debt restructurings....	48.39%	67.14%	321.95%	5,152.50%	140.09%

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(1) Total loans receivable (net) includes loans held for sale and is before the allowance for loan losses.

The following table sets forth the allocation of the allowance for loan losses by loan catego
dates indicated.

At September 30,								
2009		2008		2007		2006		
Amount	Percent of Loans in Category to Total Loans	Amount	Percent of Loans in Category to Total Loans	Amount	Percent of Loans in Category to Total Loans	Amount	Percent of Loans in Category to Total Loans	Amount

(Dollars in thousands)

Mortgage loans:									
One- to four-family.......	$ 616	18.58%	$ 476	18.35%	$ 396	17.40%	$ 502	20.11%	$ 494
Multi-family..	431	4.31	248	4.24	200	5.97	112	3.60	194
Commercial....	2,719	31.63	1,521	23.90	1,368	21.72	1,222	28.04	1,544
Construction..	5,132	23.48	3,254	30.46	1,047	31.64	761	29.92	652
Land..........	3,348	11.03	1,435	9.92	549	10.30	275	6.03	255
Non-mortgage loans:									
Consumer loans........	1,216	8.66	457	9.69	412	9.88	497	9.90	255
Commercial business loans........	710	2.31	659	3.44	825	3.09	753	2.40	705
Total allowance for loan losses......	$14,172	100.00%	$8,050	100.00%	$4,797	100.00%	$4,122	100.00%	$4,099

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Investment Activities

The investment policies of the Company are established and monitored by the Board of Directors. The policies are designed primarily to provide and maintain liquidity, to generate a favorable return on investments without incurring undue interest rate and credit risk, and to compliment the Bank's lending activities. These policies dictate the criteria for classifying securities as either available-for-sale or held-to-maturity. The policies permit investment in various types of liquid assets permissible under applicable regulations, which includes U.S. Treasury obligations, securities of various federal agencies, certain certificates of deposit of insured banks, banker's acceptances, federal funds, mortgage-backed securities, and mutual funds. The Company's investment policy also permits investment in equity securities in certain financial service companies.

At September 30, 2009, the Company's investment portfolio totaled $20.6 million, primarily consisting of $12.5 million of mortgage-backed securities available-for-sale, $968,000 of mutual funds available-for-sale, and $7.1 million of mortgaged-backed securities held-to-maturity. The Company does not maintain a trading account for any investments. This compares with a total investment portfolio of $31.3 million at September 30, 2008, primarily consisting of $936,000 of mutual funds available-for-sale, $16.2 million of mortgage-backed securities available-for-sale, and $14.2 million of mortgage-backed securities held-to-maturity. The composition of the portfolios by type of security, at each respective date is presented in the following table.

	At September 30,		
	2008	2007	2006

	Recorded Value	Percent of Total	Recorded Value	Percent of Total	Recorded Value	Percent of Total
			(Dollars in thousands)			
Held-to-Maturity:						
U.S. agency securities........	$ 27	0.13%	$ 28	0.09%	$ --	--%
Mortgage-backed securities........	7,060	34.34	14,205	45.34	71	0.11
Available-for-Sale (at fair value):						
U.S. agency securities........	--	--	--	--	18,976	29.66
Mortgage-backed securities........	12,503	60.82	16,162	51.58	13,047	20.39
Mutual funds.......	968	4.71	936	2.99	31,875	49.84
Total portfolio.....	$20,558	100.00%	$31,331	100.00%	$63,969	100.00%

The following table sets forth the maturities and weighted average yields of the investment and mortgage-backed securities in the Company's investment securities portfolio at September 30, 2009. Mutual funds, which by their nature do not have maturities, are classified in the one year or less category.

	One Year or Less		After One to Five Years		After Five to Ten Years		After Year
	Amount	Yield	Amount	Yield	Amount	Yield	Amount
				(Dollars in thousands)			
Held-to-Maturity:							
U.S. agency securities...	$ --	--%	$ 14	3.25%	$ 14	3.98%	$ --
Mortgage-backed securities.............	--	--	--	--	43	4.66	7,016
Available-for-Sale:							
Mortgage-backed securities.............	--	--	418	2.11	256	5.92	11,829
Mutual funds............	968	3.78	--	--	--	--	--

Total portfolio..........	$968	3.78%	$432	2.14%	$313	5.65%	$18,845
	====	====	====	====	====	====	=======

There were no securities which had an aggregate book value in excess of 10% of the Company's total equity at September 30, 2009. At September 30, 2009, the Company had 29 private label mortgage backed securities totaling $477,000 on non-accrual status. For additional information regarding investment securities, see "Item 1A, Risk Factors - Risks Related to Our Business - Other-than-temporary impairment charges in our investment securities portfolio could result in significant losses and adversely affect our continuing operations" and Note 3 of the Notes to the Consolidated Financial Statements included in Item 8 of this Annual Report on Form 10-K.

