NORTHEAST BANCORP /ME/
Form 10-Q
November 13, 2015

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

FORM 10-Q

Quarterly report pursuant to Section 13 or 15 (d) of the Securities Exchange Act of 1934

For the quarterly period ended September 30, 2015

Commission File Number: 1-14588

Northeast Bancorp

(Exact name of registrant as specified in its charter)

Maine	**01-0425066**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
500 Canal Street, Lewiston, Maine	**04240**
(Address of Principal executive offices)	**(Zip Code)**

(207) 786-3245

Registrant's telephone number, including area code

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§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 whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definition of "accelerated filer", "large accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (check one): Large accelerated filer __ Accelerated filer __ Non-accelerated filer ___ Smaller Reporting Company

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date. As of November 8, 2015 the registrant had outstanding 8,559,312 shares of voting common stock, $1.00 par value per share and 1,022,717 shares of non-voting common stock, $1.00 par value per share.

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PART 1- FINANCIAL INFORMATION

Item 1. Financial Statements (Unaudited)

NORTHEAST BANCORP AND SUBSIDIARY CONSOLIDATED BALANCE SHEETS
(Unaudited)
(Dollars in thousands, except share data)

	September 30, 2015	June 30, 2015
Assets		
Cash and due from banks	$ 2,979	$ 2,789
Short-term investments	83,234	87,061
Total cash and cash equivalents	86,213	89,850
Available-for-sale securities, at fair value	101,344	101,908
Residential real estate loans held for sale	5,366	7,093
SBA loans held for sale	2,170	1,942
Total loans held for sale	7,536	9,035
Loans	625,842	612,137
Less: Allowance for loan losses	2,065	1,926
Loans, net	623,777	610,211
Premises and equipment, net	8,460	8,253
Real estate owned and other repossessed collateral, net	1,279	1,651
Federal Home Loan Bank stock, at cost	4,102	4,102
Intangible assets, net	2,078	2,209
Bank owned life insurance	15,387	15,276
Other assets	8,073	8,223
Total assets	$ 858,249	$ 850,718
Liabilities and Stockholders' Equity		
Liabilities		

Deposits:		
Demand	$ 62,687	$ 60,383
Savings and interest checking	106,679	100,134
Money market	182,690	168,527
Time	341,422	345,715
Total deposits	693,478	674,759
Federal Home Loan Bank advances	30,159	30,188
Wholesale repurchase agreements	-	10,037
Short-term borrowings	2,479	2,349
Junior subordinated debentures issued to affiliated trusts	8,674	8,626
Capital lease obligation	1,312	1,368
Other liabilities	8,443	10,664
Total liabilities	744,545	737,991
Commitments and contingencies	-	-
Stockholders' equity		
Preferred stock, $1.00 par value, 1,000,000 shares authorized; no shares issued and outstanding at September 30, 2015 and June 30, 2015	-	-
Voting common stock, $1.00 par value, 25,000,000 shares authorized; 8,569,612 and 8,575,144 shares issued and outstanding at September 30, 2015 and June 30, 2015, respectively	8,570	8,575
Non-voting common stock, $1.00 par value, 3,000,000 shares authorized; 1,022,717 and 1,012,739 shares issued and outstanding at September 30, 2015 and June 30, 2015, respectively	1,023	1,013
Additional paid-in capital	84,937	85,506
Retained earnings	20,693	18,921
Accumulated other comprehensive loss	(1,519)	(1,288)
Total stockholders' equity	113,704	112,727
Total liabilities and stockholders' equity	$ 858,249	$ 850,718

The accompanying notes are an integral part of these unaudited consolidated financial statements.

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NORTHEAST BANCORP AND SUBSIDIARY CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)
(Dollars in thousands, except share data)

	Three Months Ended September 30,	
	2015	2014
Interest and dividend income:		
Interest and fees on loans	$10,790	$10,922
Interest on available-for-sale securities	228	244
Other interest and dividend income	95	66
Total interest and dividend income	11,113	11,232
Interest expense:		
Deposits	1,365	1,130
Federal Home Loan Bank advances	260	323
Wholesale repurchase agreements	67	73
Short-term borrowings	9	9
Junior subordinated debentures issued to affiliated trusts	154	206
Obligation under capital lease agreements	17	20
Total interest expense	1,872	1,761
Net interest and dividend income before provision for loan losses	9,241	9,471
Provision for loan losses	169	320
Net interest and dividend income after provision for loan losses	9,072	9,151
Noninterest income:		
Fees for other services to customers	408	394
Gain on sales of residential loans held for sale	560	584
Gain on sales of portfolio loans	675	80
Loss recognized on real estate owned and other repossessed collateral, net	(59)	(23)
Bank-owned life insurance income	112	109
Other noninterest income	9	10
Total noninterest income	1,705	1,154
Noninterest expense:		
Salaries and employee benefits	4,256	4,533
Occupancy and equipment expense	1,290	1,202
Professional fees	430	308

Data processing fees	349	345
Marketing expense	70	69
Loan acquisition and collection expense	451	274
FDIC insurance premiums	114	124
Intangible asset amortization	131	166
Other noninterest expense	719	689
Total noninterest expense	7,810	7,710
Income before income tax expense	2,967	2,595
Income tax expense	1,100	948
Net income	$1,867	$1,647
Weighted average shares outstanding during the period:		
Basic	9,562,812	10,180,038
Diluted	9,562,812	10,180,038
Earnings per common share:		
Basic	$0.20	$0.16
Diluted	0.20	0.16
Cash dividends declared per common share	$0.01	$0.01

The accompanying notes are an integral part of these unaudited consolidated financial statements.

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NORTHEAST BANCORP AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited)
(Dollars in thousands)

	Three Months Ended September 30, 2015	2014
Net income	$1,867	$1,647
Other comprehensive loss, before tax:		
Available-for-sale securities:		
Change in net unrealized gain (loss) on available-for-sale securities	466	(275)
Reclassification adjustment for net gains included in net income	-	-
Total available-for-sale securities	466	(275)
Derivatives and hedging activities:		
Change in accumulated loss on effective cash flow hedges	(838)	(272)
Reclassification adjustments for net gains included in net income	-	(9)
Total derivatives and hedging activities	(838)	(281)
Total other comprehensive loss, before tax	(372)	(556)
Income tax benefit related to other comprehensive loss	(141)	(188)
Other comprehensive loss, net of tax	(231)	(368)
Comprehensive income	$1,636	$1,279

The accompanying notes are an integral part of these unaudited consolidated financial statements.

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NORTHEAST BANCORP AND SUBSIDIARY CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
(Unaudited)
(Dollars in thousands, except share data)

	Preferred Stock		Voting Common Stock		Non-voting Common Stock		Additional Paid-in	Retained	Accumulated Other Comprehensive	Total Stockholders'
	Shares	Amount	Shares	Amount	Shares	Amount	Capital	Earnings	Loss	Equity
Balance at June 30, 2014	-	$ -	9,260,331	$ 9,260	880,963	$ 881	$ 90,914	$ 12,294	$ (1,283)	$ 112,066
Net income	-	-	-	-	-	-	-	1,647	-	1,647
Other comprehensive loss, net of tax	-	-	-	-	-	-	-	-	(368)	(368)
Common stock repurchased	-	-	(14,400)	(14)	-	-	(120)	-	-	(134)
Conversion of voting common stock to non-voting common stock	-	-	-	-	-	-	-	-	-	-
Dividends on common stock at $0.01 per share	-	-	-	-	-	-	-	(102)	-	(102)
Stock-based compensation	-	-	-	-	-	-	136	-	-	136
Issuance of restricted common stock	-	-	128,000	128	-	-	(128)	-	-	-
Forfeiture of restricted common stock	-	-	(6,860)	(7)	-	-	7	-	-	-
Balance at September 30, 2014	-	$ -	9,367,071	$ 9,367	880,963	$ 881	$ 90,809	$ 13,839	$ (1,651)	$ 113,245

Balance at June 30, 2015	-	$ -	8,575,144	$ 8,575	1,012,739	$ 1,013	$ 85,506	$ 18,921	$ (1,288)	$ 112,727
Net income	-	-	-	-	-	-	-	1,867	-	1,867
Other comprehensive loss, net of tax	-	-	-	-	-	-	-	-	(231)	(231)
Common stock repurchased	-	-	(52,500)	(53)	-	-	(495)	-	-	(548)
Conversion of voting common stock to non-voting common stock	-	-	(9,978)	(10)	9,978	10	-	-	-	-
Dividends on common stock at $0.01 per share	-	-	-	-	-		-	(95)	-	(95)
Stock-based compensation	-	-	-	-	-	-	(16)	-	-	(16)
Issuance of restricted common stock	-	-	97,500	98	-	-	(98)	-	-	-
Forfeiture of restricted common stock	-	-	(40,554)	(40)	-	-	40	-	-	-
Balance at September 30, 2015	-	$ -	8,569,612	$ 8,570	1,022,717	$ 1,023	$ 84,937	$ 20,693	$ (1,519)	$ 113,704

The accompanying notes are an integral part of these unaudited consolidated financial statements.

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NORTHEAST BANCORP AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)
(Dollars in thousands)

	Three Months Ended September 30, 2015	2014
Operating activities:		
Net income	$1,867	$1,647
Adjustments to reconcile net income to net cash (used in) provided by operating activities:		
Provision for loan losses	169	320
Loss (gain) on sale and impairment of real estate owned and other repossessed collateral, net	53	(5)
Accretion of fair value adjustments on loans, net	(2,248)	(3,097)
Accretion of fair value adjustments on deposits, net	(3)	(64)
Accretion of fair value adjustments on borrowings, net	(18)	(47)
Originations of residential loans held for sale	(26,877)	(27,676)
Net proceeds from sales of residential loans held for sale	29,164	31,136
Gain on sales of residential loans held for sale, net	(560)	(584)
Gain on sales of portfolio loans, net	(675)	(80)
Amortization of intangible assets	131	166
Bank-owned life insurance income, net	(112)	(109)
Depreciation of premises and equipment	405	432
Loss on sale and disposal of premises and equipment, net	6	28
Stock-based compensation	(16)	136
Amortization of available-for-sale securities, net	222	262
Changes in other assets and liabilities:		
Other assets	521	(367)
Other liabilities	(3,059)	(1,284)
Net cash (used in) provided by operating activities	(1,030)	814
Investing activities:		
Purchases of available-for-sale securities	(5,000)	-
Proceeds from maturities and principal payments on available-for-sale securities	5,808	2,994
Loan purchases	(23,458)	(13,167)
Proceeds from sales of portfolio loans	6,154	793
Loan originations, principal collections, and purchased loan paydowns, net	5,712	(10,213)
Purchases and disposals of premises and equipment, net	(618)	(105)
Proceeds from sales of real estate owned and other repossessed collateral	642	88
Net cash used in investing activities	(10,760)	(19,610)
Financing activities:		
Net increase in deposits	18,722	19,530
Net increase in short-term borrowings	130	820

Repurchase of common stock	(548)	(134)
Dividends paid on common stock	(95)	(102)
Repayment of wholesale repurchase agreements	(10,000)	-
Repayment of capital lease obligation	(56)	(47)
Net cash provided by financing activities	8,153	20,067
Net (decrease) increase in cash and cash equivalents	(3,637)	1,271
Cash and cash equivalents, beginning of period	89,850	82,259
Cash and cash equivalents, end of period	$86,213	$83,530
Supplemental schedule of noncash investing and financing activities:		
Transfers from loans to real estate owned and other repossessed collateral	$323	$209

The accompanying notes are an integral part of these unaudited consolidated financial statements.

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NORTHEAST BANCORP AND SUBSIDIARY

Notes to Unaudited Consolidated Financial Statements

September 30, 2015

1. Basis of Presentation

The accompanying unaudited condensed and consolidated interim financial statements include the accounts of Northeast Bancorp (“Northeast” or the “Company”) and its wholly-owned subsidiary, Northeast Bank (the “Bank”).

These financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and notes required by GAAP for complete financial statements. In the opinion of management, the accompanying consolidated financial statements contain all adjustments (consisting principally of normal recurring accruals) considered necessary for a fair presentation of the Company's financial position, results of operations, and cash flows for the interim periods presented. These financial statements and notes should be read in conjunction with the audited consolidated financial statements and notes thereto for the fiscal year ended June 30, 2015 (“Fiscal 2015”) included in the Company's Annual Report on Form 10-K filed with the Securities and Exchange Commission.

2. Recent Accounting Pronouncements

In January 2014, the FASB issued ASU No. 2014-01, *Investments—Equity Method and Joint Ventures (Topic 323): Accounting for Investments in Qualified Affordable Housing Projects* ("ASU 2014-01"). The amendments in ASU 2014-01 provide guidance on accounting for investments by a reporting entity in flow-through limited liability entities that manage or invest in affordable housing projects that qualify for the low-income housing tax credit. The amendments permit reporting entities to make an accounting policy election to account for their investments in qualified affordable housing projects using the proportional amortization method if certain conditions are met. Under the proportional amortization method, an entity amortizes the initial cost of the investment in proportion to the tax credits and other tax benefits received and recognizes the net investment performance in the income statement as a component of income tax expense (benefit). The amendments are effective for fiscal years, and interim periods within those years, beginning after December 15, 2014 and should be applied retrospectively to all periods presented. Early adoption is permitted. The Company adopted the standard in the current period. See Part I. Item I. “Notes to Unaudited Consolidated Financial Statements – Note 6: Investments in Qualified Affordable Housing Projects” for further discussion and related effect.

