BROWN FORMAN CORP
Form 8-K
June 07, 2017

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

FORM 8-K

CURRENT REPORT
Pursuant to Section 13 or 15(d) of
the Securities Exchange Act of 1934

Date of Report (Date of earliest event reported):
June 7, 2017

Brown-Forman Corporation

(Exact Name of Registrant as Specified in its Charter)

Delaware	001-00123	61-0143150
(State or Other Jurisdiction of Incorporation)	(Commission File Number)	(I.R.S. Employer Identification No.)

850 Dixie Highway, Louisville, Kentucky	40210
(Address of Principal Executive Offices)	(Zip Code)

Registrant’s telephone number, including area code: (502) 585-1100

Not Applicable
(Former Name or Former Address, if Changed Since Last Report.)

Check the appropriate box below if the Form 8-K filing is intended to simultaneously satisfy the filing obligation of the registrant under any of the following provisions:

o Written communications pursuant to Rule 425 under the Securities Act (17 CFR 230.425)

o Soliciting material pursuant to Rule 14a-12 under the Exchange Act (17 CFR 240.14a-12)

o Pre-commencement communications pursuant to Rule 14d-2(b) under the Exchange Act (17 CFR 240.14d-2(b))

o Pre-commencement communications pursuant to Rule 13e-4(c) under the Exchange Act (17 CFR 240.13e-4(c))

Item 2.02. Results of Operations and Financial Condition.

On June 7, 2017, Brown-Forman Corporation issued a press release reporting its operating results for the fourth fiscal quarter and fiscal year ended April 30, 2017, and its outlook for fiscal year 2018. A copy of this press release is attached hereto as Exhibit 99.1.

The information pursuant to this Item 2.02 - Results of Operations and Financial Condition, including the information in Exhibit 99.1, is being furnished and shall not be deemed "filed" for any purpose, including for purposes of Section 18 of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), or otherwise subject to the liabilities of that Section, nor shall it be deemed incorporated by reference into any filing under the Securities Act of 1933, as amended, or under the Exchange Act, regardless of any general incorporation language in such filing, except as shall be expressly set forth by specific reference in such filing.

Item 9.01. Financial Statements and Exhibits.

(d) Exhibits

Exhibit No.	Description
99.1	Brown-Forman Corporation Press Release dated June 7, 2017.

SIGNATURES

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

	BROWN-FORMAN CORPORATION (Registrant)
Date: June 7, 2017	/s/ Michael E. Carr, Jr. Michael E. Carr, Jr. Vice President, Managing Attorney and Assistant Corporate Secretary

EXHIBIT INDEX

Exhibit No.	Description
99.1	Brown-Forman Corporation Press Release dated June 7, 2017.

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(In thousands)

	Cost	Unrealized Gains	Unrealized Losses	Market Value
Mortgage-backed securities	$56,669	$636	$67	$57,238
U.S. Government corporations and agencies	49,157	212	-	49,369
Municipal bonds	12,538	137	84	12,591
Other equity securities	211	-	82	129
	$118,575	$985	$233	$119,327

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Investment securities held to maturity at June 30, 2010 consist of the following:

		Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses		Estimated Market Value
			(In thousands)			
Municipal bonds	$	631	-	-	$	631

The mortgage-backed securities, callable bonds and municipal bonds available for sale have the following maturities at September 30, 2010:

		Amortized cost		Estimated market value
		(In thousands)		
Due or callable in one year or less	$	33,009	$	33,200
Due or callable in 1 - 5 years		70,009		70,466
Due or callable in 5 - 10 years		270		289
Due or callable in greater than 10 years		14,186		14,731
Total debt securities	$	117,474	$	118,686

All other securities available for sale at September 30, 2010 are saleable within one year. The Bank held $611,000 and $631,000 in investment securities that are being held to maturity at September 30, 2010 and June 30, 2010, respectively. The investment securities held to maturity have annual returns of principal and will be fully matured between 2014 and 2019.