Deposit Activities and Other Sources of Funds

General. Deposits and loan repayments are the major sources of the Bank's funds for lending and other investment purposes. Scheduled loan repayments are a relatively stable source of funds, while deposit inflows and outflows and loan prepayments are influenced significantly by general interest rates and money market conditions. Borrowings through the FHLB-Seattle, the Federal Reserve Bank ("FRB") and Pacific Coast Bankers' Bank ("PCBB") may be used to compensate for reductions in the availability of funds from other sources.

Deposit Accounts. Substantially all of the Bank's depositors are residents of Washington. Deposits are attracted from within the Bank's market area through the offering of a broad selection of deposit instruments, including money market deposit accounts, checking accounts, regular savings accounts and certificates of deposit. Deposit account terms vary, according to the minimum balance required, the time periods the funds must remain on deposit and the interest rate, among other factors. In determining the terms of its deposit accounts, the Bank considers current market interest rates, profitability to the Bank, matching deposit and loan products and its customer preferences and concerns. The Bank actively seeks consumer and commercial checking accounts through a checking account acquisition marketing program that was implemented in 2000. At September 30, 2009, the Bank had 33.2% of total deposits in non-interest bearing accounts and NOW checking accounts.

At September 30, 2009 the Bank had $77.9 million of jumbo certificates of deposit of $100,000 or more. The Bank also had brokered certificates of deposits totaling $3.8 million at September 30, 2009. The $3.8 million in brokered deposits consisted of reciprocal deposits in the Certificate of Deposits Account Registry Service ("CDARS") program. The Bank believes that its jumbo certificates of deposit and its brokered deposits, which represented 16.2% of total deposits at September 30, 2009, present similar interest rate risk compared to its other deposits.

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The following table sets forth information concerning the Bank's deposits at September 30, 2009.

Weighted Percentage

Category	Average Interest Rate	Amount	of Total Deposits
		(In thousands)	
Non-interest bearing	-%	$ 50,295	9.95%
Negotiable order of withdrawal ("NOW") checking	1.05	117,357	23.21
Savings	0.71	58,609	11.59
Money market	1.68	62,478	12.36
Subtotal	1.14	288,739	57.11
Certificates of Deposit(1)			
Maturing within 1 year	2.51	182,285	36.04
Maturing after 1 year but within 2 years	2.71	22,587	4.47
Maturing after 2 years but within 5 years	3.64	11,734	2.32
Maturing after 5 years	2.75	316	0.06
Total certificates of deposit	2.59	216,922	42.89
Total deposits	1.76%	$505,661	100.00%

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(1) Based on remaining maturity of certificates.

The following table indicates the amount of the Bank's jumbo certificates of deposit by time remaining until maturity as of September 30, 2009. Jumbo certificates of deposit have principal balances of $100,000 or more and the rates paid on these accounts are generally negotiable.

Maturity Period	Amount
	(In thousands)
Three months or less	$23,459
Over three through six months	16,934
Over six through twelve months	26,117
Over twelve months	11,416
Total	$77,926

Deposit Flow. The following table sets forth the balances of deposits in the various types o offered by the Bank at the dates indicated.