In May 2014, the Financial Accounting Standards Board ("FASB") issued ASU 2014-09*, Revenue from Contracts with Customers (Topic 606)* ("ASU 2014-09"). ASU 2014-09 implements a common revenue standard that clarifies the principles for recognizing revenue. The core principle of ASU 2014-09 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. To achieve that core principle, an entity should apply the following steps: (i) identify the contract(s) with a customer, (ii) identify the performance obligations in the contract, (iii) determine the transaction price, (iv) allocate the transaction price to the performance obligations in the contract and (v) recognize revenue when (or as) the entity satisfies a performance obligation. ASU 2014-09 is effective for annual periods beginning after December 15, 2016 and is not expected to have a significant impact on the Company's financial statements.

In June 2014, the FASB issued ASU 2014-11, *Transfers and Servicing (Topic 860): Repurchase-to-Maturity Transactions, Repurchase Financings, and Disclosures* ("ASU 2014-11"). ASU 2014-11 requires that repurchase-to-maturity transactions be accounted for as secured borrowings consistent with the accounting for other repurchase agreements. In addition, ASU 2014-11 requires separate accounting for repurchase financings, which entails the transfer of a financial asset executed contemporaneously with a repurchase agreement with the same counterparty. ASU 2014-11 requires entities to disclose certain information about transfers accounted for as sales in transactions that are economically similar to repurchase agreements. In addition, ASU 2014-11 requires disclosures related to collateral, remaining contractual tenor and of the potential risks associated with repurchase agreements, securities lending transactions and repurchase-to-maturity transactions. ASU 2014-11 was effective July 1, 2015 and did not have a significant impact on the Company's financial statements.

In August 2014, the FASB issued ASU 2014-14, *Receivables - Troubled Debt Restructurings by Creditors (Subtopic 310-40): Classification of Certain Government-Guaranteed Mortgage Loans upon Foreclosure ("*ASU 2014-14*").* ASU 2014-14 affects creditors that hold government-guaranteed mortgage loans, including those guaranteed by the Federal Housing Administration (FHA) of the U.S. Department of Housing and Urban Development (HUD), and the U.S. Department of Veterans Affairs (VA). The update requires that, upon foreclosure, a guaranteed mortgage loan be derecognized and a separate other receivable be recognized when specific criteria are met. ASU 2014-14 is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2014. The adoption of this guidance did not have a significant impact on the Company's financial statements.

In May 2015, the FASB issued ASU 2015-07, *Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)* ("ASU 2015-07"). The amendment affects reporting entities that elect to measure the fair value of an investment using the net asset value per share as a practical expedient. The Company adopted the standard in the current period. See Part I. Item I. "Notes to Unaudited Consolidated Financial Statements – Note 11: Fair Value Measurements" for further discussion and related effect.

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3. Securities Available-for-Sale

The following presents a summary of the amortized cost, gross unrealized holding gains and losses, and fair value of securities available for sale.

	September 30, 2015			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(Dollars in thousands)			
U.S. Government agency securities	$45,134	$ 34	$ (1)	$45,167
Agency mortgage-backed securities	51,562	21	(438)	51,145
Other investments measured at net asset value	5,018	14	-	5,032
	$101,714	$ 69	$ (439)	$101,344

	June 30, 2015			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(Dollars in thousands)			
U.S. Government agency securities	$48,191	$ 40	$ (1)	$48,230
Agency mortgage-backed securities	54,553	2	(877)	53,678
Other investments measured at net asset value	-	-	-	-
	$102,744	$ 42	$ (878)	$101,908

When securities are sold, the adjusted cost of the specific security sold is used to compute the gain or loss on sale. There were no securities sold during the three months ended September 30, 2015 or 2014. At September 30, 2015, investment securities with a fair value of approximately $3.0 million were pledged as collateral to secure outstanding borrowings.

The following summarizes the Company's gross unrealized losses and fair values aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position.

September 30, 2015					
Less than 12 Months		More than 12 Months		Total	
Fair	Unrealized	Fair	Unrealized	Fair	Unrealized

	Value	Losses	Value	Losses	Value	Losses
	(Dollars in thousands)					
U.S. Government agency securities	$2,997	$ (1)	$-	$ -	$2,997	$ (1)
Agency mortgage-backed securities	7,871	(34)	39,617	(404)	47,488	(438)
	$10,868	$ (35)	$39,617	$ (404)	$50,485	$ (439)

	June 30, 2015					
	Less than 12 Months		More than 12 Months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
	(Dollars in thousands)					
U.S. Government agency securities	$2,999	$ (1)	$-	$ -	$2,999	$ (1)
Agency mortgage-backed securities	10,295	(106)	41,349	(771)	51,644	(877)
	$13,294	$ (107)	$41,349	$ (771)	$54,643	$ (878)

There were no other-than-temporary impairment losses on securities during the three months ended September 30, 2015 or 2014.

At September 30, 2015, the Company had sixteen securities in a continuous loss position for greater than twelve months. At September 30, 2015, all of the Company’s available-for-sale securities were issued or guaranteed by either government agencies or government-sponsored enterprises. The decline in fair value of the Company’s available-for-sale securities at September 30, 2015 is attributable to changes in interest rates.

Management of the Company, in addition to considering current trends and economic conditions that may affect the quality of individual securities within the Company’s investment portfolio, also considers the Company’s ability and intent to hold such securities to maturity or recovery of cost. At September 30, 2015, it is more likely than not that the Company will not sell or be required to sell the investment securities before recovery of its amortized cost. As such, management does not believe any of the Company’s available-for-sale securities are other-than-temporarily impaired at September 30, 2015.

The investment measured at net asset value is a fund that seeks to invest in securities either issued or guaranteed by the U.S. government or its agencies. The underlying composition of the fund is primarily government agencies or other investment-grade investments. The effective duration of the investments is 4.32 years.

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The amortized cost and fair values of available-for-sale debt securities by contractual maturity are shown below as of September 30, 2015. Actual maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Amortized Cost	Fair Value
	(Dollars in thousands)	
Due within one year	$33,077	$33,095
Due after one year through five years	12,058	12,072
Due after five years through ten years	24,618	24,516
Due after ten years	26,943	26,629
Total	$96,696	$96,312

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4. **Loans, Allowance for Loan Losses and Credit Quality**

Loans are carried at the principal amounts outstanding, or amortized acquired fair value in the case of acquired loans, adjusted by partial charge-offs and net of deferred loan costs or fees. Loan fees and certain direct origination costs are deferred and amortized into interest income over the expected term of the loan using the level-yield method. When a loan is paid off, the unamortized portion is recognized in interest income. Interest income is accrued based upon the daily principal amount outstanding except for loans on nonaccrual status.

Loans purchased by the Company are accounted for under ASC 310-30, *Receivables — Loans and Debt Securities Acquired with Deteriorated Credit Quality* (“ASC 310-30”). At acquisition, the effective interest rate is determined based on the discount rate that equates the present value of the Company’s estimate of cash flows with the purchase price of the loan. Prepayments are not assumed in determining a purchased loan’s effective interest rate and income accretion. The application of ASC 310-30 limits the yield that may be accreted on the purchased loan, or the “accretable yield,” to the excess of the Company’s estimate, at acquisition, of the expected undiscounted principal, interest, and other cash flows over the Company’s initial investment in the loan. The excess of contractually required payments receivable over the cash flows expected to be collected on the loan represents the purchased loan’s “nonaccretable difference.” Subsequent improvements in expected cash flows of loans with nonaccretable differences result in a prospective increase to the loan’s effective yield through a reclassification of some, or all, of the nonaccretable difference to accretable yield. The effect of subsequent credit-related declines in expected cash flows of purchased loans are recorded through a specific allocation in the allowance for loan losses.

Loans are generally placed on nonaccrual status when they are past due 90 days as to either principal or interest, or when in management’s judgment the collectability of interest or principal of the loan has been significantly impaired. Loans accounted for under ASC 310-30 are placed on nonaccrual when it is not possible to reach a reasonable expectation of the timing and amount of cash flows to be collected on the loan. When a loan has been placed on nonaccrual status, previously accrued and uncollected interest is reversed against interest on loans. Interest on nonaccrual loans is accounted for on a cash-basis or using the cost-recovery method when collectability is doubtful. A loan is returned to accrual status when collectability of principal is reasonably assured and the loan has performed for a reasonable period of time.

In cases where a borrower experiences financial difficulties and the Company makes certain concessionary modifications to contractual terms, the loan is classified as a troubled debt restructuring (“TDR”), and therefore by definition is an impaired loan. Concessionary modifications may include adjustments to interest rates, extensions of maturity, and other actions intended to minimize economic loss and avoid foreclosure or repossession of collateral. For loans accounted for under ASC 310-30, the Company evaluates whether it has granted a concession by comparing the restructured debt terms to the expected cash flows at acquisition plus any additional cash flows expected to be collected arising from changes in estimate after acquisition. As a result, if an ASC 310-30 loan is modified to be consistent with, or better than, the Company’s expectations at acquisition, the loan would not qualify as a TDR. Nonaccrual loans that are restructured generally remain on nonaccrual status for a minimum period of six months to demonstrate that the borrower can meet the restructured terms. If the restructured loan is on accrual status prior to being modified, it is reviewed to determine if the modified loan should remain on accrual status. If the borrower's ability to meet the revised payment schedule is not reasonably assured, the loan is classified as a nonaccrual loan. With limited exceptions, loans classified as TDRs remain classified as such until the loan is paid off.

The composition of the Company's loan portfolio is as follows on the dates indicated.

	September 30, 2015			June 30, 2015		
	Originated	Purchased	Total	Originated	Purchased	Total
	(Dollars in thousands)					
Residential real estate	$102,570	$3,214	$105,784	$106,275	$2,068	$108,343
Home equity	22,480	-	22,480	24,326	-	24,326
Commercial real estate	152,873	210,727	363,600	148,425	200,251	348,676
Commercial business	126,476	258	126,734	122,860	273	123,133
Consumer	7,244	-	7,244	7,659	-	7,659
Total loans	$411,643	$214,199	$625,842	$409,545	$202,592	$612,137

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Past Due and Nonaccrual Loans

The following is a summary of past due and non-accrual loans:

	September 30, 2015							
	30-59 Days	60-89 Days	Past Due 90 Days or More-Still Accruing	Past Due 90 Days or More-Nonaccrual	Total Past Due	Total Current	Total Loans	Non-Accrual Loans
	(Dollars in thousands)							
Originated portfolio:								
Residential real estate	$176	$950	$ -	$ 1,658	$2,784	$99,786	$102,570	$3,165
Home equity	-	-	-	20	20	22,460	22,480	20
Commercial real estate	219	173	-	402	794	152,079	152,873	529
Commercial business	22	-	-	2	24	126,452	126,476	2
Consumer	198	41	-	50	289	6,955	7,244	153
Total originated portfolio	615	1,164	-	2,132	3,911	407,732	411,643	3,869
Purchased portfolio:								
Residential real estate	-	-	-	-	-	3,214	3,214	-
Commercial business	-	-	-	-	-	258	258	-
Commercial real estate	1,009	1,110	-	2,407	4,526	206,201	210,727	6,939
Total purchased portfolio	1,009	1,110	-	2,407	4,526	209,673	214,199	6,939
Total loans	$1,624	$2,274	$ -	$ 4,539	$8,437	$617,405	$625,842	$10,808

	June 30, 2015							
	30-59 Days	60-89 Days	Past Due 90 Days or More-Still Accruing	Past Due 90 Days or More-Nonaccrual	Total Past Due	Total Current	Total Loans	Non-Accrual Loans
	(Dollars in thousands)							
Originated portfolio:								
Residential real estate	$239	$973	$ -	$ 1,393	$2,605	$103,670	$106,275	$3,021
Home equity	9	-	-	11	20	24,306	24,326	11
Commercial real estate	300	-	-	704	1,004	147,421	148,425	994
Commercial business	-	-	-	2	2	122,858	122,860	2
Consumer	105	29	-	56	190	7,469	7,659	190
Total originated portfolio	653	1,002	-	2,166	3,821	405,724	409,545	4,218
Purchased portfolio:								
Residential real estate	-	-	-	-	-	2,068	2,068	-

Commercial business	-	-	-	-	-	273	273	-
Commercial real estate	86	299	-	2,410	2,795	197,456	200,251	6,532
Total purchased portfolio	86	299	-	2,410	2,795	199,797	202,592	6,532
Total loans	$739	$1,301	$ -	$ 4,576	$6,616	$605,521	$612,137	$10,750

Allowance for Loan Losses and Impaired Loans

The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. For residential and consumer loans, a charge-off is recorded no later than the point at which a loan is 180 days past due if the loan balance exceeds the fair value of the collateral, less costs to sell. For commercial loans, a charge-off is recorded on a case-by-case basis when all or a portion of the loan is deemed to be uncollectible. Subsequent recoveries, if any, are credited to the allowance.

The allowance for loan losses consists of general, specific, and unallocated reserves and reflects management's estimate of probable loan losses inherent in the loan portfolio at the balance sheet date. Management uses a consistent and systematic process and methodology to evaluate the appropriateness of the allowance for loan losses on a quarterly basis. The calculation of the allowance for loan losses is segregated by portfolio segments, which include: commercial real estate, commercial business, consumer, residential real estate, and purchased loans. Risk characteristics relevant to each portfolio segment are as follows:

Residential real estate: All loans in this segment are collateralized by residential real estate and repayment is primarily dependent on the credit quality, loan-to-value ratio and income of the individual borrower. The overall health of the economy, particularly unemployment rates and housing prices, has a significant effect on the credit quality in this segment. For purposes of the Company's allowance for loan loss calculation, home equity loans and lines of credit are included in residential real estate.