The expected returns of principal of investments held to maturity are as follows as of September 30, 2010 (dollars in thousands):

October 1, 2010 through June 30, 2011	$	45
2012		68
2013		71
2014		74
2015		77
2016 and thereafter		276
	$	611

Gross proceeds on the sale of investment and mortgage-backed securities were $4.0 million and $0.5 million for the three month periods ended September 30, 2010 and 2009, respectively. Gross realized gains for the three month periods ended September 30, 2010 and 2009 were $44,000 and $0, respectively. Gross realized losses for the three month periods ended September 30, 2010 and 2009 were $0 and $12,000, respectively.

The table below indicates the length of time individual investment securities and mortgage-backed securities have been in a continuous loss position at September 30, 2010:

Less than 12 months		12 months or longer		Total	
Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses

				(In thousands)				
Mortgage-backed securities		21,110	176	-	-		21,110	176
Municipal bonds		516	1	-	-		516	1
Other equity securities		-	-	120	90		120	90
	$	21,626	177	120	90	$	21,746	267
Number of investments			9		1			10

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Securities available for sale are reviewed for possible other-than-temporary impairment on a quarterly basis. During this review, Management considers the severity and duration of the unrealized losses as well as its intent and ability to hold the securities until recovery, taking into account balance sheet management strategies and its market view and outlook. Management also assesses the nature of the unrealized losses taking into consideration factors such as changes in risk-free interest rates, general credit spread widening, market supply and demand, creditworthiness of the issuer or any credit enhancement providers, and the quality of the underlying collateral. Management does not intend to sell these securities in the foreseeable future, and does not believe that it is more likely than not that the Bank will be required to sell a security in an unrealized loss position prior to a recovery in its value. The decline in market value is due to changes in market interest rates. The fair values are expected to recover as the securities approach maturity dates.

9. GOODWILL AND INTANGIBLE ASSET

In June 2010, the Company acquired three branches from Integra Bank National Association (“Integra”), which was accounted for under the purchase method of accounting. Under the purchase method, the Company is required to allocate the cost of an acquired company to the assets acquired, including identified intangible assets, and liabilities assumed based on their estimated fair values at the date of acquisition. The excess cost over the value of net assets acquired represents goodwill, which is not subject to amortization.

Goodwill arising from business combinations represents the value attributable to unidentifiable intangible elements in the business acquired. Goodwill recorded by the Company in connection with its acquisition relates to the inherent value in the business acquired and this value is dependent upon the Company’s ability to provide quality, cost-effective services in a competitive market place. As such, goodwill value is supported ultimately by revenue that is driven by the volume of business transacted. A decline in earnings as a result of a lack of growth or the inability to deliver cost-effective services over sustained periods can lead to impairment of goodwill that could adversely impact earnings in future periods.

Goodwill is not amortized but is tested for impairment when indicators of impairment exist, or at least annually. Potential goodwill impairment exists when the fair value of the reporting unit (as defined by US GAAP) is less than its carrying value. An impairment loss is recognized in earnings only when the carrying amount of goodwill is less than its implied fair value.

As a result of the acquisition, the Company originally recorded a core deposit intangible asset of $1,400,000 and goodwill of $3,130,000. A purchase accounting adjustment was recorded during the three month period ended September 30, 2010 related to deferred tax balances that would have affected the measurement of the amounts recognized at the date of acquisition. This adjustment had the effect of reducing goodwill and increasing deferred taxes by $608,000. As required pursuant to the guidance in FASB ASC 805, Business Combinations, this adjustment has been reflected in the Company’s consolidated statements of financial condition on a retrospective basis.

