Territorial Bancorp Inc.
Form 10-Q
August 08, 2013
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

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

For the Quarterly Period ended June 30, 2013

or

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

For transition period from to

Commission File Number 1-34403

TERRITORIAL BANCORP INC.

(Exact Name of Registrant as Specified in Charter)

Maryland	**26-4674701**
(State or Other Jurisdiction of Incorporation)	(I.R.S. Employer Identification No.)
1132 Bishop Street, Suite 2200, Honolulu, Hawaii	**96813**
(Address of Principal Executive Offices)	(Zip Code)

(808) 946-1400

Registrant s telephone number, including area code

Not Applicable

(Former name or former address, if changed since last report)

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

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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No o

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

Large accelerated filer o	Accelerated filer x
Non-accelerated filer o	Smaller reporting company o

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

Indicate the number of shares outstanding of each of the Issuer s classes of common stock as of the latest practicable date.

10,474,230 shares of Common Stock, par value $0.01 per share, were issued and outstanding as of July 31, 2013.

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TERRITORIAL BANCORP INC.

Form 10-Q Quarterly Report

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PART I

ITEM 1. FINANCIAL STATEMENTS

TERRITORIAL BANCORP INC. AND SUBSIDIARIES

Consolidated Balance Sheets (Unaudited)

(Dollars in thousands, except share data)

	June 30, 2013	December 31, 2012
ASSETS		
Cash and cash equivalents	$ 87,171	$ 182,818
Investment securities held to maturity, at amortized cost (fair value of $580,456 and $584,125 at June 30, 2013 and December 31, 2012, respectively)	582,682	554,673
Federal Home Loan Bank stock, at cost	11,908	12,128
Loans held for sale	2,991	2,220
Loans receivable, net	821,757	774,876
Accrued interest receivable	4,370	4,367
Premises and equipment, net	4,799	5,056
Bank-owned life insurance	39,656	31,177
Deferred income taxes receivable	4,861	3,580
Prepaid expenses and other assets	2,220	3,732
Total assets	$ 1,562,415	$ 1,574,627
LIABILITIES AND STOCKHOLDERS EQUITY		
Liabilities:		
Deposits	$ 1,235,456	$ 1,237,847
Advances from the Federal Home Loan Bank	15,000	20,000
Securities sold under agreements to repurchase	65,000	70,000
Accounts payable and accrued expenses	23,500	23,017
Current income taxes payable	1,857	1,152
Advance payments by borrowers for taxes and insurance	3,575	3,639
Total liabilities	1,344,388	1,355,655
Stockholders Equity:		
Preferred stock, $.01 par value; authorized 50,000,000 shares, no shares issued or outstanding	0	0
Common stock, $.01 par value; authorized 100,000,000 shares; issued and outstanding 10,474,230 and 10,806,248 shares at June 30, 2013 and December 31, 2012, respectively	105	108
Additional paid-in capital	87,618	93,616
Unearned ESOP shares	(7,585)	(7,829)
Retained earnings	142,135	137,410
Accumulated other comprehensive loss	(4,246)	(4,333)

Total stockholders equity		218,027		218,972
Total liabilities and stockholders equity	$	1,562,415	$	1,574,627

See accompanying notes to consolidated financial statements.

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TERRITORIAL BANCORP INC. AND SUBSIDIARIES

Consolidated Statements of Income (Unaudited)
(Dollars in thousands, except per share data)

	Three Months Ended June 30, 2013	Three Months Ended June 30, 2012	Six Months Ended June 30, 2013	Six Months Ended June 30, 2012
Interest and dividend income:				
Investment securities	$ 4,518	$ 6,293	$ 9,072	$ 12,809
Loans	9,199	9,110	18,429	18,139
Other investments	66	87	164	171
Total interest and dividend income	13,783	15,490	27,665	31,119
Interest expense:				
Deposits	1,074	1,582	2,194	3,152
Advances from the Federal Home Loan Bank	65	104	168	208
Securities sold under agreements to repurchase	471	831	948	1,735
Total interest expense	1,610	2,517	3,310	5,095
Net interest income	12,173	12,973	24,355	26,024
Provision (reversal of allowance) for loan losses	(16)	(79)	2	5
Net interest income after provision (reversal of allowance) for loan losses	12,189	13,052	24,353	26,019
Noninterest income:				
Service fees on loan and deposit accounts	568	480	1,069	1,030
Income on bank-owned life insurance	258	234	479	467
Gain on sale of investment securities	1,024	172	1,912	300
Gain on sale of loans	380	406	1,025	847
Other	81	115	186	205
Total noninterest income	2,311	1,407	4,671	2,849
Noninterest expense:				
Salaries and employee benefits	5,012	5,041	10,364	10,214
Occupancy	1,333	1,290	2,584	2,614
Equipment	851	811	1,723	1,623
Federal deposit insurance premiums	191	192	381	382
Loss on extinguishment of debt	0	198	0	198
Other general and administrative expenses	1,208	966	2,259	2,105
Total noninterest expense	8,595	8,498	17,311	17,136
Income before income taxes	5,905	5,961	11,713	11,732
Income taxes	2,244	2,115	4,411	4,346
Net income	$ 3,661	$ 3,846	$ 7,302	$ 7,386
Basic earnings per share	$ 0.37	$ 0.38	$ 0.74	$ 0.73
Diluted earnings per share	$ 0.36	$ 0.37	$ 0.72	$ 0.72
Cash dividends declared per common share	$ 0.13	$ 0.11	$ 0.25	$ 0.21
Basic weighted-average shares outstanding	9,841,162	10,135,179	9,879,050	10,163,647
Diluted weighted-average shares outstanding	10,070,604	10,303,363	10,093,690	10,305,751

See accompanying notes to consolidated financial statements.

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TERRITORIAL BANCORP INC. AND SUBSIDIARIES

Consolidated Statements of Comprehensive Income (Unaudited)
(Dollars in thousands)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	**2012**	**2013**	**2012**
Net income	$ 3,661	$ 3,846	$ 7,302	$ 7,386
Change in unrealized loss on securities	10	6	18	10
Noncredit related gains on securities not expected to be sold	47	0	69	0
Other comprehensive income	57	6	87	10
Comprehensive income	$ 3,718	$ 3,852	$ 7,389	$ 7,396

See accompanying notes to consolidated financial statements.

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TERRITORIAL BANCORP INC. AND SUBSIDIARIES

Consolidated Statements of Stockholders Equity and Comprehensive Income (Unaudited) (Dollars in thousands)

	Common Stock	Additional Paid-in Capital	Unearned ESOP Shares	Retained Earnings	Accumulated Other Comprehensive (Loss)/Income	Total Stockholders Equity
Balances at December 31, 2011	$ 110	$ 97,640	$ (8,319)	$ 128,300	$ (3,770)	$ 213,961
Net income	0	0	0	7,386	0	7,386
Other comprehensive income	0	0	0	0	10	10
Cash dividends declared	0	0	0	(2,259)	0	(2,259)
Share-based compensation	0	1,323	0	0	0	1,323
Allocation of 24,466 ESOP shares	0	274	245	0	0	519
Repurchase of 251,739 shares of company common stock	(2)	(5,336)	0	0	0	(5,338)
Exercise of 41,275 options on common stock	0	716	0	0	0	716
Balances at June 30, 2012	$ 108	$ 94,617	$ (8,074)	$ 133,427	$ (3,760)	$ 216,318
Balances at December 31, 2012	$ 108	$ 93,616	$ (7,829)	$ 137,410	$ (4,333)	$ 218,972
Net income	0	0	0	7,302	0	7,302
Other comprehensive income	0	0	0	0	87	87
Cash dividends declared	0	0	0	(2,577)	0	(2,577)
Share-based compensation	0	1,327	0	0	0	1,327
Allocation of 24,466 ESOP shares	0	326	244	0	0	570
Repurchase of 332,018 shares of company common stock	(3)	(7,651)	0	0	0	(7,654)
Balances at June 30, 2013	$ 105	$ 87,618	$ (7,585)	$ 142,135	$ (4,246)	$ 218,027

See accompanying notes to consolidated financial statements.