	At September 30,		
	2009	2008	2
	Percent	Percent	

	Amount	of Total	Increase (Decrease)	Amount	of Total	Increase (Decrease)	Amount
			(Dollars in thousands)				
Non-interest-bearing	$ 50,295	9.95%	$(1,660)	$ 51,955	10.42%	$ (3,007)	$ 54,9
NOW checking	117,357	23.21	26,889	90,468	18.15	10,096	80,3
Savings	58,609	11.59	2,218	56,391	11.31	(21)	56,4
Money market	62,478	12.36	(7,901)	70,379	14.11	22,311	48,0
Certificates of deposit which mature:							
Within 1 year	182,285	36.04	6,468	175,817	35.26	(32,513)	208,3
After 1 year, but within 2 years	22,587	4.47	(23,820)	46,407	9.31	33,668	12,7
After 2 years, but within 5 years	11,734	2.32	4,975	6,759	1.36	1,028	5,7
Certificates maturing thereafter	316	0.06	(80)	396	0.08	275	1
Total	$505,661	100.00%	$7,089	$498,572	100.00%	$ 31,837	$466,7

Certificates of Deposit by Rates. The following table sets forth the certificates of deposit in the Bank classified by rates as of the dates indicated.

	At September 30, 2009	2008	2007
	(In thousands)		
0.00 - 1.99%..........................	$ 59,466	$ 866	$ 676
2.00 - 3.99%..........................	146,513	203,859	46,810
4.00 - 5.99%..........................	10,569	24,274	179,008
6.00% - and over......................	374	380	427
Total................................	$216,922	$229,379	$226,921

Certificates of Deposit by Maturities. The following table sets forth the amount and maturities of certificates of deposit at September 30, 2009.

Amount Due: Less Than One Year	One to Two Years	After Two to Five Years	After Five Years	Total
		(In thousands)		

0.00 - 1.99%.............	$ 55,350	$ 3,865	$ 169	$ 82	$ 59,466
2.00 - 3.99%.............	117,421	18,325	10,533	234	146,513
4.00 - 5.99%.............	9,200	337	1,032	--	10,569
6.00% and over...........	314	60	--	--	374
Total....................	$182,285	$22,587	$11,734	$316	$216,922

Deposit Activities. The following table sets forth the savings activities of the Bank for the periods indicated.

	Year Ended September 30,		
	2009	2008	2007
	(In thousands)		
Beginning balance......................	$498,572	$466,735	$431,061
Net deposits (withdrawals) before interest credited....................	(2,383)	20,075	24,382
Interest credited......................	9,472	11,762	11,292
Net increase in deposits...............	7,089	31,837	35,674
Ending balance.........................	$505,661	$498,572	$466,735

Borrowings. Deposits and loan repayments are generally the primary source of funds for the Bank's lending and investment activities and for general business purposes. The Bank has the ability to use advances from the FHLB-Seattle to supplement its supply of lendable funds and to meet deposit withdrawal requirements. The FHLB-Seattle functions as a central reserve bank providing credit for member financial institutions. As a member of the FHLB-Seattle, the Bank is required to own capital stock in the FHLB-Seattle and is authorized to apply for advances on the security of such stock and certain mortgage loans and other assets (principally securities which are obligations of, or guaranteed by, the United States government) provided certain creditworthiness standards have been met. Advances are made pursuant to several different credit programs. Each credit program has its own interest rate and range of maturities. Depending on the program, limitations on the amount of advances are based on the financial condition of the member institution and the adequacy of collateral pledged to secure the credit. At September 30, 2009, the Bank maintained an uncommitted credit facility with the FHLB-Seattle that provided for immediately available advances up to an aggregate amount of 30% of the Bank's total assets, limited by available collateral, under which $95.0 million was outstanding.

The Bank also utilizes overnight repurchase agreements with customers. These overnight repurchase agreements are classified as other borrowings and totaled $777,000 at September 30, 2009. The Bank also maintains a short-term borrowing line with the FRB with total credit based on eligible collateral. At September 30, 2009, the Bank had $10.0 million outstanding and $6.3 million in unused borrowing capacity on this borrowing line. The Bank has also been approved for a $10.0 million overnight borrowing line with PCBB. The borrowing line must be collateralized. At September 30, 2009, the Bank had not pledged any collateral for this borrowing line and there was no outstanding balance.

The following table sets forth certain information regarding borrowings by the Bank at the end of and during the periods indicated:

	At or For the Year Ended September 30,		
	2009	2008	2007
	(Dollars in thousands)		
Average total borrowings	$ 97,393	$108,858	$ 85,599
Weighted average rate paid on total borrowings	4.14%	4.27%	5.24%
Total borrowings outstanding at end of period	$105,777	$105,386	$100,292

The following table sets forth certain information regarding short-term borrowings by the Bank at the end of and during the periods indicated. Borrowings are considered short-term when the original maturity is less than one year.