The following table indicates changes to the core deposit intangible asset and goodwill balances for the three month period ended September 30, 2010:

	Core Deposit Intangible	Goodwill
	(In thousands)	
Balance at June 30, 2010	$ 1,400	$ 2,522
Amortization	(104)	-

Balance at September 30, 2010	$	1,296	$	2,522

The core deposit intangible is being amortized using the double declining balance method over its estimated useful life of 8.75 years. Remaining amortization of the core deposit intangible is as follows (dollars in thousands) as of September 30, 2010:

October 1, 2010 through June 30, 2011	$	207
2012		226
2013		179
2014		142
2015		118
2016 and thereafter		424
	$	1,296

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10. EFFECT OF RECENT ACCOUNTING PRONOUNCEMENTS

In July 2010, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2010-20, Receivables (Topic 310): Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses. The ASU amends FASB Accounting Standards Codification™ (the "Codification" or "ASC") Topic 310, Receivables, to improve the disclosures about the credit quality of an entity's financing receivables and the related allowance for credit losses. As a result of these amendments, an entity is required to disaggregate, by portfolio segment or class of financing receivable, certain existing disclosures and provide certain new disclosures about its financing receivables and related allowance for credit losses.

Existing disclosures are amended to require an entity to provide the following disclosures about its financing receivables on a disaggregated basis:
(1) A rollforward schedule of the allowance for credit losses from the beginning of the reporting period to the end of the reporting period on a portfolio segment basis, with the ending balance further disaggregated on the basis of the impairment method;
(2) For each disaggregated ending balance in item (1) above, the related recorded investment in financing receivables;
(3) The nonaccrual status of financing receivables by class of financing receivables;
(4) Impaired financing receivables by class of financing receivables.

The amendments in the ASU also require an entity to provide the following additional disclosures about its financing receivables:
(1) Credit quality indicators of financing receivables at the end of the reporting period by class of financing receivables;
(2) The aging of past due financing receivables at the end of the reporting period by class of financing receivables;
(3) The nature and extent of troubled debt restructurings that occurred during the period by class of financing receivables and their effect on the allowance for credit losses;
(4) The nature and extent of financing receivables modified as troubled debt restructurings within the previous twelve months that defaulted during the reporting period by class of financing receivables and their effect on the allowance for credit losses; and
(5)Significant purchases and sales of financing receivables during the reporting period disaggregated by portfolio segments.

The disclosures as of the end of a reporting period will be effective for interim and annual reporting periods ending on or after December 15, 2010. The disclosures about activity that occurs during a reporting period will be effective for interim and annual reporting periods beginning on or after December 15, 2010. As this ASU is disclosure-related only, we do not expect it to have an impact on our financial condition or results of operations.

In April 2010, the FASB issued ASU No. 2010-18, Receivables (Topic 310): Effect of Loan Modification when the Loan is Part of a Pool that is Accounted for as a Single Asset (a consensus of the FASB Emerging Issues Task Force). The amendments in this update affect any entity that acquires loans subject to ASC Subtopic 310-30, that accounts for some or all of those loans within pools, and that subsequently modifies one or more of those loans after acquisition. ASU No. 2010-18 is effective for modifications of loans accounted for within pools under Subtopic 310-30 occurring in the interim period ending September 30, 2010, and the amendments are to be applied prospectively. The adoption of this guidance did not have a material impact on the Company's financial statements.

In January 2010, the FASB issued ASU No. 2010-06, Improving Disclosure about Fair Value Measurements, under Topic 820, Fair value Measurements and Disclosures, to improve and provide new disclosures for recurring and nonrecurring fair value measurements under the three-level hierarchy of inputs for transfers in and out of Levels 1 and 2, and activity in Level 3. This update also clarifies existing disclosures of the level of disaggregation for the classes of assets and liabilities and the disclosure about inputs and valuation techniques. ASU No. 2010-06 became effective during the year ended June 30, 2010, except for the disclosures about purchases, sales, issuances, and settlements in the roll forward of activity in Level 3 fair value measurements, which becomes effective for the interim period ending September 30, 2011. The adoption of this guidance is not expected to have a material impact on the Company's financial statements.