Commercial real estate: Loans in this segment are primarily income-producing properties. For owner-occupied properties, the cash flows are derived from an operating business, and the underlying cash flows may be adversely affected by deterioration in the financial condition of the operating business. The underlying cash flows generated by non-owner occupied properties may be adversely affected by increased vacancy rates. Management periodically obtains rent rolls, with which it monitors the cash flows of these loans. Adverse developments in either of these areas will have an adverse effect on the credit quality of this segment. For purposes of the allowance for loan losses, this segment also includes construction loans.

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Commercial business: Loans in this segment are made to businesses and are generally secured by the assets of the business. Repayment is expected from the cash flows of the business. Weakness in national or regional economic conditions, and a corresponding weakness in consumer or business spending, will have an adverse effect on the credit quality of this segment.

Consumer: Loans in this segment are generally secured, and repayment is dependent on the credit quality of the individual borrower. Repayment of consumer loans is generally based on the earnings of individual borrowers, which may be adversely impacted by regional labor market conditions.

Purchased: Loans in this segment are typically secured by commercial real estate, multi-family residential real estate, or business assets and have been acquired by the Bank's Loan Acquisition and Servicing Group ("LASG"). Loans acquired by the LASG are, with limited exceptions, performing loans at the date of purchase. Loans in this segment acquired with specific material credit deterioration since origination are identified as purchased credit-impaired. Repayment of loans in this segment is largely dependent on cash flow from the successful operation of the property, in the case of non-owner occupied property, or operating business, in the case of owner-occupied property. Loan performance may be adversely affected by factors affecting the general economy or conditions specific to the real estate market, such as geographic location or property type. Loans in this segment are evaluated for impairment under ASC 310-30. The Company reviews expected cash flows from purchased loans on a quarterly basis. The effect of a decline in expected cash flows subsequent to the acquisition of the loan is recognized through a specific allocation in the allowance for loan losses.

The general component of the allowance for loan losses is based on historical loss experience adjusted for qualitative factors stratified by loan segment. The Company does not weight periods used in that analysis to determine the average loss rate in each portfolio segment. This historical loss factor is adjusted for the following qualitative factors:

- Levels and trends in delinquencies and nonperforming loans

- Trends in the volume and nature of loans

- Trends in credit terms and policies, including underwriting standards, procedures and practices, and the experience and ability of lending management and staff

- Trends in portfolio concentration

- National and local economic trends and conditions

Effects of changes or trends in internal risk ratings

Other effects resulting from trends in the valuation of underlying collateral

The allocated component of the allowance for loan losses relates to loans that are classified as impaired. Impairment is measured on a loan-by-loan basis for commercial business and commercial real estate loans by either the present value of expected future cash flows discounted at the loan's effective interest rate or the fair value of the collateral if the loan is collateral dependent. An allowance is established when the discounted cash flows or collateral value of the impaired loan is lower than the carrying value of that loan. Large groups of smaller-balance homogeneous loans, such as consumer and residential real estate loans are collectively evaluated for impairment based on the group's historical loss experience adjusted for qualitative factors. Accordingly, the Company does not separately identify individual consumer and residential loans for individual impairment and disclosure. However, all TDRs are individually reviewed for impairment.

For all portfolio segments, except loans accounted for under ASC 310-30, a loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed. For the purchased loan segment, a loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to realize cash flows as expected at acquisition. For loans accounted for under ASC 310-30 for which cash flows can reasonably be estimated, loan impairment is measured based on the decrease in expected cash flows from those estimated at acquisition, excluding changes due to changes in interest rate indices and other non-credit related factors, discounted at the loan's effective rate assumed at acquisition. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting the scheduled principal and interest payments when due.

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The following table sets forth activity in the Company's allowance for loan losses.

	Three Months Ended September 30, 2015						
	Residential Real Estate	Commercial Real Estate	Commercial Business	Consumer	Purchased	Unallocated	Total
	(Dollars in thousands)						
Beginning balance	$741	$ 694	$ 117	$ 35	$ 283	$ 56	$1,926
Provision	(21)	62	16	31	81	-	169
Recoveries	12	5	1	2	-	-	20
Charge-offs	-	(28)	-	(22)	-	-	(50)
Ending balance	$732	$ 733	$ 134	$ 46	$ 364	$ 56	$2,065

	Three Months Ended September 30, 2014						
	Residential Real Estate	Commercial Real Estate	Commercial Business	Consumer	Purchased	Unallocated	Total
	(Dollars in thousands)						
Beginning balance	$580	$ 358	$ 48	$ 79	$ 267	$ 35	$1,367
Provision	358	(18)	1	(35)	4	10	320
Recoveries	5	-	-	10	-	-	15
Charge-offs	(160)	-	-	(3)	-	-	(163)
Ending balance	$783	$ 340	$ 49	$ 51	$ 271	$ 45	$1,539

The following table sets forth information regarding the allowance for loan losses by portfolio segment and impairment methodology.

	September 30, 2015						
	Residential Real Estate	Commercial Real Estate	Commercial Business	Consumer	Purchased	Unallocated	Total
	(Dollars in thousands)						
Allowance for loan losses:							
Individually evaluated	$415	$ 21	$ -	$ -	$ -	$ -	$436
Collectively evaluated	317	712	134	46	-	56	1,265
ASC 310-30	-	-	-	-	364	-	364
Total	$732	$ 733	$ 134	$ 46	$364	$ 56	$2,065

Loans:							
Individually evaluated	$5,071	$ 1,866	$ 2	$ 375	$ -	$ -	$7,314
Collectively evaluated	119,979	151,007	126,474	6,869	-	-	404,329
ASC 310-30	-	-	-	-	214,199	-	214,199
Total	$125,050	$ 152,873	$ 126,476	$ 7,244	$214,199	$ -	$625,842

	June 30, 2015						
	Residential Real Estate	Commercial Real Estate	Commercial Business	Consumer	Purchased	Unallocated	Total
	(Dollars in thousands)						
Allowance for loan losses:							
Individually evaluated	$435	$ 21	$ -	$ -	$ -	$ -	$456
Collectively evaluated	306	673	117	35	-	56	1,187
ASC 310-30	-	-	-	-	283	-	283
Total	$741	$ 694	$ 117	$ 35	$283	$ 56	$1,926
Loans:							
Individually evaluated	$4,095	$ 2,381	$ 2	$ 253	$ -	$ -	$6,731
Collectively evaluated	126,506	146,044	122,858	7,406	-	-	402,814
ASC 310-30	-	-	-	-	202,592	-	202,592
Total	$130,601	$ 148,425	$ 122,860	$ 7,659	$202,592	$ -	$612,137

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The following table sets forth information regarding impaired loans. Loans accounted for under ASC 310-30 that have performed based on cash flow and accretable yield expectations determined at date of acquisition are not considered impaired assets and have been excluded from the tables below.

	September 30, 2015			June 30, 2015		
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Recorded Investment	Unpaid Principal Balance	Related Allowance
	(Dollars in thousands)					
Impaired loans without a valuation allowance:						
Originated:						
Residential real estate	$3,063	$3,244	$ -	$1,975	$2,076	$ -
Consumer	328	361	-	253	262	-
Commercial real estate	895	894	-	1,505	1,510	-
Commercial business	2	2	-	2	2	-
Purchased:						
Commercial real estate	8,012	10,163	-	7,673	9,606	-
Total	12,300	14,664	-	11,408	13,456	-
Impaired loans with a valuation allowance:						
Originated:						
Residential real estate	2,008	1,948	415	2,120	2,060	435
Consumer	47	53	-	-	-	-
Commercial real estate	971	965	21	876	870	21
Commercial business	-	-	-	-	-	-
Purchased:						
Commercial real estate	2,745	3,635	309	1,208	1,644	260
Total	5,771	6,601	745	4,204	4,574	716
Total impaired loans	$18,071	$21,265	$ 745	$15,612	$18,030	$ 716

The following tables set forth information regarding interest income recognized on impaired loans.

	Three Months Ended September 30,			
	2015		2014	
	Average Recorded Investment	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized
	(Dollars in thousands)			
Impaired loans without a valuation allowance:				
Originated:				
Residential real estate	$2,520	$ 39	$1,201	$ 17
Consumer	290	5	196	3

Commercial real estate	1,200	7	1,088	7
Commercial business	2	-	-	1
Purchased:				
Commercial real estate	7,842	14	3,938	75
Total	11,854	65	6,423	103
Impaired loans with a valuation allowance:				
Originated:				
Residential real estate	2,064	23	1,707	28
Consumer	23	1	35	1
Commercial real estate	924	12	1,334	20
Commercial business	-	-	-	-
Purchased:				
Commercial real estate	1,976	36	1,573	3
Total	4,987	72	4,649	52
Total impaired loans	$16,841	$ 137	$11,072	$ 155

Credit Quality

The Company utilizes a ten-point internal loan rating system for commercial real estate, construction, commercial business, and certain residential loans as follows:

Loans rated 1 — 6: Loans in these categories are considered “pass” rated loans. Loans in categories 1-5 are considered to have low to average risk. Loans rated 6 are considered marginally acceptable business credits and have more than average risk.

Loans rated 7: Loans in this category are considered “special mention.” These loans show signs of potential weakness and are being closely monitored by management.

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Loans rated 8: Loans in this category are considered “substandard.” Loans classified as substandard are inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. Assets so classified have a well-defined weakness or weaknesses that jeopardize the orderly repayment of the debt.

Loans rated 9: Loans in this category are considered “doubtful.” Loans classified as doubtful have all the weaknesses inherent in one graded 8 with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable and improbable.

Loans rated 10: Loans in this category are considered “loss” and of such little value that their continuance as loans is not warranted.

On an annual basis, or more often if needed, the Company formally reviews the ratings of all loans subject to risk ratings. Semi-annually, the Company engages an independent third-party to review a significant portion of loans within these segments. Management uses the results of these reviews as part of its annual review process. Risk ratings on purchased loans, with and without evidence of credit deterioration at acquisition, are determined relative to the Company’s recorded investment in that loan, which may be significantly lower than the loan’s unpaid principal balance.

The following tables present the Company’s loans by risk rating.

	September 30, 2015				
	Originated Portfolio				
	Commercial Real Estate	Commercial Business	Residential[1]	Purchased Portfolio	Total
	(Dollars in thousands)				
Loans rated 1- 6	$148,790	$ 126,452	$ 7,583	$200,745	$483,570
Loans rated 7	3,045	24	627	5,189	8,885
Loans rated 8	1,038	-	610	8,265	9,913
Loans rated 9	-	-	23	-	23
Loans rated 10	-	-	-	-	-
	$152,873	$ 126,476	$ 8,843	$214,199	$502,391

June 30, 2015
Originated Portfolio
Commercial Commercial Purchased

	Real Estate	Business	Residential[1]	Portfolio	Total
	(Dollars in thousands)				
Loans rated 1- 6	$ 142,321	$ 122,829	$ 8,049	$ 190,193	$ 463,392
Loans rated 7	4,417	31	634	5,628	10,710
Loans rated 8	1,687	-	429	6,771	8,887
Loans rated 9	-	-	23	-	23
Loans rated 10	-	-	-	-	-
	$ 148,425	$ 122,860	$ 9,135	$ 202,592	$ 483,012

(1)Certain of the Company's loans made for commercial purposes, but secured by residential collateral, are rated under the Company's risk-rating system.

The payment status and loan-to-value ratio are the primary credit quality indicators used for residential mortgage loans and home equity loans. Consumer loans that become 90 days or more past due, or are placed on nonaccrual regardless of past due status, are reviewed on an individual basis for impairment by assessing the net realizable value of underlying collateral and the economic condition of the borrower.

Troubled Debt Restructurings

The following table shows the Company's post-modification balance of TDRs by type of modification.

	Three Months Ended September 30,			
	2015		2014	
	Number of Contracts	Recorded Investment	Number of Contracts	Recorded Investment
	(Dollars in thousands)			
Extended maturity	-	$ -	2	$ 234
Adjusted interest rate	-	-	-	-
Rate and maturity	-	-	4	246
Principal deferment	-	-	1	461
Court ordered concession	-	-	4	85
	-	$ -	11	$ 1,026

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The following table shows loans modified in a TDR and the change in the recorded investment subsequent to the modifications occurring.

	Three Months Ended September 30,					
	2015			2014		
	Number of Contracts	Recorded Investment Pre-Modification	Recorded Investment Post-Modification	Number of Contracts	Recorded Investment Pre-Modification	Recorded Investment Post-Modification
	(Dollars in thousands)					
Originated portfolio:						
Residential real estate	-	$ -	$ -	9	$ 823	$ 823
Home equity	-	-	-	-	-	-
Commercial real estate	-	-	-	1	200	200
Commercial business	-	-	-	-	-	-
Consumer	-	-	-	1	3	3
Total originated portfolio	-	-	-	11	1,026	1,026
Purchased portfolio:						
Residential real estate	-	-	-	-	-	-
Commercial real estate	-	-	-	-	-	-
Total purchased portfolio	-	-	-	-	-	-
Total	-	$ -	$ -	11	$ 1,026	$ 1,026

The Company considers TDRs past due 90 days or more to be in payment default. One loan modified in a TDR in the last twelve months defaulted during the three months ended September 30, 2015; the recorded investment of such loans was $50 thousand. As of September 30, 2015, there were no further commitments to lend associated with loans modified in a TDR.