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TERRITORIAL BANCORP INC. AND SUBSIDIARIES

Consolidated Statements of Cash Flows (Unaudited)
(Dollars in thousands)

	Six Months Ended June 30, 2013	Six Months Ended June 30, 2012
Cash flows from operating activities:		
Net income	$ 7,302	$ 7,386
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	2	5
Depreciation and amortization	567	571
Deferred income tax benefit	(1,339)	(655)
Amortization of fees, discounts, and premiums	401	(133)
Origination of loans held for sale	(47,607)	(44,376)
Proceeds from sales of loans held for sale	47,861	46,539
Gain on sale of loans, net	(1,025)	(847)
Net gain on sale of real estate owned	0	(38)
Gain on sale of investment securities held to maturity	(1,912)	(300)
ESOP expense	570	519
Share-based compensation expense	1,327	1,323
Excess tax benefits from share-based compensation	0	(54)
(Increase) decrease in accrued interest receivable	(3)	94
Net increase in bank-owned life insurance	(479)	(467)
Net decrease in prepaid expenses and other assets	1,512	409
Net increase (decrease) in accounts payable and accrued expenses	483	(1,665)
Net increase (decrease) in income taxes payable	705	(1,435)
Net cash provided by operating activities	8,365	6,876
Cash flows from investing activities:		
Purchases of investment securities held to maturity	(167,189)	(67,354)
Principal repayments on investment securities held to maturity	110,983	95,378
Proceeds from sale of investment securities held to maturity	29,188	4,559
Loan originations, net of principal repayments on loans receivable	(46,218)	(37,383)
Proceeds from redemption of Federal Home Loan Bank stock	220	0
Purchases of bank-owned life insurance	(8,000)	0
Proceeds from sale of real estate owned	0	262
Purchases of premises and equipment	(310)	(282)
Net cash used in investing activities	(81,326)	(4,820)

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TERRITORIAL BANCORP INC. AND SUBSIDIARIES

Consolidated Statements of Cash Flows (Unaudited)
(Dollars in thousands)

	Six Months Ended June 30, 2013	Six Months Ended June 30, 2012
Cash flows from financing activities:		
Net increase (decrease) in deposits	$ (2,391)	$ 47,166
Proceeds from advances from the Federal Home Loan Bank	5,000	100
Repayments of advances from the Federal Home Loan Bank	(10,000)	(100)
Repayments of securities sold under agreements to repurchase	(5,000)	(18,000)
Purchases of Fed Funds	0	10
Sales of Fed Funds	0	(10)
Net increase (decrease) in advance payments by borrowers for taxes and insurance	(64)	41
Excess tax benefits from share-based compensation	0	54
Proceeds from issuance of common stock	0	716
Repurchases of company stock	(7,654)	(5,338)
Cash dividends paid	(2,577)	(2,259)
Net cash provided by (used in) financing activities	(22,686)	22,380
Net increase (decrease) in cash and cash equivalents	(95,647)	24,436
Cash and cash equivalents at beginning of the period	182,818	131,937
Cash and cash equivalents at end of the period	$ 87,171	$ 156,373
Supplemental disclosure of cash flow information:		
Cash paid for:		
Interest on deposits and borrowings	$ 3,305	$ 5,162
Income taxes	5,045	6,436

See accompanying notes to consolidated financial statements.

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TERRITORIAL BANCORP INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Unaudited)

(1) Basis of Presentation

The accompanying unaudited consolidated financial statements of Territorial Bancorp Inc. have been prepared in accordance with U.S. generally accepted accounting principles (GAAP) for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules and regulations. These interim condensed consolidated financial statements and notes should be read in conjunction with Territorial Bancorp Inc. s consolidated financial statements and notes thereto filed as part of the Annual Report on Form 10-K for the year ended December 31, 2012. In the opinion of management, all adjustments necessary for a fair presentation have been made and include all normal recurring adjustments. Interim results of operations are not necessarily indicative of results to be expected for the year.

(2) Organization

On November 4, 2008, the Board of Directors of Territorial Mutual Holding Company approved a plan of conversion and reorganization under which the Company would convert from a mutual holding company to a stock holding company. The conversion to a stock holding company was approved by the depositors and borrowers of Territorial Savings Bank and the Office of Thrift Supervision (OTS) and included the filing of a registration statement with the U.S. Securities and Exchange Commission. Upon the completion of the conversion and reorganization on July 10, 2009, Territorial Mutual Holding Company and Territorial Savings Group, Inc. ceased to exist as separate legal entities and Territorial Bancorp Inc. became the holding company for Territorial Savings Bank. A total of 12,233,125 shares were issued in the conversion at $10 per share, raising $122.3 million of gross proceeds. $3.7 million of conversion expenses were offset against the gross proceeds. Territorial Bancorp Inc. s common stock began trading on the NASDAQ Global Select Market under the symbol TBNK on July 13, 2009.

Upon completion of the conversion and reorganization, a special liquidation account was established in an amount equal to the total equity of Territorial Mutual Holding Company as of December 31, 2008. The liquidation account is to provide eligible account holders and supplemental eligible account holders who maintain their deposit accounts with Territorial Savings Bank after the conversion with a liquidation interest in the unlikely event of the complete liquidation of Territorial Savings Bank after the conversion. The liquidation account will be reduced annually to the extent that eligible account holders and supplemental eligible account holders have reduced their qualifying deposits. Subsequent increases will not restore an eligible account holder s or supplemental eligible account holder s interest in the liquidation account. In the event of a complete liquidation of Territorial Savings Bank, and only in such event, each account holder will be entitled to receive a distribution from the liquidation account in an amount proportionate to the adjusted qualifying account balances then held.

(3) Recently Adopted Accounting Pronouncements

In June 2011, the Financial Accounting Standards Board (FASB) amended the Comprehensive Income topic of the FASB Accounting Standards Codification (ASC). The amendment eliminated the option of presenting components of other comprehensive income as part of the statement of changes in stockholders equity. Nonowner changes in stockholders equity must be presented either in a continuous statement of comprehensive income or in two separate but consecutive statements. The amendment was effective for interim or annual periods beginning after December 15, 2011, with early

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adoption permitted. In December 2011, the FASB deferred the effective date of the part of this amendment requiring reclassifications out of accumulated other comprehensive income to be shown on the face of the financial statements to allow time for further deliberation. Until final reporting requirements were effective, previous disclosure requirements would remain in effect. The Company adopted this amendment on January 1, 2012, and other than the location of disclosures related to other comprehensive income, the adoption did not have a material effect on its consolidated financial statements. In February 2013, the FASB finalized the reporting requirements for reclassifications out of accumulated other comprehensive income. When an amount reclassified out of accumulated other comprehensive income is required to be reported in net income in its entirety, the effect on income statement items must be disclosed. When an amount reclassified out of accumulated other comprehensive income is not required to be reported in net income in its entirety in the same period, cross references to other required disclosures providing information about the transaction are required. This amendment was effective for reporting periods beginning after December 15, 2012. The Company adopted this amendment on January 1, 2013 and the adoption did not have a material effect on its consolidated financial statements.