	At or For the Year Ended September 30,		
	2009	2008	2007
	(Dollars In thousands)		
Maximum amount outstanding at any month end:			
FHLB advances	$ --	$42,600	$72,750
Repurchase agreements	844	1,884	4,460
PCBB advances	--	--	--
FRB advances	10,000	--	--
Average outstanding during period:			
FHLB advances	15	$13,366	$34,156
Repurchase agreements	624	943	1,019
PCBB advances	6	12	32
FRB advances	27	--	--
Total average outstanding during period	$ 672	$14,321	$35,207
Weighted average rate paid during period:			
FHLB advances	0.71%	4.44%	5.58%
Repurchase agreements	0.08	2.12	4.61
PCBB advances	1.48	5.27	6.45
FRB advances	0.50	--	--
Total weighted average rate paid during period	0.12	4.29%	5.55%

(table continued on following page)

	At or For the Year Ended September 30,

	2009	2008	2007
	(Dollars In thousands)		
Outstanding at end of period:			
FHLB advances	$ --	$ --	$30,000
Repurchase agreements	777	758	595
PCBB advances	--	--	--
FRB advances	10,000	--	--
Total outstanding at end of period	$10,777	$ 758	$30,595
Weighted average rate at end of period:			
FHLB advances	--%	--%	5.19%
Repurchase agreements	0.05	1.05	4.42
PCBB advances	--	--	--
FRB advances	0.50	--	--
Total weighted average rate at end of period	0.50%	1.05%	5.17%

Bank Owned Life Insurance

The Bank has purchased life insurance policies covering certain officers. These policies are recorded at their cash surrender value, net of any policy premium charged. Increases in cash surrender value, net of policy premiums, and proceeds from death benefits are recorded in non-interest income. At September 30, 2009, the Bank had $12.9 million in bank owned life insurance.

Regulation of the Bank

General. The Bank, as a state-chartered savings bank, is subject to regulation and oversight by the Division and the applicable provisions of Washington law and regulations of the Division adopted thereunder. The Bank also is subject to regulation and examination by the FDIC, which insures the deposits of the Bank to the maximum extent permitted by law, and requirements established by the Federal Reserve. State law and regulations govern the Bank's ability to take deposits and pay interest thereon, to make loans on or invest in residential and other real estate, to make consumer loans, to invest in securities, to offer various banking services to its customers, and to establish branch offices. Under state law, savings banks in Washington also generally have all of the powers that federal savings banks have under federal laws and regulations. The Bank is subject to periodic examination and reporting requirements by and of the Division and the FDIC.

In December 2009, the FDIC and the Division agreed to terms on an informal supervisory agreement, a MOU, which will be reviewed for approval by the Board on December 22, 2009. The MOU restricts certain operations of the Bank and requires the Bank to maintain a higher level of regulatory capital. The Board and Bank management do not believe that this agreement will constrain the Bank's business plan and furthermore, we believe that the Bank is currently in compliance with many of the requirements through its normal business operations. These requirements will remain in effect until modified or terminated by the FDIC and the Division. For more information about the MOU and its impact on the Bank, see "Item 1A, Risk Factors   Risks Related to Our Business   We are required to comply with the terms of a pending memoranda of understanding issued by the FDIC and the Division and lack of compliance could result in additional regulatory actions."

Recent Legislative and Regulatory Initiatives to Address Financial and Economic Crises. The Congress, Treasury Department and the federal banking regulators, including the FDIC, have taken broad action since early September 2008 to address volatility in the U.S. banking system.

In October 2008, the Emergency Economic Stabilization Act of 2008 ("EESA") was enacted which, among other measures, authorized the Treasury Secretary to establish the Troubled Asset Relief Program ("TARP"). EESA gives broad authority to Treasury to purchase, manage, modify, sell and insure the troubled mortgage related assets that triggered the current economic crisis as well as other "troubled assets." EESA includes additional provisions directed at bolstering the economy, including:

* Authority for the Federal Reserve to pay interest on depository institution balances;
* Mortgage loss mitigation and homeowner protection;
* Temporary increase in FDIC insurance coverage from $100,000 to $250,000 through December 31, 2013; and
* Authority to the Securities and Exchange Commission (the "SEC") to suspend mark-to-market accounting requirements for any issuer or class of category of transactions.

Under the TARP, the Treasury has created a capital purchase program ("CPP"), pursuant to