ASC 310-30 Loans

The following table presents a summary of loans accounted for under ASC 310-30 that were acquired by the Company during the period indicated.

	Three Months Ended September	Three Months Ended September

	30, 2015 (Dollars in thousands)	30, 2014
Contractually required payments receivable	$31,276	$ 21,108
Nonaccretable difference	(291)	(304)
Cash flows expected to be collected	30,985	20,804
Accretable yield	(7,527)	(7,960)
Fair value of loans acquired	$23,458	$ 12,844

Certain of the loans accounted for under ASC 310-30 that were acquired by the Company are not accounted for using the income recognition model because the Company cannot reasonably estimate cash flows expected to be collected. These loans when acquired are placed on non-accrual. The carrying amounts of such loans are as follows.

	As of and for the Three Months Ended September 30, 2015 (Dollars in thousands)
Loans acquired during the period	$ -
Loans at end of period	6,826

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The following table summarizes the activity in the accretable yield for loans accounted for under ASC 310-30.

	Three Months Ended September 30, 2015	Three Months Ended September 30, 2014
	(Dollars in thousands)	
Beginning balance	$111,449	$109,040
Acquisitions	7,527	7,960
Accretion	(3,755)	(4,443)
Reclassifications from non-accretable difference to accretable yield	277	10
Disposals and other changes	(5,883)	(4,215)
Ending balance	$109,615	$108,352

The following table provides information related to the unpaid principal balance and carrying amounts of ASC 310-30 loans.

	September 30, 2015	June 30, 2015
	(Dollars in thousands)	
Unpaid principal balance	$244,468	$235,716
Carrying amount	210,285	199,113

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5. **Transfers and Servicing of Financial Assets**

The Company sells loans in the secondary market and for certain loans, retains the servicing responsibility. Consideration for the sale includes the cash received as well as the related servicing rights asset. The Company receives fees for the services provided.

Capitalized servicing rights as of September 30, 2015 totaled $1.3 million, compared to $1.1 million as of June 30, 2015.

Mortgage loans sold in the quarter ended September 30, 2015 totaled $28.9 million, compared to $30.8 million in the quarter ended September 30, 2015. Mortgage loans serviced for others totaled $104.3 million at September 30, 2015 and $108.4 million at June 30, 2015. SBA loans sold during the quarter ended September 30, 2015 totaled $5.5 million, compared to $687 thousand in the quarter ended September 30, 2014. SBA loans serviced for others totaled $56.9 million at September 30, 2015 and $53.5 million at June 30, 2015.

Mortgage and SBA loans serviced for others are accounted for as sales and therefore are not included in the accompanying consolidated balance sheets. The risks inherent in mortgage servicing assets and SBA servicing assets relate primarily to changes in prepayments that result from shifts in interest rates.

Contractually specified servicing fees were $149 thousand and $125 thousand for the quarters ended September 30, 2015 and 2014, respectively, and were included as a component of loan related fees within non-interest income.

The significant assumptions used in the valuation for mortgage servicing rights as of September 30, 2015 included a weighted average discount rate of 7.0% and a weighted average prepayment speed assumption of 12.7%. For the SBA servicing rights, the significant assumptions used in the valuation included a pre-payment speed assumption of 7.1% and discount rates ranging from 4.4% to 6.0%.

6. **Investments in Qualified Affordable Housing Projects**

On July 1, 2015, the Company adopted ASU 2014-01, *Accounting for Investments in Qualified Affordable Housing Projects*, which required retrospective application. Under the proportional amortization method in ASU 2014-01, the initial costs of investment in qualified affordable housing projects are amortized in proportion to tax credits and other tax benefits received, and are recognized as a component of the provision for income taxes in the consolidated statements of income. Prior to the implementation of ASU 2014-01, the Company's investments in qualified affordable housing projects were amortized and included as a component of non-interest income in the consolidated statements of income. Further information regarding the Company's investments in affordable housing projects follows:

	September 30, 2015	June 30, 2015
	(Dollars in thousands)	
Investments in affordable housing projects included in other assets	$474	$508

Included in the effective tax rate for the quarter ended September 30, 2015 and 2014 is the effect of the following:

	Three Months Ended September 30, 2015	Three Months Ended September 30, 2014
	(Dollars in thousands)	
Investment amortization included in income tax expense	$92	$ 92
Tax credit recognized as income tax benefit	118	118

ASU 2014-01 was applied retrospectively to all periods presented. The cumulative effect on retained earnings and other assets was $112 thousand at July 1, 2015.

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7. Earnings Per Share (EPS)

EPS is computed by dividing net income allocated to common shareholders by the weighted average common shares outstanding (including participating securities). The Company's only participating securities are unvested restricted stock awards that contain non-forfeitable rights to dividends. The following table shows the weighted average number of shares outstanding for the periods indicated. Shares issuable relative to stock options granted have been reflected as an increase in the shares outstanding used to calculate diluted EPS, after applying the treasury stock method. The number of shares outstanding for basic and diluted EPS is presented as follows:

	Three months Ended September 30,	
	2015	2014
	(Dollars in thousands, except share and per share data)	
Net income	1,867	1,647
Preferred stock dividends or accretion	-	-
Net income available to common shareholders	$1,867	$1,647
Weighted average shares used in calculation of basic EPS	9,562,812	10,180,038
Incremental shares from assumed exercise of dilutive securities	-	-
Weighted average shares used in calculation of diluted EPS	9,562,812	10,180,038
Earnings per common share:		
Basic	$0.20	$0.16
Diluted	0.20	0.16

For the three months ended September 30, 2015, the following stock options were excluded from the calculation of diluted EPS due to the exercise price of these options exceeding the average market price of the Company's common stock for the period. These options, which were not dilutive at that date, may potentially dilute EPS in the future.

	Three Months Ended September 30,	
	2015	2014
Stock options	980,269	1,082,121

8. **Derivatives and Hedging Activities**

The Company has stand-alone derivative financial instruments in the form of interest rate caps that derive their value from a fee paid and are adjusted to fair value based on index and strike rate, and swap agreements that derive their value from the underlying interest rate. These transactions involve both credit and market risk. The notional amounts are amounts on which calculations, payments and the value of the derivative are based. Notional amounts do not represent direct credit exposures. Direct credit exposure arises in the event of nonperformance by the counterparties to these agreements, and is limited to the net difference between the calculated amounts to be received and paid, if any. Such differences, which represent the fair value of the derivative instruments, are reflected on the Company's balance sheet as derivative assets and derivative liabilities. The Company seeks to manage the credit risk of its financial contracts through credit approvals, limits and monitoring procedures, and does not expect any counterparties to fail to meet their obligations.

The Company currently holds derivative instruments that contain credit-risk related features that are in a net liability position, which may require that collateral be assigned to dealer banks. At September 30, 2015, the Company had posted cash collateral totaling $1.8 million with dealer banks related to derivative instruments in a net liability position.

The Company does not offset fair value amounts recognized for derivative instruments. The Company does not net the amount recognized for the right to reclaim cash collateral against the obligation to return cash collateral arising from derivative instruments executed with the same counterparty under a master netting arrangement.

Risk Management Policies – Derivative Instruments

The Company evaluates the effectiveness of entering into any derivative instrument agreement by measuring the cost of such an agreement in relation to the reduction in net income volatility within an assumed range of interest rates.

Interest Rate Risk Management – Cash Flow Hedging Instruments

The Company uses variable rate debt as a source of funds for use in the Company's lending and investment activities and other general business purposes. These debt obligations expose the Company to variability in interest payments due to changes in interest rates. If interest rates increase, interest expense increases. Conversely, if interest rates decrease, interest expense decreases. Management believes it is prudent to limit the variability of a portion of its interest payments and, therefore, generally hedges a portion of its variable-rate interest payments.

Information pertaining to outstanding interest rate caps and swap agreements used to hedge variable rate debt is as follows.

September 30, 2015

Notional Amount	Inception Date	Termination Date	Index	Receive Rate	Pay Rate	Strike Rate	Unrealized Loss	Fair Value	Balance Sheet Location
(Dollars in thousands)									
Interest rate swaps:									
$ 5,000	July 2013	July 2033	3 Mo. LIBOR	0.33 %	3.38 %	n/a	(801)	(801)	Other Liabilities
5,000	July 2013	July 2028	3 Mo. LIBOR	0.33 %	3.23 %	n/a	(624)	(624)	Other Liabilities
5,000	July 2013	July 2023	3 Mo. LIBOR	0.33 %	2.77 %	n/a	(377)	(377)	Other Liabilities
Interest rate caps:									
6,000	October 2014	September 2019	3 Mo. LIBOR	n/a	n/a	2.50 %	(141)	35	Other Assets
10,000	March 2015	February 2020	3 Mo. LIBOR	n/a	n/a	2.50 %	(136)	80	Other Assets
$ 31,000							$ (2,079)	$ (1,687)	

June 30, 2015

Notional Amount	Inception Date	Termination Date	Index	Receive Rate	Pay Rate	Strike Rate	Unrealized Loss	Fair Value	Balance Sheet Location
(Dollars in thousands)									
Interest rate swaps:									
$ 5,000	July 2013	July 2033	3 Mo. LIBOR	0.28 %	3.38 %	n/a	$ (472)	$ (472)	Other Liabilities
5,000	July 2013	July 2028	3 Mo. LIBOR	0.28 %	3.23 %	n/a	$ (368)	$ (368)	Other Liabilities
5,000	July 2013	July 2023	3 Mo. LIBOR	0.28 %	2.77 %	n/a	$ (208)	$ (208)	Other Liabilities
Interest rate caps:									
6,000	October 2014	September 2019	3 Mo. LIBOR	n/a	n/a	2.50 %	(114)	63	Other Assets
10,000	March 2015	February 2020	3 Mo. LIBOR	n/a	n/a	2.50 %	(80)	136	Other Assets
$ 31,000							$ (1,242)	$ (849)	

During the three months ended September 30, 2015 and 2014, no interest rate cap or swap agreements were terminated prior to maturity. Changes in the fair value of interest rate caps and swaps designated as hedging instruments of the variability of cash flows associated with variable rate debt are reported in other comprehensive income. These amounts subsequently are reclassified into interest expense as a yield adjustment in the same period in which the related interest on the debt affects earnings. Risk management results for the three months ended September 30, 2015 and 2014 related to the balance sheet hedging of variable rate debt indicates that the hedges were effective.

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9. Other Comprehensive Income

The components of other comprehensive loss follow.

	Three Months Ended September 30,					
	2015			2014		
	Pre-tax Amount	Tax Expense (Benefit)	After-tax Amount	Pre-tax Amount	Tax Expense (Benefit)	After-tax Amount
	(Dollars in thousands)					
Change in net unrealized gain or loss on available-for-sale securities	$466	$ 178	$ 288	$(275)	$ (93)	$ (182)
Reclassification adjustment for net gains included in net income	-	-	-	-	-	-
Total available-for-sale securities	466	178	288	(275)	(93)	(182)
Change in accumulated loss on effective cash flow hedges	(838)	(319)	(519)	(272)	(92)	(180)
Reclassification adjustment for net gains included in net income	-	-	-	(9)	(3)	(6)
Total derivatives and hedging activities	(838)	(319)	(519)	(281)	(95)	(186)
Total other comprehensive loss	$(372)	$ (141)	$ (231)	$(556)	$ (188)	$ (368)

Accumulated other comprehensive loss is comprised of the following.

	September 30, 2015	June 30, 2015
	(Dollars in thousands)	
Unrealized loss on available-for-sale securities	$(370)	$(836)
Tax effect	140	318
Net-of-tax amount	(230)	(518)
Unrealized loss on cash flow hedges	(2,080)	(1,242)
Tax effect	791	472
Net-of-tax amount	(1,289)	(770)
Accumulated other comprehensive loss	$(1,519)	$(1,288)

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10. Commitments and Contingencies

Commitments

The Company is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers and to reduce its own exposure to fluctuations in interest rates. These financial instruments include commitments to extend credit, standby letters of credit, and commitments to fund investments. Those instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the consolidated balance sheets. The contract amounts of those instruments reflect the extent of involvement the Company has in particular classes of financial instruments.

The Company's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and standby letters of credit is represented by the contractual amount of those instruments. The Company uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments.

Financial instruments with contract amounts which represent credit risk are as follows:

	September 30, 2015	June 30, 2015
	(Dollars in thousands)	
Commitments to grant loans	$24,954	$24,966
Unfunded commitments under lines of credit	39,509	39,414
Standby letters of credit	60	60
Commitment to fund investment	2,500	-

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Company evaluates each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Company upon extension of credit, is based on management's credit evaluation of the counter party. Collateral held varies but may include accounts receivable, inventory, property, plant and equipment, and income-producing commercial properties. The Company has recorded an allowance for possible losses on commitments and unfunded loans totaling

$37 thousand recorded in other liabilities at both September 30, 2015 and June 30, 2015.

The Company committed $2.5 million to a fund that acquires CRA qualified investments in loans for the Company's portfolio. The fund manager will call the funds from the Company when an investment is successfully acquired. Through the quarter ended September 30, 2015, the fund has not called any funds from the Company.

Contingencies

The Company and its subsidiary are parties to litigation and claims arising in the normal course of business. Management believes that the liabilities, if any, arising from such litigation and claims will not be material to the Company's consolidated financial position or results of operations.