In December 2011, the FASB amended the Balance Sheet topic of the FASB ASC. The amendment requires disclosures about the gross and net information related to instruments and transactions eligible for offset in the statement of financial position. The disclosures are meant to assist users of financial statements to more easily compare information that is presented based on the differing offsetting requirements of U.S. generally accepted accounting principles and International Financial Reporting Standards. In January 2013, the FASB issued a clarification that stated the amendment applies only to certain derivatives, repurchase and reverse repurchase agreements, and securities borrowing and securities lending transactions that are either offset or subject to an enforceable master netting arrangement or similar agreement. The amendment was effective for interim and annual periods beginning on or after January 1, 2013. The Company adopted this amendment on January 1, 2013 and the adoption did not have a material effect on its consolidated financial statements.

(4) Cash and Cash Equivalents

The table below presents the balances of cash and cash equivalents:

(Dollars in thousands)		**June 30, 2013**		**December 31, 2012**
Cash and due from banks	$	12,628	$	10,574
Interest-earning deposits in other banks		74,543		172,244
Cash and cash equivalents	$	87,171	$	182,818

Interest-earning deposits in other banks consist primarily of deposits at the Federal Reserve Bank.

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(5) Investment Securities

The amortized cost and fair values of investment securities are as follows:

(Dollars in thousands)		Carrying value		Gross unrealized Gains		Gross unrealized Losses		Estimated fair value
June 30, 2013:								
Held to maturity:								
U.S. government-sponsored mortgage-backed securities	$	582,146	$	12,590	$	(14,816)	$	579,920
Trust preferred securities		536		0		0		536
Total	$	582,682	$	12,590	$	(14,816)	$	580,456
December 31, 2012:								
Held to maturity:								
U.S. government-sponsored mortgage-backed securities	$	554,252	$	29,706	$	(254)	$	583,704
Trust preferred securities		421		0		0		421
Total	$	554,673	$	29,706	$	(254)	$	584,125

The carrying and estimated fair value of investment securities at June 30, 2013 are shown below. Incorporated in the maturity schedule are mortgage-backed and trust preferred securities, which are allocated using the contractual maturity as a basis. Expected maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

(Dollars in thousands)		Carrying Value		Estimated fair value
Held to maturity:				
Due within 5 years	$	1,730	$	1,751
Due after 5 years through 10 years		562		596
Due after 10 years		580,390		578,109
Total	$	582,682	$	580,456

Realized gains and losses and the proceeds from sales of securities available for sale, held to maturity and trading are shown in the table below. All sales of securities were U.S. government-sponsored mortgage-backed securities.

(Dollars in thousands)		Three months ended June 30, 2013		Three months ended June 30, 2012		Six months ended June 30, 2013		Six months ended June 30, 2012
Proceeds from sales	$	15,558	$	2,926	$	29,188	$	4,559
Gross gains		1,024		172		1,912		300
Gross losses		0		0		0		0

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During the three months ended June 30, 2013 and 2012, all sales were related to $14.5 million and $2.8 million, respectively, of held-to-maturity debt securities. During the six months ended June 30, 2013 and 2012, all sales were related to $27.3 million and $4.3 million, respectively, of held-to-maturity debt securities. The sale of these securities, for which the Company had already collected a substantial portion of the outstanding principal (at least 85%), is in accordance with the Investment topic of the FASB ASC and will not affect the historical cost basis used to account for the remaining securities in the held-to-maturity portfolio.

Investment securities with carrying values of $227.3 million and $221.3 million at June 30, 2013 and December 31, 2012, respectively, were pledged to secure public deposits, securities sold under agreements to repurchase and transaction clearing accounts.

Provided below is a summary of investment securities which were in an unrealized loss position at June 30, 2013 and December 31, 2012. The Company does not intend to sell these securities until such time as the value recovers or the securities mature and it is not more likely than not that the Company will be required to sell the securities prior to recovery of value or the securities mature.

	Less than 12 months		12 months or longer			Total	
Description of securities (Dollars in thousands)	**Fair value**	**Unrealized Losses**	**Fair value**	**Unrealized losses**	**Number of securities**	**Fair value**	**Unrealized losses**
June 30, 2013:							
Mortgage-backed securities	$ 295,810	$ 14,772	$ 2,593	$ 44	51	$ 298,403	$ 14,816
December 31, 2012:							
Mortgage-backed securities	$ 32,921	$ 253	$ 47	$ 1	21	$ 32,968	$ 254

Mortgage-Backed Securities. The unrealized losses on the Company s investment in mortgage-backed securities were caused by increases in market interest rates. All of the mortgage-backed securities are guaranteed by Freddie Mac or Fannie Mae, which are U.S. government-sponsored enterprises, or Ginnie Mae, which is a U.S. government agency. Since the decline in market value is attributable to changes in interest rates and not credit quality, and the Company does not intend to sell these investments until maturity and it is not more likely than not that the Company will be required to sell such investments prior to recovery of its amortized cost basis, the Company does not consider these investments to be other-than-temporarily impaired as of June 30, 2013 and December 31, 2012.

Trust Preferred Securities. At June 30, 2013, the Company owns two trust preferred securities, PreTSL XXIII and XXIV. The trust preferred securities represent investments in a pool of debt obligations issued primarily by holding companies for Federal Deposit Insurance Corporation-insured financial institutions. Both of these securities are classified in the Bank s held-to-maturity investment portfolio.

The trust preferred securities market is considered to be inactive as only three transactions have occurred over the past 18 months in the same tranche of securities owned by the Company. The Company used a discounted cash flow model to determine whether these securities are other-than-temporarily impaired. The assumptions used in preparing the discounted cash flow model include the following: estimated discount rates, estimated deferral and default rates on collateral, and estimated cash flows.

Based on the Company s review, the Company s investment in trust preferred securities did not incur additional impairment during the quarter ending June 30, 2013.

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PreTSL XXIV has a book value of $0. PreTSL XXIII has a book value of $536,000. The difference between the book value of $536,000 and the remaining amortized cost basis of $1.1 million is reported as other comprehensive loss and is related to noncredit factors such as the trust preferred securities market being inactive.

It is reasonably possible that the fair values of the trust preferred securities could decline in the near term if the overall economy and the financial condition of some of the issuers continue to deteriorate and the liquidity of these securities remains low. As a result, there is a risk that the Company s remaining amortized cost basis of $1.1 million on its trust preferred securities could be credit-related other-than-temporarily impaired in the near term. The impairment could be material to the Company s consolidated statements of income.

The table below provides a cumulative roll forward of credit losses recognized in earnings for debt securities held and not intended to be sold:

(Dollars in thousands)	**2013**	**2012**
Balance at January 1,	$ 5,885	$ 5,885
Credit losses on debt securities for which other-than-temporary impairment was not previously recognized	0	0
Balance at June 30,	$ 5,885	$ 5,885

The table below shows the components of comprehensive loss, net of taxes, resulting from other-than-temporarily impaired securities:

	June 30,	
(Dollars in thousands)	**2013**	**2012**
Noncredit losses on other-than-temporarily impaired securities, net of taxes	$ 376	$ 679

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(6) Loans Receivable and Allowance for Loan Losses

The components of loans receivable are as follows:

(Dollars in thousands)	June 30, 2013	December 31, 2012
Real estate loans:		
First mortgages:		
One- to four-family residential	$ 789,788	$ 741,334
Multi-family residential	5,712	6,888
Construction, commercial, and other	12,851	13,819
Home equity loans and lines of credit	15,070	15,202
Total real estate loans	823,421	777,243
Other loans:		
Loans on deposit accounts	395	493
Consumer and other loans	4,593	3,988
Total other loans	4,988	4,481
Less:		
Net unearned fees and discounts	(5,030)	(5,176)
Allowance for loan losses	(1,622)	(1,672)
	(6,652)	(6,848)
Loans receivable, net	$ 821,757	$ 774,876

The activity in the allowance for loan losses on loans receivable is as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
(Dollars in thousands)	2013	2012	2013	2012
Balance, beginning of period	$ 1,667	$ 1,529	$ 1,672	$ 1,541
Provision (reversal of allowance) for loan losses	(16)	(79)	2	5
	1,651	1,450	1,674	1,546
Charge-offs	(85)	(22)	(137)	(136)
Recoveries	56	29	85	47
Net charge-offs	(29)	7	(52)	(89)
Balance, end of period	$ 1,622	$ 1,457	$ 1,622	$ 1,457

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The table below presents the activity in the allowance for loan losses by portfolio segment:

(Dollars in thousands)	Residential Mortgage	Construction, Commercial and Other Mortgage Loans	Home Equity Loans and Lines of Credit	Consumer and Other	Unallocated	Totals
Three months ended June 30, 2013:						
Balance, beginning of period	$ 585	$ 818	$ 35	$ 107	$ 122	$ 1,667
Provision (reversal of allowance) for loan losses	(42)	(5)	(3)	20	14	(16)
	543	813	32	127	136	1,651
Charge-offs	(80)	0	0	(5)	0	(85)
Recoveries	50	0	3	3	0	56
Net charge-offs	(30)	0	3	(2)	0	(29)
Balance, end of period	$ 513	$ 813	$ 35	$ 125	$ 136	$ 1,622
Six months ended June 30, 2013:						
Balance, beginning of period	$ 590	$ 818	$ 35	$ 107	$ 122	$ 1,672
Provision (reversal of allowance) for loan losses	(68)	(5)	(6)	67	14	2
	522	813	29	174	136	1,674
Charge-offs	(81)	0	0	(56)	0	(137)
Recoveries	72	0	6	7	0	85
Net charge-offs	(9)	0	6	(49)	0	(52)
Balance, end of period	$ 513	$ 813	$ 35	$ 125	$ 136	$ 1,622

(Dollars in thousands)	Residential Mortgage	Construction, Commercial and Other Mortgage Loans	Home Equity Loans and Lines of Credit	Consumer and Other	Unallocated	Totals
Three months ended June 30, 2012:						
Balance, beginning of period	$ 544	$ 641	$ 34	$ 174	$ 136	$ 1,529
Provision (reversal of allowance) for loan losses	(12)	8	0	(61)	(14)	(79)
	532	649	34	113	122	1,450
Charge-offs	(4)	(8)	0	(10)	0	(22)
Recoveries	24	0	1	4	0	29
Net charge-offs	20	(8)	1	(6)	0	7
Balance, end of period	$ 552	$ 641	$ 35	$ 107	$ 122	$ 1,457
Six months ended June 30, 2012:						
Balance, beginning of period	$ 631	$ 285	$ 258	$ 291	$ 76	$ 1,541
Provision (reversal of allowance) for loan losses	(6)	364	(224)	(175)	46	5
	625	649	34	116	122	1,546
Charge-offs	(108)	(8)	(1)	(19)	0	(136)
Recoveries	35	0	2	10	0	47
Net charge-offs	(73)	(8)	1	(9)	0	(89)
Balance, end of period	$ 552	$ 641	$ 35	$ 107	$ 122	$ 1,457

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In 2012, the Company enhanced its methodology for reviewing its loan portfolio when calculating the general portion of the allowance for loan losses. The modification consisted of additional segmentation of the residential mortgage loan portfolio by items such as year of origination, loan-to-value ratios, owner or nonowner occupancy status and the purpose of the loan (purchase, cash-out refinance, no cash-out refinance or construction). As under our prior methodology, the allowance for loan loss for each segment of the loan portfolio is determined by calculating the historical loss of each segment for a two- to three-year look-back period and adding a qualitative adjustment for the following factors:

- Changes in lending policies and procedures;
- Changes in economic trends;
- Changes in types of loans in the loan portfolio;
- Changes in experience and ability of personnel in the loan origination and loan servicing departments;
- Changes in the number and amount of delinquent loans and classified assets;
- Changes in our internal loan review system;
- Changes in the value of underlying collateral for collateral dependent loans;
- Changes in any concentrations of credit; and
- External factors such as competition, legal and regulatory requirements on the level of estimated credit losses in the existing loan portfolio.

The Company also revised the qualitative factors that were used to determine the allowance for loan losses on construction, commercial and other mortgage loans, home equity loans and lines of credit and consumer and other loans. As a result of these modifications, the Company increased the portion of the allowance for loan losses attributable to construction, commercial and other mortgage loans and decreased the portion of the allowance for loan losses attributable to residential mortgages, home equity loans and lines of credit and consumer and other loans. The allocation of a portion of the allowance to one category of loans does not preclude its availability to absorb losses in other categories. The unallocated allowance is established for probable losses that have been incurred as of the reporting date but are not reflected in the allocated allowance.

Management considers the allowance for loan losses at June 30, 2013 to be at an appropriate level to provide for probable losses that can be reasonably estimated based on general and specific conditions. While the Company uses the best information it has available to make evaluations, future adjustments to the allowance may be necessary if conditions differ substantially from the information used in making the evaluations. To the extent actual outcomes differ from the estimates, additional provisions for credit losses may be required that would reduce future earnings. In addition, as an integral part of their examination process, the Office of the Comptroller of the Currency will periodically review the allowance for loan losses. The Office of the Comptroller of the Currency may require the Company to increase the allowance based on their analysis of information available at the time of their examination.

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The table below presents the balance in the allowance for loan losses and the recorded investment in loans by portfolio segment and based on impairment method:

(Dollars in thousands)	Residential Mortgage	Construction, Commercial and Other Mortgage Loans	Home Equity Loans and Lines of Credit	Consumer and Other	Unallocated	Totals
June 30, 2013:						
Allowance for loan losses:						
Ending allowance balance:						
Individually evaluated for impairment	$ 0	$ 0	$ 0	$ 0	$ 0	$ 0
Collectively evaluated for impairment	513	813	35	125	136	1,622
Total ending allowance balance	$ 513	$ 813	$ 35	$ 125	$ 136	$ 1,622
Loans:						
Ending loan balance:						
Individually evaluated for impairment	$ 7,736	$ 0	$ 162	$ 0	$ 0	$ 7,898
Collectively evaluated for impairment	782,783	12,793	14,916	4,989	0	815,481
Total ending loan balance	$ 790,519	$ 12,793	$ 15,078	$ 4,989	$ 0	$ 823,379
December 31, 2012:						
Allowance for loan losses:						
Ending allowance balance:						
Individually evaluated for impairment	$ 0	$ 0	$ 0	$ 0	$ 0	$ 0
Collectively evaluated for impairment	590	818	35	107	122	1,672
Total ending allowance balance	$ 590	$ 818	$ 35	$ 107	$ 122	$ 1,672
Loans:						
Ending loan balance:						
Individually evaluated for impairment	$ 6,775	$ 0	$ 160	$ 0	$ 0	$ 6,935
Collectively evaluated for impairment	736,297	13,784	15,051	4,481	0	769,613
Total ending loan balance	$ 743,072	$ 13,784	$ 15,211	$ 4,481	$ 0	$ 776,548

The table below presents the balance of impaired loans and the related amount of allocated loan loss allowances:

(Dollars in thousands)	June 30, 2013	December 31, 2012
Loans with no allocated allowance for loan losses	$ 7,898	$ 6,935
Loans with allocated allowance for loan losses	0	0
Total impaired loans	$ 7,898	$ 6,935

Amount of allocated loan loss allowance	$ 0	$ 0

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The table below presents the balance of impaired loans individually evaluated for impairment by class of loans:

(Dollars in thousands)	Recorded Investment	Unpaid Principal Balance
June 30, 2013:		
With no related allowance recorded:		
One- to four-family residential mortgages	$ 7,736	$ 8,232
Home equity loans and lines of credit	162	165
Total	$ 7,898	$ 8,397
December 31, 2012:		
With no related allowance recorded:		
One- to four-family residential mortgages	$ 6,775	$ 7,175
Home equity loans and lines of credit	160	165
Total	$ 6,935	$ 7,340

The table below presents the average recorded investment and interest income recognized on impaired loans by class of loans:

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
(Dollars in thousands)	Average Recorded Investment	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized
2013:				
With no related allowance recorded:				
One- to four-family residential mortgages	$ 7,793	$ 34	$ 7,806	$ 68
Home equity loans and lines of credit	161	0	161	0
Total	$ 7,954	$ 34	$ 7,967	$ 68
2012:				
With no related allowance recorded:				
One- to four-family residential mortgages	$ 4,869	$ 41	$ 4,918	$ 84
Construction, commercial and other mortgages	180	0	180	0
Home equity loans and lines of credit	160	2	160	3
Consumer and other	1	0	2	0
Total	$ 5,210	$ 43	$ 5,260	$ 87

There were no loans individually evaluated for impairment with a related allowance for loan loss as of June 30, 2013 or December 31, 2012. Loans individually evaluated for impairment do not have an allocated allowance for loan loss because they are written down to fair value.

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The table below presents the aging of loans and accrual status by class of loans:

(Dollars in thousands)	30 59 Days Past Due	60 89 Days Past Due	90 Days or Greater Past Due	Total Past Due	Loans Not Past Due	Total Loans	Nonaccrual Loans	Loans More Than 90 Days Past Due and Still Accruing
June 30, 2013:								
One- to four-family residential mortgages	$ 515	$ 0	$ 1,965	$ 2,480	$ 782,357	$ 784,837	$ 5,224	$ 0
Multi-family residential mortgages	0	0	0	0	5,682	5,682	0	0
Construction, commercial and other mortgages	0	0	0	0	12,793	12,793	0	0
Home equity loans and lines of credit	0	0	0	0	15,078	15,078	162	0
Loans on deposit accounts	0	0	0	0	395	395	0	0
Consumer and other	10	0	0	10	4,584	4,594	0	0
Total	$ 525	$ 0	$ 1,965	$ 2,490	$ 820,889	$ 823,379	$ 5,386	$ 0
December 31, 2012:								
One- to four-family residential mortgages	$ 2,298	$ 152	$ 2,044	$ 4,494	$ 731,730	$ 736,224	$ 4,246	$ 0
Multi-family residential mortgages	0	0	0	0	6,848	6,848	0	0
Construction, commercial and other mortgages	0	0	0	0	13,784	13,784	0	0
Home equity loans and lines of credit	44	0	0	44	15,167	15,211	160	0
Loans on deposit accounts	0	0	0	0	493	493	0	0
Consumer and other	78	2	0	80	3,908	3,988	0	0
Total	$ 2,420	$ 154	$ 2,044	$ 4,618	$ 771,930	$ 776,548	$ 4,406	$ 0

The Company primarily uses the aging of loans and accrual status to monitor the credit quality of its loan portfolio. When a mortgage loan becomes seriously delinquent (90 days or more contractually past due), it displays weaknesses that may result in a loss. As a loan becomes more delinquent, the likelihood of the borrower repaying the loan decreases and the loan becomes more collateral-dependent. A mortgage loan becomes collateral-dependent when the proceeds for repayment can be expected to come only from the sale or operation of the collateral and not from borrower repayments. Generally, appraisals are obtained after a loan becomes collateral-dependent or is five months delinquent. The carrying value of collateral-dependent loans is adjusted to the fair value of the collateral less selling costs. Any commercial real estate, commercial, construction or equity loan that has a loan balance in excess of a specified amount is also periodically reviewed to determine whether the loan exhibits any weaknesses and is performing in accordance with its contractual terms.

The Company had 19 nonaccrual loans with a book value of $5.4 million at June 30, 2013 and 19 nonaccrual loans with a book value of $4.4 million as of December 31, 2012. The Company collected interest on nonaccrual loans of $77,000 during the six months ended June 30, 2013, but due to regulatory requirements, we recorded it as a reduction of principal. The Company collected and recognized interest

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income on nonaccrual loans of $27,000 during the six months ended June 30, 2012. The Company would have recognized additional interest income of $141,000 and $123,000 during the six months ended June 30, 2013 and 2012, respectively, had the loans been accruing interest. The Company did not have any loans more than 90 days past due and still accruing interest as of June 30, 2013 and December 31, 2012.

The table below presents information related to loans modified in a troubled debt restructuring during the three and six months ended June 30, 2013 and 2012:

	2013			2012		
(Dollars in thousands)	Number of Loans	Pre-Modification Recorded Investment	Post-Modification Recorded Investment	Number of Loans	Pre-Modification Recorded Investment	Post-Modification Recorded Investment
Three months ended June 30:						
One- to four-family residential	1	$ 700	$ 700	0	$ 0	$ 0
Total	1	$ 700	$ 700	0	$ 0	$ 0
Six months ended June 30:						
One- to four-family residential	1	$ 700	$ 700	0	$ 0	$ 0
Total	1	$ 700	$ 700	0	$ 0	$ 0

There were no new troubled debt restructurings within the past 12 months that subsequently defaulted.

The Company had 20 troubled debt restructurings totaling $5.7 million as of June 30, 2013 that were considered to be impaired. This total included 19 one- to four-family residential mortgage loans totaling $5.5 million and one home equity loan for $162,000. Eight of the loans, totaling $2.5 million, are performing in accordance with their restructured terms and accruing interest at June 30, 2013. 11 of the loans, totaling $2.9 million, are performing in accordance with their restructured terms but not accruing interest at June 30, 2013. One of the loans, for $329,000, is more than 150 days delinquent and not accruing interest as of June 30, 2013. There were 20 troubled debt restructurings totaling $5.2 million as of December 31, 2012 that were considered to be impaired. This total included 19 one- to four-family residential mortgage loans totaling $5.1 million and one home equity loan for $160,000. Eight of the loans, totaling $2.5 million, are performing in accordance with their restructured terms and accruing interest at December 31, 2012. 11 of the loans, totaling $2.4 million, are performing in accordance with their restructured terms but not accruing interest at December 31, 2012. One of the loans, for $329,000, is more than 150 days delinquent and not accruing interest at December 31, 2012. Restructurings include deferrals of interest and/or principal payments and temporary or permanent reductions in interest rates due to the financial difficulties of the borrowers. We have no commitments to lend any additional funds to these borrowers.

Nearly all of our real estate loans are collateralized by real estate located in the State of Hawaii. Loan-to-value ratios on these real estate loans generally do not exceed 80% at the time of origination.

During the six months ended June 30, 2013 and 2012, the Company sold $47.1 million and $46.2 million, respectively, of mortgage loans held for sale and recognized gains of $1.0 million and $847,000, respectively. During the three months ended June 30, 2013 and 2012, the Company sold $22.3 million and $22.3 million, respectively, of mortgage loans held for sale and recognized gains of $380,000 and $406,000, respectively. The Company had 10 loans held for sale totaling $3.0 million at June 30, 2013 and six loans held for sale totaling $2.2 million at December 31, 2012.