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11. Fair Value Measurements

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction (that is, not a forced liquidation or distressed sale) between market participants at the measurement date under current market conditions. The Company uses prices and inputs that are current as of the measurement date, including during periods of market dislocation. In periods of market dislocation, the observability of prices and inputs may be reduced for many instruments. This condition could cause an instrument to be reclassified from one level to another. When market assumptions are not readily available, the Company's own assumptions are set to reflect those that market participants would use in pricing the asset or liability at the measurement date. If there has been a significant decrease in the volume and level of activity for the asset or liability, regardless of the valuation technique(s) used, the objective of a fair value measurement remains the same.

ASC 820 defines fair value and establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy under ASC 820 are described below:

Level 1 — Inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date.

Level 2 — Valuations based on significant observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

Level 3 — Prices or valuations that require inputs that are both significant to the fair value measurement and unobservable.

To the extent that valuation is based on models or inputs that are less observable or unobservable in the market, the determination of fair value requires more judgment. Accordingly, the degree of judgment exercised by the Company in determining fair value is greatest for instruments categorized in Level 3. A financial instrument's level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement.

*Valuation technique*s - There have been no changes in the valuation techniques used during the current period.

Transfers- There were no transfers of assets and liabilities measured at fair value on a recurring or nonrecurring basis during the current period.

Assets and Liabilities Measured at Fair Value on a Recurring Basis:

Available-for-sale securities - Where quoted prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. Examples of such instruments include publicly-traded common and preferred stocks. If quoted prices are not available, then fair values are estimated by using pricing models (*i.e.*, matrix pricing) and market interest rates and credit assumptions or quoted prices of securities with similar characteristics and are classified within Level 2 of the valuation hierarchy. Examples of such instruments include government agency and government sponsored agency mortgage-backed securities, as well as certain preferred and trust preferred stocks. Level 3 securities are securities for which significant unobservable inputs are utilized.

Certain investments are measured at fair value using the net asset value per share as a practical expedient. The fund seeks to invest in securities either issued or guaranteed by the U.S. government or its agencies. The Company's investments can be redeemed daily at the closing net asset value per share. In accordance with ASU 2015-07, these investments have not been included in the fair value hierarchy.

Derivative financial instruments - The valuation of the Company's interest rate swaps and caps are determined using widely accepted valuation techniques including discounted cash flow analyses on the expected cash flows of derivatives. These analyses reflect the contractual terms of the derivatives, including the period to maturity, and use observable market-based inputs, including forward interest rate curves and implied volatilities. Unobservable inputs, such as credit valuation adjustments are insignificant to the overall valuation of the Company's derivative financial instruments. Accordingly, the Company has determined that its interest rate derivatives fall within Level 2 of the fair value hierarchy.

The fair value of derivative loan commitments and forward loan sale agreements are estimated using the anticipated market price based on pricing indications provided from syndicate banks. These commitments and agreements are categorized as Level 2. The fair value of such instruments was nominal at each date presented.

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Assets and Liabilities Measured at Fair Value on a Nonrecurring Basis:

Collateral Dependent Impaired Loans- Valuations of impaired loans measured at fair value are determined by a review of collateral values. Certain inputs used in appraisals are not always observable, and therefore impaired loans are generally categorized as Level 3 within the fair value hierarchy.

Real Estate Owned and Other Repossessed collateral - The fair values of real estate owned and other repossessed collateral are estimated based upon appraised values less estimated costs to sell. Certain inputs used in appraisals are not always observable, and therefore may be categorized as Level 3 within the fair value hierarchy. When inputs used in appraisals are primarily observable, they are classified as Level 2.

Loan servicing rights— The fair value of the SBA and mortgage servicing rights is based on a valuation model that calculates the present value of estimated future net servicing income. Adjustments are only recorded when the discounted cash flows derived from the valuation model are less than the carrying value of the asset. Certain inputs are not observable, and therefore loan servicing rights are generally categorized as Level 3 within the fair value hierarchy.

Fair Value of other Financial Instruments:

Cash and cash equivalents - The fair value of cash, due from banks, interest bearing deposits and FHLB overnight deposits approximates their relative book values, as these financial instruments have short maturities.

FHLB stock - The carrying value of FHLB stock approximates fair value based on redemption provisions of the FHLB.

Loans- Fair values are estimated for portfolios of loans with similar financial characteristics. The fair value of performing loans is calculated by discounting scheduled cash flows through the estimated maturity using estimated market discount rates that reflect the credit and interest rate risk inherent in the loan. The estimates of maturity are based on the Company’s historical experience with repayments for each loan classification, modified, as required, by an estimate of the effect of current economic conditions, lending conditions and the effects of estimated prepayments.

Loans held for sale - The fair value of loans held-for-sale is estimated based on bid quotations received from loan dealers.

Interest receivable - The fair value of this financial instrument approximates the book value as this financial instrument has a short maturity. It is the Company's policy to stop accruing interest on loans past due by more than 90 days. Therefore, this financial instrument has been adjusted for estimated credit loss.

Deposits - The fair value of deposits with no stated maturity, such as noninterest-bearing demand deposits, savings, NOW accounts and money market accounts, is equal to the amount payable on demand. The fair values of time deposits are based on the discounted value of contractual cash flows. The discount rate is estimated using the rates currently offered for deposits of similar remaining maturities. The fair value estimates do not include the benefit that results from the low-cost funding provided by the deposit liabilities compared to the cost of borrowing funds in the market. If that value were considered, the fair value of the Company's net assets could increase.

Borrowings - The fair value of the Company's borrowings with the FHLB is estimated by discounting the cash flows through maturity or the next re-pricing date based on current rates available to the Company for borrowings with similar maturities. The fair value of the Company's short-term borrowings, capital lease obligations, wholesale repurchase agreements and other borrowings is estimated by discounting the cash flows through maturity based on current rates available to the Company for borrowings with similar maturities.

Off-Balance Sheet Credit-Related Instruments -Fair values for off-balance-sheet, credit-related financial instruments are based on fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the counterparties' credit standing. The fair value of such instruments was nominal at each date presented.

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Assets and liabilities measured at fair value on a recurring basis are summarized below.

	September 30, 2015			
	Total	Level 1	Level 2	Level 3
	(Dollars in thousands)			
Assets				
Securities available-for-sale:				
U.S. Government agency securities	$45,167	$ -	$45,167	$ -
Agency mortgage-backed securities	51,145	-	51,145	-
Other investments measured at net asset value[1]	5,032	-	-	-
Other assets – interest rate caps	115	-	115	-
Liabilities				
Other liabilities – interest rate swaps	$1,802	$ -	$1,802	$ -

	June 30, 2015			
	Total	Level 1	Level 2	Level 3
	(Dollars in thousands)			
Assets				
Securities available-for-sale:				
U.S. Government agency securities	$48,230	$ -	$48,230	$ -
Agency mortgage-backed securities	53,678	-	53,678	-
Other investments measured at net asset value[1]	-	-	-	-
Other assets – interest rate caps	199	-	199	-
Liabilities				
Other liabilities – interest rate swap	$1,048	$ -	$1,048	$ -

(1) In accordance with ASU 820-10, certain investments that are measured at fair value using the net asset value per share (or its equivalent) as a practical expedient have not been classified in the fair value hierarchy. The fair value amounts presented in the table are intended to permit reconciliation of the fair value amount to the consolidated financial statements.

Assets measured at fair value on a nonrecurring basis are summarized below.

	September 30, 2015			
	Total	Level 1	Level 2	Level 3
	(Dollars in thousands)			
Collateral dependent impaired loans	$987	$ -	$ -	$987

Real estate owned and other repossessed collateral	1,279	-	-	1,279
Loan servicing rights	1,310	-	-	1,310

	June 30, 2015			
	Total	Level 1	Level 2	Level 3
	(Dollars in thousands)			
Collateral dependent impaired loans	$932	$ -	$ -	$932
Real estate owned and other repossessed collateral	1,651	-	-	1,651
Loan servicing rights	1,123	-	-	1,123

The table below presents quantitative information about significant unobservable inputs (Level 3) for assets measured at fair value on a nonrecurring basis at the dates indicated.

	Fair Value		Valuation Technique
	September 30, 2015	June 30, 2015	
	(Dollars in thousands)		
Collateral dependent impaired loans	$987	$932	Appraisal of collateral(1)
Real estate owned and other repossessed collateral	1,279	1,651	Appraisal of collateral(1)
Loan servicing rights	1,385	1,123	Discounted cash flow(2)

(1) Fair value is generally determined through independent appraisals of the underlying collateral. The Company may also use another available source of collateral assessment to determine a reasonable estimate of the fair value of the collateral. Appraisals may be adjusted by management for qualitative factors such as economic factors and estimated liquidation expenses. The range of these possible adjustments was 5% to 60%.

(2) Fair value is determined using a discounted cash flow model. The unobservable inputs include anticipated rate of loan prepayments and discount rates. The range of prepayment assumptions used was 7.06% to 12.71%. For discount rates, the range was 4.36% to 7.00%.

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The following table presents the estimated fair value of the Company's financial instruments.

	Carrying	Fair Value Measurements at September 30, 2015			
	Amount	Total	Level 1	Level 2	Level 3
	(Dollars in thousands)				
Financial assets:					
Cash and cash equivalents	$86,213	$86,213	$86,213	$-	$-
Available-for-sale securities	96,312	96,312	-	96,312	-
Other investments measured at net asset value[1]	5,032	5,032	-	-	-
Federal Home Loan Bank stock	4,102	4,102	-	4,102	-
Loans held for sale	7,536	7,536	-	7,536	-
Loans, net	623,777	625,655	-	-	625,655
Accrued interest receivable	1,361	1,361	-	1,361	-
Interest rate caps	115	115	-	115	-
Financial liabilities:					
Deposits	693,478	693,873	-	693,873	-
FHLB advances	30,159	30,768	-	30,768	-
Short-term borrowings	2,479	2,479	-	2,479	-
Capital lease obligation	1,312	1,415	-	1,415	-
Subordinated debentures	8,674	8,992	-	-	8,992
Interest rate swaps	1,802	1,802	-	1,802	-

	Carrying	Fair Value Measurements at June 30, 2015			
	Amount	Total	Level 1	Level 2	Level 3
	(Dollars in thousands)				
Financial assets:					
Cash and cash equivalents	$89,850	$89,850	$89,850	$-	$-
Available-for-sale securities	101,908	101,908	-	101,908	-
Other investments measured at net asset value[1]	-	-	-	-	-
Federal Home Loan Bank stock	4,102	4,102	-	4,102	-
Loans held for sale	9,035	9,035	-	9,035	-
Loans, net	610,211	613,896	-	-	613,896
Accrued interest receivable	1,335	1,335	-	1,335	-
Interest rate caps	199	199	-	199	-
Financial liabilities:					
Deposits	674,759	675,285	-	675,285	-
FHLB advances	30,188	30,867	-	30,867	-
Wholesale repurchase agreements	10,037	10,098	-	10,098	-
Short-term borrowings	2,349	2,349	-	2,349	-
Capital lease obligation	1,368	1,448	-	1,448	-
Subordinated debentures	8,626	8,471	-	-	8,471

Interest rate swaps	1,048	1,048	-	1,048	-

(1) In accordance with ASU 820-10, certain investments that are measured at fair value using the net asset value per share (or its equivalent) as a practical expedient have not been classified in the fair value hierarchy. The fair value amounts presented in the table are intended to permit reconciliation of the fair value amount to the consolidated financial statements.

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion should be read in conjunction with the consolidated financial statements, notes and tables included in Northeast Bancorp's Annual Report on Form 10-K for the fiscal year ended June 30, 2015, filed with the Securities and Exchange Commission.

A Note about Forward Looking Statements

This report contains certain "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended and Section 21E of the Securities Exchange Act of 1934, as amended, such as statements relating to the Company's financial condition, prospective results of operations, future performance or expectations, plans, objectives, prospects, loan loss allowance adequacy, simulation of changes in interest rates, capital spending and finance sources and revenue sources. These statements relate to expectations concerning matters that are not historical facts. Accordingly, statements that are based on management's projections, estimates, assumptions, and judgments constitute forward-looking statements. These forward-looking statements, which are based on various assumptions (some of which are beyond the Company's control), may be identified by reference to a future period or periods, or by the use of forward-looking terminology such as "believe", "expect", "estimate", "anticipate", "continue", "plan", "approximate "intend", "objective", "goal", "project", or other similar terms or variations on those terms, or the future or conditional verbs such as "will", "may", "should", "could", and "would". Although the Company believes that these forward-looking statements are based on reasonable estimates and assumptions, they are not guarantees of future performance and are subject to known and unknown risks, uncertainties, contingencies, and other factors. Accordingly, the Company cannot give you any assurance that its expectations will, in fact, occur or that its estimates or assumptions will be correct. The Company cautions you that actual results could differ materially from those expressed or implied by such forward-looking statements as a result of, among other factors, changes in interest rates and real estate values; competitive pressures from other financial institutions; the effects of continuing weakness in general economic conditions on a national basis or in the local markets in which the Company operates, including changes which adversely affect borrowers' ability to service and repay the Company's loans; changes in loan defaults and charge-off rates; changes in the value of securities and other assets, adequacy of loan loss reserves, or deposit levels necessitating increased borrowing to fund loans and investments; changes in government regulation; the risk that the Company may not be successful in the implementation of its business strategy; the risk of compromises or breaches of the company's security systems; the risk that intangibles recorded in the Company's financial statements will become impaired; changes in assumptions used in making such forward-looking statements; and the other risks and uncertainties detailed in the Company's Annual Report on Form 10-K for the fiscal year ended June 30, 2015 as updated in the Company's Quarterly Reports on Form 10-Q and other filings submitted to the Securities and Exchange Commission. These forward-looking statements speak only as of the date of this report and the Company does not undertake any obligation to update or revise any of these forward-looking statements to reflect events or circumstances occurring after the date of this report or to reflect the occurrence of unanticipated events.

Description of Business and Strategy

Business Overview

Northeast Bancorp ("we," "our," "us," "Northeast" or the "Company"), incorporated under Maine law in 1987, is a bank holdin company registered with the Board of Governors of the Federal Reserve System (the "Federal Reserve"). As a bank holding company registered under the Bank Holding Company Act of 1956, as amended (the "BHCA"), the Company is subject to regulation and supervision by the Federal Reserve. The Company's primary subsidiary and principal asset is its wholly-owned banking subsidiary, Northeast Bank (the "Bank" or "Northeast Bank"), a Maine state-chartered bank originally organized in 1872. As a Federal Deposit Insurance Corporation ("FDIC") insured Maine-chartered bank, the Bank is subject to regulation and supervision by the Maine Bureau of Financial Institutions (the "Bureau") and the FDIC.

On December 29, 2010, the merger of the Company and FHB Formation LLC, a Delaware limited liability company ("FHB"), was consummated. As a result of the merger, the surviving company received a capital contribution of $16.2 million (in addition to the approximately $13.1 million in cash consideration paid to former shareholders), and the former members of FHB collectively acquired approximately 60% of the Company's outstanding common stock. The Company applied the acquisition method of accounting, as described in Accounting Standards Codification ("ASC") 805, *Business Combinations* ("ASC 805") to the merger, which represents an acquisition by FHB of Northeast, with Northeast as the surviving company.

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In connection with the transaction, as part of the regulatory approval process, the Company and the Bank made certain commitments to the Federal Reserve, the most significant of which are (i) to maintain a Tier 1 leverage ratio of at least 10%, (ii) to maintain a total risk-based capital ratio of at least 15%, (iii) to limit purchased loans to 40% of total loans, (iv) to fund 100% of the Company's loans with core deposits (defined as non-maturity deposits and non-brokered insured time deposits), and (v) to hold commercial real estate loans (including owner-occupied commercial real estate) to within 300% of total risk-based capital. On June 28, 2013, the Federal Reserve approved the amendment to exclude owner-occupied commercial real estate loans from the commitment to hold commercial real estate loans to within 300% of total risk-based capital. All other commitments made to the Federal Reserve in connection with the merger remain unchanged. The Company and the Bank are currently in compliance with all commitments to the Federal Reserve. The Company's compliance ratios at September 30, 2015 follow:

Condition	Ratios as of September 30, 2015	
(i) Tier 1 leverage capital ratio	14.23	%
(ii) Total capital ratio	20.03	%
(iii) Ratio of purchased loans to total loans, including loans held for sale	33.82	%
(iv) Ratio of loans to core deposits (1)	91.04	%
(v) Ratio of commercial real estate loans to total risk-based capital (2)	195.50	%

(1) Core deposits include all non-maturity deposits and maturity deposits less than $250 thousand

(2) For purposes of calculating this ratio, commercial real estate includes all non-owner occupied commercial real estate loans defined as such by regulatory guidance, including all land development and construction loans.

As of September 30, 2015, the Company, on a consolidated basis, had total assets of $858.2 million, total deposits of $693.5 million, and shareholders' equity of $113.7 million. The Company gathers retail deposits through its banking offices in Maine and the Bank's online affinity deposit program, ableBanking; originates loans through the Bank's Community Banking Division; originates Small Business Administration ("SBA") loans through the Bank's SBA National group ("SBA National"); and purchases and originates commercial loans through the Bank's Loan Acquisition and Servicing Group ("LASG"). The Community Banking Division, with ten full-service branches and two loan production offices, operates from the Bank's headquarters in Lewiston, Maine. LASG, ableBanking, and SBA National operate from the Company's offices in Boston, Massachusetts.

Unless the context otherwise requires, references herein to the Company include the Company and its subsidiary on a consolidated basis.

Strategy

The Company's goal is to prudently grow its franchise, while maintaining sound operations and risk management, by implementing the following strategies:

Continuing our community banking tradition. With a history that dates to 1872, our Community Banking Division maintains its focus on sales and service, with the goal of attracting and retaining deposits, and serving the lending needs of retail and commercial customers within our core markets.

Growing LASG's national originated and purchased loan business. We purchase performing commercial real estate loans nationally, at prices that on average have produced yields significantly higher than those available on our originated loan portfolio. We also originate loans nationally, taking advantage of our core expertise in underwriting and servicing national credits.

Growing our national SBA origination business. We originate loans on a national basis to small businesses, primarily through the SBA 7(a) program, which provides the partial guarantee of the SBA.

Generating deposits to fund our business. We offer a full line of deposit products through our ten-branch network located in the Community Banking Division's market. AbleBanking is a direct savings platform providing an additional channel to raise core deposits to fund our asset strategy.

Critical Accounting Policies

Critical accounting policies are those that involve significant judgments and assessments by management, and which could potentially result in materially different results under different assumptions and conditions. The reader is encouraged to review each of the policies included in Form 10-K for the year ended June 30, 2015 to gain a better understanding of how Northeast's financial performance is measured and reported. There has been no material change in critical accounting policies during the three months ended September 30, 2015.

Overview

Net income was $1.9 million, or $0.20 per diluted common share, for the quarter ended September 30, 2015, compared to $1.6 million, or $0.16 per diluted common share, for the quarter ended September 30, 2014.

Net interest and dividend income before provision for loan losses decreased by $230 thousand, or 2.4%, for the quarter ended September 30, 2015, compared to the quarter ended September 30, 2014. The decrease is primarily due to lower interest income in the purchased loan portfolio, mainly due to a decline in yield to 12.1% in the current quarter from 12.8% earned in the quarter ended September 30, 2014.

Noninterest income increased by $551 thousand for the quarter ended September 30, 2015, compared to the quarter ended September 30, 2014, principally due to an increase in gains realized on sale of portfolio loans. The recent quarter includes gains realized on sale of SBA loans of $675 thousand, compared to an $80 thousand gain on sale of commercial loans in the quarter ended September 30, 2014.

Noninterest expense increased by $100 thousand for the quarter ended September 30, 2015, compared to the quarter ended September 30, 2014, principally due to the following:

- An increase of $177 thousand in loan acquisition and collections expense related to the collections of two loans;
- An increase of $122 thousand in professional fees related to IT consulting;
- An increase of $88 thousand in occupancy and equipment expense, due to increases in rent and IT-related equipment expense; and
- A decrease of $277 thousand in salaries and employee benefits, principally due to the current quarter benefit recognized upon the forfeiture of stock awards and a decrease in incentive compensation. This decrease is partially offset by an increase in employee head count.

Financial Condition

Overview

At September 30, 2015, total assets were $858.2 million, an increase of $7.5 million, or 0.9%, compared to June 30, 2015. The principal components of the change in the balance sheet follow.

The loan portfolio – excluding loans held for sale – grew by $13.7 million, or 2.2%, compared to June 30, 2015, principally on the strength of $13.0 million of net growth in commercial loans purchased or originated by the Bank's Loan Acquisition and Servicing Group ("LASG") and net growth of $4.1 million in commercial originations by the Bank's Community Banking Division. This net growth was offset by a $5.8 million decrease in the Community Banking Division's residential and consumer loan portfolio.

Loans generated by the LASG totaled $34.4 million for the quarter ended September 30, 2015. The growth in LASG loans consisted of $23.5 million of purchased loans, at an average price of 99.5%, and $10.9 million of originated loans. SBA loans closed during the quarter totaled $10.6 million, of which $7.3 million were funded and $5.5 million were sold in the secondary market. Residential and consumer loan production sold in the secondary market totaled $28.9 million for the quarter.

As noted above in "*Description of Business Stategy-Business Overview,*" the Company made certain commitments to the Board of Governors of the Federal Reserve System in connection with the merger of FHB Formation LLC with and into the Company in December 2010. The Company's loan purchase and commercial real estate loan availability under these conditions follow.

Basis for Regulatory Condition	Condition	Availability at September 30, 2015 (Dollars in millions)
Total Loans	Purchased loans may not exceed 40% of total loans	$ 65.3
Regulatory Capital	Non-owner occupied commercial real estate loans may not exceed 300% of total risk-based capital	$ 130.5

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An overview of the LASG portfolio follows:

	LASG Portfolio Three Months Ended September 30,							
	2015				2014			
	Purchased	Originated	Secured Loans to Broker-Dealers	Total LASG	Purchased	Originated	Secured Loans to Broker-Dealers	Total LASG
	(Dollars in thousands)							
Loans purchased or originated during the period:								
Unpaid principal balance	$23,583	$10,941	$ -	$34,524	$16,117	$16,358	$ 24,000	$56,475
Net investment basis	23,458	10,944	-	34,402	13,167	16,353	24,000	53,520
Loan returns during the period:								
Yield	12.07 %	5.67 %	0.50 %	8.23 %	12.76 %	9.88 %	0.42 %	10.93 %
Total Return (1)	12.11 %	5.67 %	0.50 %	8.26 %	12.75 %	10.53 %	0.42 %	11.05 %
Total loans as of period end:								
Unpaid principal balance	$249,229	$119,732	$ 60,000	$428,961	$244,910	$60,534	$ 48,000	$353,444
Net investment basis	$214,199	$119,670	$ 60,005	$393,874	$205,928	$60,497	$ 48,000	$314,425

(1) The total return on purchased loans represents scheduled accretion, accelerated accretion, gains on asset sales, and other noninterest income recorded during the period divided by the average invested balance, on an annualized basis.

Assets

Cash, Short-term Investments and Securities

Cash and short-term investments were $86.2 million as of September 30, 2015, a decrease of $3.7 million, or 4.1%, from $89.9 million at June 30, 2015. The decrease is primarily due to loan purchases for the quarter, offset by growth in the Bank's deposit balances.

Available-for-sale securities totaled $101.3 million as of September 30, 2015 as compared to $101.9 million as of June 30, 2015, representing a decrease of $564 thousand or 0.5%. Included in available-for-sale securities are securities issued by government agencies and government-sponsored enterprises, as well as an investment of approximately $5.0 million in a CRA qualified fund that seeks to invest in securities either issued or guaranteed by the U.S. government or its agencies. At September 30, 2015, securities with a fair value of $3.0 million were pledged for outstanding borrowings.

Loans

The Company's loan portfolio (excluding loans held-for-sale) by lending division follows:

	September 30, 2015				
	Community Banking Division	LASG	SBA National	Total	Percent of Total
	(Dollars in thousands)				
Originated loans:					
Residential real estate	$102,434	$-	$136	$102,570	16.39 %
Home equity	22,480	-	-	22,480	3.59 %
Commercial real estate: non-owner occupied	49,930	52,976	668	103,574	16.55 %
Commercial real estate: owner occupied	23,003	15,091	11,205	49,299	7.88 %
Commercial business	11,559	111,607	3,310	126,476	20.21 %
Consumer	7,244	-	-	7,244	1.16 %
Subtotal	216,650	179,674	15,319	411,643	65.77 %
Purchased loans:					
Residential real estate	-	3,214	-	3,214	0.51 %
Commercial business	-	258	-	258	0.04 %
Commercial real estate: non-owner occupied	-	140,709	-	140,709	22.48 %
Commercial real estate: owner occupied	-	70,018	-	70,018	11.19 %
Subtotal	-	214,199	-	214,199	34.23 %
Total	$216,650	$393,873	$15,319	$625,842	100.00%

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	June 30, 2015				
	Community Banking Division	LASG	SBA National	Total	Percent of Total
	(Dollars in thousands)				
Originated loans:					
Residential real estate	$106,138	$137	$-	$106,275	17.36 %
Home equity	24,326	-	-	24,326	3.97 %
Commercial real estate: non-owner occupied	48,933	53,051	3,865	105,849	17.29 %
Commercial real estate: owner occupied	21,657	16,507	4,461	42,576	6.96 %
Commercial business	11,597	108,577	2,637	122,860	20.06 %
Consumer	7,659	-	-	7,659	1.25 %
Subtotal	220,310	178,272	10,963	409,545	66.90 %
Purchased loans:					
Residential real estate	-	2,068	-	2,068	0.34 %
Commercial business	-	273	-	273	0.04 %
Commercial real estate: non-owner occupied	-	128,182	-	128,182	20.94 %
Commercial real estate: owner occupied	-	72,069	-	72,069	11.77 %
Subtotal	-	202,592	-	202,592	33.10 %
Total	$220,310	$380,864	$10,963	$612,137	100.00%

Classification of Assets

Loans are classified as non-performing when 90 days past due, unless a loan is well-secured and in the process of collection. Loans less than 90 days past due, for which collection of principal or interest is considered doubtful, also may be designated as non-performing. In both situations, accrual of interest ceases. The Company typically maintains such loans as non-performing until the respective borrowers have demonstrated a sustained period of payment performance.

In cases where a borrower experiences financial difficulties and the Company makes certain concessionary modifications, the loan is classified as a troubled debt restructuring ("TDR"). Concessionary modifications may include adjustments to interest rates, extensions of maturity, or other actions intended to minimize economic loss and avoid foreclosure or repossession of collateral. Nonaccrual loans that are restructured generally remain on nonaccrual status for a minimum period of six months to demonstrate that the borrower can meet the restructured terms. If the restructured loan is on accrual status prior to being modified, it is reviewed to determine if the modified loan should remain on accrual status. If the borrower's ability to meet the revised payment schedule is not reasonably assured, the loan is classified as a nonaccrual loan. With limited exceptions, loans classified as TDRs remain classified as such until the loan is paid off.