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The Company serviced loans for others of $75.2 million at June 30, 2013 and $84.8 million at December 31, 2012. Of these amounts, $3.6 million and $5.1 million relate to securitizations for which the Company continues to hold the related mortgage-backed securities at June 30, 2013 and December 31, 2012, respectively. The amount of contractually specified servicing fees earned for the six-month periods ended June 30, 2013 and 2012 was $113,000 and $145,000, respectively. The amount of contractually specified servicing fees earned for the three-month periods ended June 30, 2013 and 2012 was $55,000 and $73,000, respectively. The fees are reported in service fees on loan and deposit accounts in the consolidated statements of income.

(7) Securities Sold Under Agreements to Repurchase

Securities sold under agreements to repurchase are treated as financings and the obligations to repurchase the identical securities sold are reflected as a liability with the dollar amount of securities underlying the agreements remaining in the asset accounts. Securities sold under agreements to repurchase are summarized as follows:

	June 30, 2013		December 31, 2012	
(Dollars in thousands)	**Repurchase liability**	**Weighted average rate**	**Repurchase liability**	**Weighted average rate**
Maturing:				
1 year or less	$ 18,000	4.87%	$ 23,000	4.40%
Over 1 year to 2 years	42,000	2.13	0	0.00
Over 2 years to 3 years	5,000	1.90	47,000	2.11
Total	$ 65,000	2.87%	$ 70,000	2.86%

During the quarter ended June 30, 2012, the Company prepaid $15.0 million of securities sold under agreements to repurchase and incurred a $198,000 prepayment penalty.

Below is a summary comparing the carrying value and fair value of securities pledged to secure repurchase agreements, the repurchase liability, and the amount at risk at June 30, 2013. The amount at risk is the greater of the carrying value or fair value over the repurchase liability. All the agreements to repurchase are with JP Morgan Securities and the securities pledged are issued and guaranteed by U.S. government-sponsored enterprises.

(Dollars in thousands)	**Carrying value of securities**	**Fair value of securities**	**Repurchase liability**	**Amount at risk**	**Weighted average months to maturity**
Maturing:					
Over 90 days	$ 76,751	$ 76,576	$ 65,000	$ 11,751	15

(8) Offsetting of Financial Liabilities

Securities sold under agreements to repurchase are subject to a conditional right of offset in the event of default. See Footnote 7, Securities Sold Under Agreements to Repurchase, for additional information.

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(Dollars in thousands)	Gross amount of recognized liabilities	Gross amount offset in the statement of financial position	Net amount of liabilities presented in the statement of financial position	Gross amount not offset in the statement of financial position: Financial instruments	Gross amount not offset in the statement of financial position: Cash collateral pledged	Net amount
June 30, 2013:						
Securities sold under agreements to repurchase	$ 65,000	$ 0	$ 65,000	$ 65,000	$ 0	$ 0
December 31, 2012:						
Securities sold under agreements to repurchase	$ 70,000	$ 0	$ 70,000	$ 70,000	$ 0	$ 0

(9) Employee Benefit Plans

The Company has a noncontributory defined benefit pension plan (Pension Plan) that covers substantially all employees with at least one year of service. Effective December 31, 2008, under approved changes to the Pension Plan, there were no further accruals of benefits for any participants and benefits will not increase with any additional years of service. Net periodic benefit cost, subsequent to December 31, 2008, has not been significant and is not disclosed in the table below.

In addition, the Company sponsors a Supplemental Employee Retirement Plan (SERP), a noncontributory supplemental retirement benefit plan, which covers certain current and former employees of the Company for amounts in addition to those provided under the Pension Plan.

The components of net periodic benefit cost were as follows:

	SERP Three Months Ended June 30,		SERP Six Months Ended June 30,	
(Dollars in thousands)	2013	2012	2013	2012
Net periodic benefit cost for the period				
Service cost	$ 42	$ 49	$ 83	$ 98
Interest cost	27	24	55	49
Expected return on plan assets	0	0	0	0
Amortization of prior service cost	0	0	0	0
Recognized actuarial loss	0	0	0	0
Recognized curtailment loss	0	0	0	0
Net periodic benefit cost	$ 69	$ 73	$ 138	$ 147

(10) Employee Stock Ownership Plan

Effective January 1, 2009, Territorial Savings Bank adopted an Employee Stock Ownership Plan (ESOP) for eligible employees. The ESOP borrowed $9.8 million from the Company and used those funds to acquire 978,650 shares, or 8%, of the total number of shares issued by the Company in its initial public offering. The shares were acquired at a price of $10.00 per share.

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The loan is secured by the shares purchased with the loan proceeds and will be repaid by the ESOP over the 20-year term of the loan with funds from Territorial Savings Bank s contributions to the ESOP and dividends payable on the shares. The interest rate on the ESOP loan is an adjustable rate equal to the prime rate, as published in The Wall Street Journal. The interest rate adjusts annually and will be the prime rate on the first business day of the calendar year.

Shares purchased by the ESOP are held by a trustee in an unallocated suspense account, and shares are released annually from the suspense account on a pro-rata basis as principal and interest payments are made by the ESOP to the Company. The trustee allocates the shares released among participants on the basis of each participant s proportional share of compensation relative to all participants. As shares are committed to be released from the suspense account, Territorial Savings Bank reports compensation expense based on the average fair value of shares released with a corresponding credit to stockholders equity. The shares committed to be released are considered outstanding for earnings per share computations. Compensation expense recognized for the three months ended June 30, 2013 and 2012 amounted to $261,000 and $248,000, respectively. Compensation expense recognized for the six months ended June 30, 2013 and 2012 amounted to $523,000 and $488,000, respectively.

Shares held by the ESOP trust were as follows:

	June 30, 2013	December 31, 2012
Allocated shares	215,058	191,577
Unearned shares	758,455	782,921
Total ESOP shares	973,513	974,498
Fair value of unearned shares, in thousands	$ 17,149	$ 17,890

The ESOP restoration plan is a nonqualified plan that provides supplemental benefits to certain executives who are prevented from receiving the full benefits contemplated by the employee stock ownership plan s benefit formula. The supplemental cash payments consist of payments representing shares that cannot be allocated to the participants under the ESOP due to IRS limitations imposed on tax-qualified plans. We accrue for these benefits over the period during which employees provide services to earn these benefits. For the three months ended June 30, 2013 and 2012, we accrued $31,000 and $18,000, respectively, for the ESOP restoration plan. For the six months ended June 30, 2013 and 2012, we accrued $120,000 and $104,000, respectively, for the ESOP restoration plan.

(11) Share-Based Compensation

On August 19, 2010, Territorial Bancorp Inc. adopted the 2010 Equity Incentive Plan, which provides for awards of stock options and restricted stock to key officers and outside directors. In accordance with the Compensation Stock Compensation topic of the FASB ASC, the cost of the 2010 Equity Incentive Plan is based on the fair value of the awards on the grant date. The fair value of restricted stock is based on the closing price of the Company s stock on the grant date. The fair value of stock options is estimated using a Black-Scholes option pricing model using assumptions for dividend yield, stock price volatility, risk-free interest rate and option term. These assumptions are based on our judgments regarding future events, are subjective in nature, and cannot be determined with precision. The cost of the awards will be recognized on a straight-line basis over the five- to six-year vesting period during which participants are required to provide services in exchange for the awards.

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The Company recognized compensation expense, measured as the fair value of the share-based award on the date of grant, on a straight-line basis over the vesting period. Share-based compensation is recorded in the statement of income as a component of salaries and employee benefits with a corresponding increase in shareholders equity. The table below presents information on compensation expense and the related tax benefit for all share-based awards:

(In thousands)	For the Three Months Ended June 30, 2013	For the Three Months Ended June 30, 2012	For the Six Months Ended June 30, 2013	For the Six Months Ended June 30, 2012
Compensation expense	$ 667	$ 660	$ 1,327	$ 1,323
Income tax benefit	314	386	652	722

Shares of our common stock issued under the 2010 Equity Incentive Plan shall be authorized but unissued shares. The maximum number of shares that will be awarded under the plan will be 1,712,637 shares.

Stock Options

The table below presents the stock option activity for the six months ended June 30, 2013 and 2012:

	Options	Weighted average exercise price	Remaining contractual life (years)	Aggregate intrinsic value (in thousands)
Options outstanding at December 31, 2012	832,954	$ 17.38	7.67	$ 4,554
Granted	0	0	0	0
Exercised	0	0	0	0
Forfeited	0	0	0	0
Expired	0	0	0	0
Options outstanding at June 30, 2013	832,954	$ 17.38	7.18	$ 4,353
Options outstanding at December 31, 2011	871,144	$ 17.36	8.67	$ 2,082
Granted	0	0	0	0
Exercised	41,275	17.36	0	171
Forfeited	0	0	0	0
Expired	0	0	0	0
Options outstanding at June 30, 2012	829,869	$ 17.36	8.17	$ 4,490
Options vested and exercisable at June 30, 2013	277,240	$ 17.37	7.17	$ 1,452

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The following summarizes certain stock option activity of the Company:

(In thousands)	For the Three Months Ended June 30, 2013	For the Three Months Ended June 30, 2012	For the Six Months Ended June 30, 2013	For the Six Months Ended June 30, 2012
Intrinsic value of stock options exercised	$ 0	$ 117	$ 0	$ 171
Cash received from stock options exercised	0	489	0	717
Tax benefits realized from stock options exercised	0	47	0	69
Total fair value of stock options that vested	0	0	0	0

As of June 30, 2013, the Company had $2.2 million of unrecognized compensation costs related to the stock option plan. The cost of the stock option plan is being amortized over the five- to six-year vesting period. The fair value of the Company s stock options was determined using the Black-Scholes option pricing formula. The following assumptions were used in the formula for options issued in 2012 and 2010:

	2012	2010
Expected volatility	35.82%	31.98%
Risk-free interest rate	1.27%	2.58%
Expected dividends	1.86%	1.61%
Expected life (in years)	6.50	6.75
Grant price for the stock options	$ 23.62	$ 17.36

Expected volatility - Based on the historical volatility of the Company s stock and a peer group of comparable thrifts.

Risk-free interest rate - Based on the U.S. Treasury yield curve and expected life of the options at the time of grant.

Expected dividends - Based on the quarterly dividend and the price of the Company s stock at the time of grant.

Expected life - Based on a weighted-average of the five- or six-year vesting period and the 10-year contractual term of the stock option plan.

Grant price for the stock options - Based on the closing price of the Company s stock at the time of grant.

There were no options granted in 2011 or the six months ended June 30, 2013.

Restricted Stock Awards

Restricted stock awards are accounted for as fixed grants using the fair value of the Company s stock at the time of grant. Unvested restricted stock awards may not be disposed of or transferred during the vesting period. Restricted stock awards carry with them the right to receive dividends.

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The table below presents the restricted stock award activity:

	Restricted stock awards	Weighted average grant date fair value
Nonvested at December 31, 2012	453,397	$ 17.39
Granted	0	0
Vested	0	0
Forfeited	0	0
Nonvested at June 30, 2013	453,397	$ 17.39
Nonvested at December 31, 2011	563,994	$ 17.36
Granted	0	0
Vested	0	0
Forfeited	0	0
Nonvested at June 30, 2012	563,994	$ 17.36

As of June 30, 2013, the Company had $6.2 million of unrecognized compensation costs related to restricted stock awards. The cost of the restricted stock awards is being amortized over the five- or six-year vesting period.

(12) Earnings Per Share

The table below presents the information used to compute basic and diluted earnings per share:

	Three Months Ended June 30,		Six Months Ended June 30,	
(Dollars in thousands, except share data)	**2013**	**2012**	**2013**	**2012**
Net income	$ 3,661	$ 3,846	$ 7,302	$ 7,386
Weighted-average number of shares used in:				
Basic earnings per share	9,841,162	10,135,179	9,879,050	10,163,647
Dilutive common stock equivalents:				
Stock options and restricted stock units	229,442	168,184	214,640	142,104
Diluted earnings per share	10,070,604	10,303,363	10,093,690	10,305,751
Net income per common share, basic	$ 0.37	$ 0.38	$ 0.74	$ 0.73
Net income per common share, diluted	$ 0.36	$ 0.37	$ 0.72	$ 0.72

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(13) Other Comprehensive Loss

The table below presents the changes in the components of accumulated other comprehensive loss, net of taxes:

(Dollars in thousands)	Unfunded pension liability	Noncredit related losses on securities not expected to be sold	Unrealized loss on securities	Total
Balances at December 31, 2012	$ 3,792	$ 445	$ 96	$ 4,333
Other comprehensive income before reclassifications	0	(69)	(18)	(87)
Amounts reclassified from accumulated other comprehensive loss	0	0	0	0
Net current period other comprehensive income	0	(69)	(18)	(87)
Balances at June 30, 2013	$ 3,792	$ 376	$ 78	$ 4,246
Balances at December 31, 2011	$ 2,966	$ 679	$ 125	$ 3,770
Other comprehensive income before reclassifications	0	0	(10)	(10)
Amounts reclassified from accumulated other comprehensive loss	0	0	0	0
Net current period other comprehensive income	0	0	(10)	(10)
Balances at June 30, 2012	$ 2,966	$ 679	$ 115	$ 3,760

The table below presents the tax effect on each component of accumulated other comprehensive loss:

	Six Months Ended June 30,					
	2013			2012		
(Dollars in thousands)	Pretax amount	Tax	After tax amount	Pretax amount	Tax	After tax amount
Unfunded pension liability	$ 6,295	$ (2,503)	$ 3,792	$ 4,954	$ (1,988)	$ 2,966
Noncredit related losses on securities not expected to be sold	602	(226)	376	1,106	(427)	679
Unrealized loss on securities	131	(53)	78	193	(78)	115
Total	$ 7,028	$ (2,782)	$ 4,246	$ 6,253	$ (2,493)	$ 3,760

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(14) Fair Value of Financial Instruments

In accordance with the Fair Value Measurements and Disclosures topic of the FASB ASC, the Company groups its financial assets and liabilities at fair value into three levels based on the markets in which the financial assets and liabilities are traded and the reliability of the assumptions used to determine fair value as follows:

- Level 1 Valuation is based upon quoted prices (unadjusted) for identical assets or liabilities traded in active markets. A quoted price in an active market provides the most reliable evidence of fair value and shall be used to measure fair value whenever available.

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

- Level 3 Valuation is generated from model-based techniques that use significant assumptions not observable in the market. These unobservable assumptions reflect management s own estimates of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include use of discounted cash flow models and similar techniques that require the use of significant judgment or estimation.

In accordance with the Fair Value Measurements and Disclosures topic, the Company bases its fair values on the price that it would expect to receive if an asset were sold or the price that it would expect to pay to transfer a liability in an orderly transaction between market participants at the measurement date. Also as required, the Company maximizes the use of observable inputs and minimizes the use of unobservable inputs when developing fair value measurements.

The Company uses fair value measurements to determine fair value disclosures. Investment securities held for sale and derivatives are recorded at fair value on a recurring basis. From time to time, the Company may be required to record other financial assets at fair value on a nonrecurring basis, such as loans held for sale, impaired loans and investments, and mortgage servicing assets. These nonrecurring fair value adjustments typically involve application of the lower of cost or fair value accounting or write-downs of individual assets.