Other nonperforming assets include other real estate owned ("OREO") and other personal property securing loans repossessed by the Bank. The real estate and personal property collateral for commercial and consumer loans is written down to its estimated realizable value upon repossession. Revenues and expenses are recognized in the period when received or incurred on OREO and in substance foreclosures. Gains and losses on disposition are recognized in noninterest income.

The following table details the Company's nonperforming assets and other credit quality indicators as of September 30, 2015 and June 30, 2015. Management believes that, based on their carrying amounts, nonperforming assets are well secured based on the estimated fair value of underlying collateral.

	Non-Performing Assets at September 30, 2015			
	Originated	Purchased	Total	
	(Dollars in thousands)			
Loans:				
Residential real estate	$3,165	$ -	$3,165	
Home equity	20	-	20	
Commercial real estate	529	6,939	7,468	
Commercial business	2	-	2	
Consumer	153	-	153	
Subtotal	3,869	6,939	10,808	
Real estate owned and other repossessed collateral	1,279	-	1,279	
Total	$5,148	$ 6,939	$12,087	
Ratio of nonperforming loans to total loans			1.73	%
Ratio of nonperforming assets to total assets			1.41	%
Ratio of loans past due to total loans			1.35	%
Nonperforming loans that are current			$5,221	
Commercial loans risk rated substandard or worse			$9,936	
Troubled debt restructurings:				
On accrual status			$6,816	
On nonaccrual status			$1,443	

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	Non-Performing Assets at June 30, 2015		
	Originated	Purchased	Total
	(Dollars in thousands)		
Loans:			
Residential real estate	$3,021	$ -	$3,021
Home equity	11	-	11
Commercial real estate	994	6,532	7,526
Commercial business	2	-	2
Consumer	190	-	190
Subtotal	4,218	6,532	10,750
Real estate owned and other repossessed collateral	1,651	-	1,651
Total	$5,869	$ 6,532	$12,401
Ratio of nonperforming loans to total loans			1.76 %
Ratio of nonperforming assets to total assets			1.46 %
Ratio of loans past due to total loans			1.08 %
Nonperforming loans that are current			$5,357
Commercial loans risk rated substandard or worse			$8,910
Troubled debt restructurings:			
On accrual status			$6,365
Nonaccrual status			$2,131

At September 30, 2015, nonperforming assets totaled $12.1 million, or 1.4% of total assets, as compared to $12.4 million, or 1.5% of total assets, at June 30, 2015.

Allowance for Loan Losses

In connection with the application of the acquisition method of accounting for the merger on December 29, 2010, the allowance for loan losses was reduced to zero when the loan portfolio was marked to its then current fair value. Since that date, the Company has provided for an allowance for loan losses as new loans are originated or in the event that credit exposure in the pre-merger loan portfolio or other acquired loans exceeds the exposure estimated when initial fair values were determined.

The Company’s allowance for loan losses was $2.1 million as of September 30, 2015, which represents an increase of $139 thousand from $1.9 million as of June 30, 2015. The increase during the period was principally due to increased volume of newly originated loans.

The following table details ratios related to the allowance for loan losses for the periods indicated.

	September 30, 2015	June 30, 2015	September 30, 2014
Allowance for loan losses to nonperforming loans	19.11 %	17.92 %	21.12 %
Allowance for loan losses to total loans	0.33 %	0.31 %	0.28 %
Last twelve months of net-charge offs to average loans	0.03 %	0.03 %	0.09 %

While management believes that it uses the best information available to make its determinations with respect to the allowance, there can be no assurance that the Company will not have to increase its provision for loan losses in the future as a result of changing economic conditions, adverse markets for real estate or other factors.

Other Assets

The cash surrender value of the Company's bank-owned life insurance ("BOLI") assets increased $111 thousand, or 0.7% to $15.4 million at September 30, 2015, compared to $15.3 million at June 30, 2015. Increases in cash surrender value are recognized in other income and are not subject to income taxes. Borrowing on, or surrendering a policy, may subject the Company to income tax expense on the increase in cash surrender value. For these reasons, management considers BOLI an illiquid asset. BOLI represented 12.5% of the Company's total risk-based capital at September 30, 2015.

Intangible assets totaled $2.1 million and $2.2 million at September 30, 2015 and June 30, 2015, respectively. The $131 thousand decrease was the result of core deposit intangible asset amortization during the period.

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Deposits, Borrowed Funds, Capital Resources and Liquidity

Deposits

The Company’s principal source of funding is its core deposit accounts. At September 30, 2015, non-maturity accounts, and certificates of deposit with balances less than $250 thousand represented 100% of total deposits.

Total deposits increased $18.7 million to $693.5 million as of September 30, 2015 from $674.8 million as of June 30, 2015. The increase, which funded growth in the Company’s loan portfolio, was centered mainly in money market accounts attracted through the Bank’s community bank division. The composition of total deposits at September 30, 2015 and June 30, 2015 follows.

	September 30, 2015		June 30, 2015	
	Amount	Percent of Total	Amount	Percent of Total
	(Dollars in thousands)			
Demand deposits	$62,687	9.04 %	$60,383	8.95 %
NOW accounts	71,767	10.35 %	64,289	9.53 %
Regular and other savings	34,912	5.03 %	35,845	5.31 %
Money market deposits	182,690	26.34 %	168,527	24.98 %
Total non-certificate accounts	352,056	50.77 %	329,044	48.76 %
Term certificates less than $250 thousand	341,422	49.23 %	345,146	51.15 %
Term certificates of $250 thousand or more	-	0.00 %	569	0.08 %
Total certificate accounts	341,422	49.23 %	345,715	51.24 %
Total deposits	$693,478	100.00%	$674,759	100.00%

Borrowed Funds

Advances from the FHLB were $30.2 million at both September 30, 2015 and June 30, 2015, respectively. At September 30, 2015, the Company had pledged investment securities with a fair value of $3.0 million, as well as certain residential real estate loans, commercial real estate loans, and FHLB deposits free of liens or pledges to secure outstanding advances and available additional borrowing capacity.

During the quarter ended September 30, 2015, the Company's wholesale repurchase agreements paid off at maturity, representing a $10.0 million decrease from June 30, 2015.

Short-term borrowings, consisting of sweep accounts and repurchase agreements, were $2.5 million and $2.3 million as of September 30, 2015 and June 30, 2015, respectively.

Liquidity

The following table is a summary of unused borrowing capacity of the Company at September 30, 2015, in addition to traditional retail deposit products (dollars in thousands):

Brokered time deposits	$214,562	Subject to policy limitation of 25% of total assets
Federal Home Loan Bank of Boston	45,030	Unused advance capacity subject to eligible and qualified collateral
Federal Discount Window Borrower-in-Custody	2,124	Unused credit line subject to the pledge of loans
Other available lines	17,500	
Total unused borrowing capacity	279,216	

Retail deposits and other core deposit sources including deposit listing services are used by the Bank to manage its overall liquidity position. While we currently do not seek wholesale funding such as FHLB advances and brokered deposits, the ability to raise them remains an important part of our liquidity contingency planning. While we closely monitor and forecast our liquidity position, it is affected by asset growth, deposit withdrawals and meeting other contractual obligations and commitments. The accuracy of our forecast assumptions may increase or decrease our overall available liquidity. To utilize the FHLB advance capacity, the purchase of additional capital stock in the Federal Home Loan Bank of Boston may be required.

At September 30, 2015, the Company had $377.6 million of immediately accessible liquidity, defined as cash that the Bank reasonably believes could be raised within 7 days through collateralized borrowings, brokered deposits or security sales. This position represented 44.0% of total assets. The Company also had $86.2 million of cash and cash equivalents at September 30, 2015.

Management believes that there are adequate funding sources to meet its liquidity needs for the foreseeable future. Primary funding sources are the repayment of principal and interest on loans, the renewal of time deposits, the potential for growth in the deposit base, and the credit availability from the FHLB. Management does not believe that the terms and conditions that will be present at the renewal of these funding sources will significantly impact the Company's operations, due to its management of the maturities of its assets and liabilities.

Capital

The carrying amount and unpaid principal balance of junior subordinated debentures totaled $8.7 million and $16.5 million, respectively, as of September 30, 2015. This debt represents qualifying Tier 1 capital for the Company, up to a maximum of 25% of total Tier 1 capital. At September 30, 2015, the carrying amounts of the junior subordinated notes, net of the Company's $496 thousand investment in the affiliated trusts, qualified as Tier 1 capital.

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At September 30, 2015, shareholders’ equity was $113.7 million, an increase of $977 thousand, or 0.9% from June 30, 2015. Book value per outstanding common share was $11.85 at September 30, 2015 and $11.76 at June 30, 2015. Tier 1 capital to total average assets of the Company was 14.23% as of September 30, 2015 and 14.49% at June 30, 2015.

Under the capital rules, risk-based capital ratios are calculated by dividing Tier 1 and total risk-based capital, respectively, by risk-weighted assets. Assets and off-balance sheet credit equivalents are assigned to one of several risk-weight categories, based primarily on relative risk. The rules require banks and bank holding companies to maintain a minimum common equity Tier 1 capital ratio of 4.5%, a minimum Tier 1 capital ratio of 6%, a total capital ratio of 8% and a leverage ratio of 4%. Additionally, subject to a transition schedule, the capital rules require a bank holding company to establish a capital conservation buffer of Tier 1 capital in an amount above the minimum risk-based capital requirements for "adequately capitalized" institutions equal to 2.5% of total risk weighted assets, or face restrictions on the ability to pay dividends, pay discretionary bonuses, and to engage in share repurchases.

Under rules effective January 1, 2015, a bank holding company, such as the Company, is considered "well capitalized" if the bank holding company (i) has a total risk based capital ratio of at least 10%, (ii) has a Tier 1 risk-based capital ratio of at least 6%, and (iii) is not subject to any written agreement order, capital directive or prompt corrective action directive to meet and maintain a specific capital level for any capital measure. In addition, the FDIC has amended its prompt corrective action rules to reflect the revisions made by the revised capital rules described above. Under the FDIC's revised rules, which became effective January 1, 2015, an insured state nonmember bank is considered "well capitalized" if it (i) has a total risk-based capital ratio of 10.0% or greater; (ii) a Tier 1 risk-based capital ratio of 8.0% or greater; (iii) a common Tier 1 equity ratio of 6.5% or greater, (iv) a leverage capital ratio of 5.0% or greater; and (iv) is not subject to any written agreement, order, capital directive, or prompt corrective action directive to meet and maintain a specific capital level for any capital measure.

The Company and the Banks are considered "well capitalized" under all regulatory definitions. The Company's and the Bank's regulatory capital ratios are set forth below.

	Actual		Minimum Capital Requirements		Minimum To Be Well Capitalized Under Prompt Correction Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
	(Dollars in thousands)					
September 30, 2015:						
Common equity tier 1 capital to risk weighted assets:						
Company	$122,789	19.69%	$28,063	>4.5%	N/A	N/A
Bank	110,172	17.63%	28,115	>4.5%	40,610	>6.5%

Total capital to risk weighted assets:						
Company	124,891	20.03%	49,889	>8.0%	N/A	N/A
Bank	113,409	18.15%	49,982	>8.0%	62,447	>10.0%
Tier 1 capital to risk weighted assets:						
Company	122,789	19.69%	24,945	>4.0%	N/A	N/A
Bank	110,172	17.63%	24,991	>4.0%	37,486	>6.0%
Tier 1 capital to average assets:						
Company	122,789	14.23%	34,511	>4.0%	N/A	N/A
Bank	110,172	12.79%	34,467	>4.0%	43,084	>5.0%
June 30, 2015:						
Common equity tier 1 capital to risk weighted assets:						
Company	$121,224	19.82%	$27,523	>4.5%	N/A	N/A
Bank	107,477	17.55%	27,558	>4.5%	39,806	>6.5%
Total capital to risk weighted assets:						
Company	123,187	20.14%	48,932	>8.0%	N/A	N/A
Bank	111,228	18.16%	48,999	>8.0%	61,249	>10.0%
Tier 1 capital to risk weighted assets:						
Company	121,224	19.82%	24,465	>4.0%	N/A	N/A
Bank	107,477	17.55%	24,496	>4.0%	36,744	>6.0%
Tier 1 capital to average assets:						
Company	121,224	14.49%	33,464	>4.0%	N/A	N/A
Bank	107,477	12.86%	33,421	>4.0%	41,776	>5.0%

Off-balance Sheet Financial Instruments

The Company is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit, unused lines of credit and standby letters of credit. These instruments involve, to varying degrees, elements of credit and interest-rate risk in excess of the amounts recognized in the condensed consolidated balance sheet. The contract or notional amounts of these instruments reflect the extent of the Company’s involvement in particular classes of financial instruments.

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See Part I. Item I. “Notes to Unaudited Consolidated Financial Statements – Note 10: Commitments and Contingencies” for further discussion.

Results of Operations

General

Net income increased by $220 thousand to $1.9 million for the quarter ended September 30, 2015, compared to $1.6 million for the quarter ended September 30, 2014. When compared to the prior year, increases in net income for the three months ended September 30, 2015 resulted principally from higher noninterest income, as well as a slight increase in transactional income recognized on purchased loans.

The following table details the total return on purchased loans, which includes transactional income of $2.2 million for the quarter ended September 30, 2015, an increase of $209 thousand from the quarter ended September 30, 2014.

	Total Return on Purchased Loans Three Months Ended September 30,			
	2015		2014	
	Income	Return (1)	Income	Return (1)
	(Dollars in thousands)			
Regularly scheduled interest and accretion	$3,887	7.70 %	$4,497	8.80 %
Transactional income:				
Gain (loss) on loan sales	-	0.00 %	(4)	-0.01 %
Gain on sale of real estate owned	22	0.04 %	-	0.00 %
Other noninterest income	-	0.00 %	-	0.00 %
Accelerated accretion and loan fees	2,208	4.37 %	2,025	3.96 %
Total transactional income	2,230	4.41 %	2,021	3.95 %
Total	$6,117	12.11 %	$6,518	12.75 %

(1) The total return on purchased loans represents scheduled accretion, accelerated accretion, gains on asset sales, and other noninterest income recorded during the period divided by the average invested balance, on an annualized basis.

Net Interest Income

Net interest and dividend income before provision for loan losses decreased by $230 thousand, or 2.4%, for the quarter ended September 30, 2015, compared to the quarter ended September 30, 2014. The decrease is primarily due to lower interest income in the purchased loan portfolio, mainly due to a decline in yield to 12.1% in the current quarter from 12.8% earned in the quarter ended September 30, 2014.

The various components of transactional income are set forth in the table below entitled "Total Return on Purchased Loans." When compared to the three months ended September 30, 2014, transactional interest income increased by $183 thousand. The following table summarizes interest income and related yields recognized on the loan portfolios:

	Interest Income and Yield on Loans Three Months Ended September 30,					
	2015			2014		
	Average Balance	Interest Income	Yield	Average Balance	Interest Income	Yield
	(Dollars in thousands)					
Community Banking Division	$238,873	$2,924	4.86 %	$241,165	$3,062	5.04 %
LASG:						
Originated	118,574	1,696	5.67 %	52,430	1,306	9.88% (1)
Purchased	200,385	6,095	12.07%	202,856	6,522	12.76 %
Secured Loans to Broker-Dealers	60,007	75	0.50 %	29,905	32	0.42 %
Total LASG	378,966	7,866	8.23 %	285,191	7,860	10.93 %
Total	$617,839	$10,790	6.93 %	$526,356	$10,922	8.23 %

(1) The yield for LASG originated loans included $335 thousand of loan fees in the quarter ended September 30, 2014, compared to $1 thousand of loan fees in the quarter ended September 30, 2015. The yield for LASG originated loans, excluding loan fees, was 7.35% in the quarter ended September 30, 2014.

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In the quarter ended September 30, 2015, net interest income was negatively affected by a lower level of noncash accretion of fair value adjustments resulting from the 2010 merger than in the quarter ended September 30, 2014. The effect of such accretion will continue to diminish as financial instruments held at the merger mature or prepay.

The Company's interest rate spread and net interest margin decreased by 70 basis points for the quarter ended September 30, 2015 compared to the quarter ended September 30, 2014. The following sets forth the average balance sheets, interest income and interest expense, and average yields and costs for the three months ended September 30, 2015 and 2014.

NORTHEAST BANCORP AND SUBSIDIARY CONSOLIDATED AVERAGE BALANCE SHEETS AND ANNUALIZED YIELDS
(Unaudited)
(Dollars in thousands)

	Three Months Ended September 30,							
	2015				2014			
	Average Balance	Interest Income/ Expense	Average Yield/ Rate		Average Balance	Interest Income/ Expense	Average Yield/ Rate	
Assets:								
Interest-earning assets:								
Investment securities (1)	$102,241	$228	0.88	%	$112,250	$244	0.86	%
Loans (2) (3)	617,839	10,790	6.93	%	526,356	10,922	8.23	%
Federal Home Loan Bank stock	4,102	34	3.29	%	4,102	15	1.45	%
Short-term investments (4)	99,649	61	0.24	%	82,762	51	0.24	%
Total interest-earning assets	823,831	11,113	5.35	%	725,470	11,232	6.14	%
Cash and due from banks	3,026				2,712			
Other non-interest earning assets	36,420				34,736			
Total assets	$863,277				$762,918			
Liabilities & Stockholders' Equity:								
Interest-bearing liabilities:								
NOW accounts	$69,619	$46	0.26	%	$63,608	$41	0.26	%
Money market accounts	170,566	353	0.82	%	86,294	110	0.51	%

Savings accounts	36,360	12	0.13	%	34,361	11	0.13	%
Time deposits	350,867	954	1.08	%	340,368	968	1.13	%
Total interest-bearing deposits	627,412	1,365	0.86	%	524,631	1,130	0.85	%
Short-term borrowings	1,950	9	1.83	%	3,320	9	1.08	%
Borrowed funds	39,324	344	3.47	%	52,979	416	3.12	%
Junior subordinated debentures	8,650	154	7.06	%	8,461	206	9.66	%
Total interest-bearing liabilities	677,336	1,872	1.10	%	589,391	1,761	1.19	%
Non-interest bearing liabilities:								
Demand deposits and escrow accounts	64,008				53,245			
Other liabilities	8,763				7,891			
Total liabilities	750,107				650,527			
Stockholders' equity	113,170				112,391			
Total liabilities and stockholders' equity	$863,277				$762,918			
Net interest income		$9,241				$9,471		
Interest rate spread			4.25	%			4.95	%
Net interest margin (5)			4.45	%			5.18	%

(1) Interest income and yield are stated on a fully tax-equivalent basis using a 34% tax rate.
(2) Includes loans held for sale.
(3) Nonaccrual loans are included in the computation of average, but unpaid interest has not been included for purposes of determining interest income.
(4) Short term investments include FHLB overnight deposits and other interest-bearing deposits.

(5) Net interest margin is calculated as net interest income divided by total interest-earning assets.

The following table presents the extent to which changes in volume and interest rates of interest earning assets and interest bearing liabilities have affected the Company's interest income and interest expense during the periods indicated. Information is provided in each category with respect to (i) changes attributable to changes in volume (changes in volume multiplied by prior period rate), (ii) changes attributable to changes in rates (changes in rates multiplied by prior period volume) and (iii) change attributable to a combination of changes in rate and volume (change in rates multiplied by the changes in volume). Changes attributable to the combined impact of volume and rate have been allocated proportionately to the changes due to volume and the changes due to rate.

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	Three Months Ended September, 2015 compared to 2014		
	Change Due to Volume	Change Due to Rate	Total Change
	(Dollars in thousands)		
Interest earning assets:			
Investment securities	$(22)	$6	$ (16)
Loans	1,741	(1,873)	(132)
Federal Home Loan Bank stock	-	19	19
Short-term investments	10	-	10
Total interest-earning assets	1,729	(1,848)	(119)
Interest-bearing liabilities:			
Interest-bearing deposits	197	38	235
Short-term borrowings	(5)	5	-
Borrowed funds	(115)	43	(72)
Junior subordinated debentures	5	(57)	(52)
Total interest-bearing liabilities	82	29	111
Total change in net interest income	$1,647	$(1,877)	$ (230)

Provision for Loan Losses

Quarterly, the Company determines the amount of the allowance for loan losses that is appropriate to provide for losses inherent in the Company's loan portfolios, with the provision for loan losses determined by the net change in the allowance for loan losses. For loans acquired with deteriorated credit quality, a provision for loan a loss is recorded when estimates of future cash flows are lower than had been previously expected. See Part I. Item I. "Notes to Unaudited Consolidated Financial Statements — Note 4: Loans, Allowance for Loan losses and Credit Quality" for further discussion.

The provision for loan losses for periods subsequent to the merger with FHB Formation LLC reflects the impact of adjusting loans to their then fair values, as well as the elimination of the allowance for loan losses in accordance with the acquisition method of accounting. Subsequent to the merger, the provision for loan losses has been recorded based on estimates of inherent losses in newly originated loans and for incremental reserves required for pre-merger loans based on estimates of deteriorated credit quality post-merger.

The provision for loan losses for the quarter ended September 30, 2015 and 2014 was $169 thousand and $320 thousand, respectively. The decrease in the Company's loan loss provision resulted principally from a higher level of allowance built over the year, as well as a decrease in charge-offs.

Noninterest Income

Noninterest income increased by $551 thousand for the quarter ended September 30, 2015, compared to the quarter ended September 30, 2014, principally due to an increase in gains realized on sale of portfolio loans. The recent quarter includes gains realized on sale of SBA loans of $675 thousand, compared to an $80 thousand gain on sale of commercial loans in the quarter ended September 30, 2014.

Noninterest Expense

Noninterest expense increased by $100 thousand for the quarter ended September 30, 2015, compared to the quarter ended September 30, 2014, principally due to the following:

- An increase of $177 thousand in loan acquisition and collections expense related to the collections of two loans;
- An increase of $122 thousand in professional fees related to IT consulting;
- An increase of $88 thousand in occupancy and equipment expense, due to increases in rent and IT-related equipment expense; and
- A decrease of $277 thousand in salaries and employee benefits, principally due to the current quarter benefit recognized upon the forfeiture of stock awards and a decrease in incentive compensation. This decrease is partially offset by an increase in employee head count.

Income Taxes

The Company's effective tax rate for the quarter ended September 30, 2015 was 37.07%, compared to 36.53% for the quarter ended September 30, 2014. The increase in the quarter was primarily due to fluctuations in projected pre-tax income and the adoption of ASU 2014-01.

Item 3. Quantitative and Qualitative Disclosure about Market Risk

Not required for smaller reporting companies.

Item 4. Controls and Procedures

The Company maintains controls and procedures designed to ensure that information required to be disclosed in the reports the Company files or submits under the Securities Exchange Act of 1934 (“Exchange Act”) is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the Securities and Exchange Commission, and that such information is accumulated and communicated to the Company’s management, including the Chief Executive Officer and Chief Financial Officer (the Company’s principal executive officer and principal financial officer, respectively), as appropriate to allow for timely decisions regarding timely disclosure. In designing and evaluating disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management is required to apply its judgment in evaluating the cost/benefit relationship of possible controls and procedures.

The Company's management, with the participation of the Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of its disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of the end of the period covered by this Quarterly Report on Form 10-Q.

Based on this evaluation of the Company's disclosure controls and procedures, the Chief Executive Officer and Chief Financial Officer have concluded that these disclosure controls and procedures were effective as of September 30, 2015.

There were no changes in the Company's internal controls over financial reporting (as defined in Rule 13a-15(f) of the Exchange Act) that occurred during the quarter ended September 30, 2015 that have materially affected, or is reasonably likely to materially affect, the Company's internal controls over financial reporting.

PART II – OTHER INFORMATION

Item 1. Legal Proceedings

None.

Item 1A. Risk Factors

Not required for smaller reporting companies.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

On April 23, 2014, the Company announced that its Board of Directors authorized the Company to purchase up to 870,000 shares of its common stock, representing 8.3% of the Company's outstanding common shares and approximately $8.4 million based on the Company's closing stock price on April 22, 2014.

On April 30, 2015, the Board of Directors voted to amend the existing stock repurchase program to authorize the Company to purchase an additional 500,000 shares of its common stock, representing

5.1% of the Company's outstanding common shares or approximately $4.7 million based on the Company's closing price on April 29, 2015. The amended stock repurchase program will expire on April 30, 2017.

As of September 30, 2015, 1,054,362 shares had been repurchased under this plan at a weighted average price of $9.52.

The following table sets forth information with respect to purchases made by the Company of its common stock during the three months ended September 30, 2015.

Period	**Total Number of Shares Purchased (1)**	**Average Price Per Share**	**Total Number of Shares Purchased as Part of Publicly Announced Programs**	**Maximum Number of Shares that May Yet Be Purchased Under the Program**
Jul. 1 –Jul. 31	17,300	$ 10.07	1,019,162	350,838
Aug. 1 – Aug. 31	13,900	10.60	1,033,062	336,938
Sep. 1 – Sep. 30	21,300	10.65	1,054,362	315,638

(1) Based on trade date, not settlement date

Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

None.

Item 6. Exhibits

Exhibits No.	Description
31.1	Certification of the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (Rule 13a-14(a)). *
31.2	Certification of the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (Rule 13a-14(a)). *
32.1	Certificate of the Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (Rule 13a-14(b)). **
32.2	Certificate of the Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (Rule 13a-14(b)). **
101	The following materials from Northeast Bancorp’s Quarterly Report on Form 10-Q for the quarter ended September 30, 2015 formatted in XBRL: (i) Consolidated Balance Sheets at September 30, 2015 and June 30, 2015; (ii) Consolidated Statements of Income for the three months ended September 30, 2015 and 2014; (iii) Consolidated Statements of Comprehensive Income for the three months ended September 30, 2015 and 2014; (iv) Consolidated Statements of Changes in Shareholders’ Equity for the three months ended September 30, 2015 and 2014; (v) Consolidated Statements of Cash Flows for the three months ended September 30, 2015 and 2014; and (v) Notes to Unaudited Consolidated Financial Statements.

* Filed herewith

** Furnished herewith

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SIGNATURES

Pursuant to the requirements of the Securities Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Date: November 13, 2015 **NORTHEAST BANCORP**

By: /s/ Richard Wayne
Richard Wayne
President and Chief Executive Officer

By: /s/ Brian Shaughnessy
Brian Shaughnessy
Chief Financial Officer

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NORTHEAST BANCORP

Index to Exhibits

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