Cash and Cash Equivalents, Accrued Interest Receivable, Accounts Payable and Accrued Expenses, Current Income Taxes Payable, and Advance Payments by Borrowers for Taxes and Insurance. The carrying amount approximates fair value because of the short maturity of these instruments.

Investment Securities. The estimated fair values of U.S. government-sponsored mortgage-backed securities are considered Level 2 inputs because the valuation for investment securities utilized pricing models that varied based on asset class and included trade, bid and other observable market information.

The trust preferred securities represent investments in a pool of debt obligations issued primarily by holding companies for Federal Deposit Insurance Corporation-insured financial institutions. The trust preferred securities market is considered to be inactive since there have been only three sales transactions of similar rated securities over the past 18 months and no new issues of pooled trust preferred securities have occurred since 2007. The fair value of our trust preferred securities was determined using a discounted cash flow model. Our model used a discount rate equal to three-month LIBOR plus 20.00% and provided a fair value estimate of $15.13 per $100 of par value for PreTSL XXIII.

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The discounted cash flow analysis included a review of all issuers within the pool. The fair value of the trust preferred securities are classified as Level 3 inputs because they are based on discounted cash flow models.

FHLB Stock. FHLB stock, which is redeemable for cash at par value, is reported at its par value.

Loans. The fair value of loans is estimated by discounting the future cash flows using the current rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities. The fair value of loans is not based on the concept of exit price.

Loans Held for Sale. The fair value of loans held for sale is determined based on the prices quoted in the secondary market for similar loans.

Deposits. The fair value of checking and Super NOW savings accounts, passbook accounts, and certain money market deposits is the amount payable on demand at the reporting date. The fair value of fixed-maturity certificates of deposit is estimated by discounting future cash flows using the rates currently offered for deposits with similar remaining maturities.

Advances from the FHLB and Securities Sold Under Agreements to Repurchase. Fair value is estimated by discounting future cash flows using the rates currently offered to the Company for debt with similar remaining maturities.

Interest Rate Contracts. The Company may enter into interest rate lock commitments with borrowers on loans intended to be sold. To manage interest rate risk on the lock commitments, the Company may also enter into forward loan sale commitments. The interest rate lock commitments and forward loan sale commitments are treated as derivatives and are recorded at their fair value determined by referring to prices quoted in the secondary market for similar contracts. Interest rate contracts that are classified as assets are included with prepaid expenses and other assets on the consolidated balance sheet while interest rate contracts that are classified as liabilities are included with accounts payable and accrued expenses.

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The estimated fair values of the Company s financial instruments are as follows:

(Dollars in thousands)	Carrying amount	Fair value	Fair Value Measurements Using Level 1	Level 2	Level 3
June 30, 2013					
Assets					
Cash and cash equivalents	$ 87,171	$ 87,171	$ 87,171	$ 0	$ 0
Investment securities held to maturity	582,682	580,456	0	579,920	536
FHLB stock	11,908	11,908	11,908	0	0
Loans held for sale	2,991	3,002	0	3,002	0
Loans receivable, net	821,757	848,585	0	0	848,585
Accrued interest receivable	4,370	4,370	4,370	0	0
Interest rate contracts	197	197	0	197	0
Liabilities					
Deposits	1,235,456	1,222,929	1,052,910	0	170,019
Advances from the Federal Home Loan Bank	15,000	15,172	0	0	15,172
Securities sold under agreements to repurchase	65,000	66,509	0	0	66,509
Accounts payable and accrued expenses (excluding interest rate contracts)	23,283	23,283	23,283	0	0
Interest rate contracts	217	217	0	217	0
Current income taxes payable	1,857	1,857	1,857	0	0
Advance payments by borrowers for taxes and insurance	3,575	3,575	3,575	0	0
December 31, 2012					
Assets					
Cash and cash equivalents	$ 182,818	$ 182,818	$ 182,818	$ 0	$ 0
Investment securities held to maturity	554,673	584,125	0	583,704	421
FHLB stock	12,128	12,128	12,128	0	0
Loans held for sale	2,220	2,335	0	2,335	0
Loans receivable, net	774,876	831,734	0	0	831,734
Accrued interest receivable	4,367	4,367	4,367	0	0
Interest rate contracts	124	124	0	124	0
Liabilities					
Deposits	1,237,847	1,239,385	1,032,467	0	206,918
Advances from the Federal Home Loan Bank	20,000	20,397	0	0	20,397
Securities sold under agreements to repurchase	70,000	72,340	0	0	72,340
Accounts payable and accrued expenses (excluding interest rate contracts)	22,906	22,906	22,906	0	0
Interest rate contracts	111	111	0	111	0
Current income taxes payable	1,152	1,152	1,152	0	0
Advance payments by borrowers for taxes and insurance	3,639	3,639	3,639	0	0

At June 30, 2013 and December 31, 2012, neither the commitment fees received on commitments to extend credit nor the fair value thereof was material to the consolidated financial statements of the Company.

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The table below presents the balance of assets and liabilities measured at fair value on a recurring basis:

(Dollars in thousands)		Level 1	Level 2	Level 3	Total
June 30, 2013					
Interest rate contracts	assets	$ 0	$ 197	$ 0	$ 197
Interest rate contracts	liabilities	0	(217)	0	(217)
December 31, 2012					
Interest rate contracts	assets	$ 0	$ 124	$ 0	$ 124
Interest rate contracts	liabilities	0	(111)	0	(111)

The fair value of interest rate contracts was determined by referring to prices quoted in the secondary market for similar contracts. Gains and losses are included in gain on sale of loans in the consolidated statements of income.

The table below presents the balance of assets measured at fair value on a nonrecurring basis as of June 30, 2013 and December 31, 2012 and the related losses for the six months ended June 30, 2013 and the year ended December 31, 2012:

(Dollars in thousands)	Level 1	Level 2	Level 3	Total	Total Gains/ (Losses)
June 30, 2013					
Impaired loans	$ 0	$ 145	$ 4,750	$ 4,895	$ (20)
Trust preferred securities	0	0	536	536	115
December 31, 2012:					
Impaired loans	$ 0	$ 468	$ 4,907	$ 5,375	$ (222)
Mortgage servicing assets	0	0	651	651	(220)
Trust preferred securities	0	0	421	421	389

The fair value of impaired loans that are considered to be collateral-dependent is determined using the value of collateral less estimated selling costs. The fair value of impaired loans not considered to be collateral-dependent is determined using a discounted cash flow analysis. Assumptions used in the analysis include the discount rate and projected cash flows. Gains and losses on impaired loans are included in the provision for loan losses in the consolidated statements of income. Mortgage servicing assets are valued using a discounted cash flow model. Assumptions used in the model include mortgage prepayment speeds, discount rates, cost of servicing and ancillary income. Losses on mortgage servicing assets are included in service fees on loan and deposit accounts in the consolidated statements of income. The fair value of trust preferred securities is determined using a discounted cash flow model. The assumptions used in the discounted cash flow model are discussed above. Gains and losses on trust preferred securities that are credit related are included in net other-than-temporary impairment losses in the consolidated statements of income. Gains and losses on trust preferred securities that are not credit related are included in other comprehensive income in the consolidated statements of comprehensive income.

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The table below presents the significant unobservable inputs for Level 3 nonrecurring fair value measurements:

(Dollars in thousands)	Fair Value	Valuation Technique	Unobservable Input	Value
June 30, 2013:				
Impaired loans non-collateral dependent	$ 4,750	Discounted cash flow	Discount rate (1)	3.15% - 6.94%
Trust preferred securities	536	Discounted cash flow	Discount rate	Three-month LIBOR plus 20%
December 31, 2012:				
Impaired loans non-collateral dependent	$ 4,907			