In October 2010, the FASB issued a proposed Accounting Standards Update (ASU), "Receivables (Topic 310): Clarifications to Accounting for Troubled Debt Restructurings ("TDR") by Creditors" to assist creditors in determining whether a modification is a TDR. Currently, there is diversity in practice in identifying loan modifications that constitute TDRs, particularly when determining whether a concession has been granted. The clarifications are proposed to be effective for interim and annual periods ending after June 15, 2011, and would be applied retrospectively to restructurings occurring on or after the beginning of the earliest period presented.

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

Forward-Looking Statements

This report contains forward-looking statements that are based on assumptions and may describe future plans, strategies and expectations of the Company. These forward-looking statements are generally identified by use of the words "believe," "expect," "intend," "anticipate," "estimate," "project" or similar expressions. The Company's ability to predi results or the actual effect of future plans or strategies is inherently uncertain. Factors which could have a material adverse effect on the operations of the Company and its subsidiaries include, but are not limited to, general economic conditions, changes in the interest rate environment, legislative or regulatory changes that may adversely affect our business, changes in accounting policies and practices, changes in competition and demand for financial services, adverse changes in the securities markets, changes in deposit flows, changes in the quality or composition of the Company's loan or investment portfolios, and the Company's ability to successfully integrate assets, liabilities, customers, systems, and personnel of the three branches of Integra Bank it is acquiring into its operations and the Company's ability to recognize revenue synergies and cost savings within expected time frames. Additionally, other risks and uncertainties may be described in the Company's Annual Report on Form 10-K as filed with the Securities and Exchange Commission on September 28, 2010, which is available through the SEC's website at www.sec.gov. These risks and uncertainties should be considered in evaluating forward-looking statements and undue reliance should not be placed on such statements. Except as required by applicable law or regulation, the Company does not undertake the responsibility, and specifically disclaims any obligation, to release publicly the result of any revisions that may be made to any forward-looking statements to reflect events or circumstances after the date of the statements or to reflect the occurrence of anticipated or unanticipated events.

Critical Accounting Policies

We consider accounting policies involving significant judgments and assumptions by management that have, or could have, a material impact on the carrying value of certain assets or on income to be critical accounting policies. We consider the following to be our critical accounting policies: allowance for loan losses, deferred income taxes and investment securities.

ALLOWANCE FOR LOAN LOSSES - The allowance for loan losses is the amount estimated by management as necessary to cover probable credit losses in the loan portfolio at the statement of financial condition date. The allowance is established through the provision for loan losses, which is charged to income. Determining the amount of the allowance for loan losses necessarily involves a high degree of judgment. Among the material estimates required to establish the allowance are: loss exposure at default; the amount and timing of future cash flows on impacted loans; value of collateral; and determination of loss factors to be applied to the various elements of the portfolio. All of these estimates are susceptible to significant change. Management reviews the level of the allowance on a quarterly basis and establishes the provision for loan losses based upon an evaluation of the portfolio, past loss experience, current economic conditions and other factors related to the collectability of the loan portfolio. Although we believe that we use the best information available to establish the allowance for loan losses, future adjustments to the allowance may be necessary if economic conditions differ substantially from the assumptions used in making the evaluation. In addition, the Office of Thrift Supervision (OTS), as an integral part of its examination process, periodically reviews our allowance for loan losses. This agency may require us to recognize adjustments to the allowance based on its judgments about information available to it at the time of its examination. A large loss could deplete the allowance and require increased provisions to replenish the allowance, which would negatively affect earnings. For additional discussion, see notes 1 and 5 of the notes to the consolidated financial statements included in Item 8 of the Annual Report on Form 10-K filed with the Securities and Exchange Commission on September 28, 2010.

DEFERRED INCOME TAXES - We use the asset and liability method of accounting for income taxes as prescribed in Accounting Standards Codification (ASC) 740-10-50. Under this method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. If current available information raises doubt as to the realization of the deferred tax assets, a valuation allowance is established. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. We exercise significant judgment in evaluating the amount and timing of recognition of the resulting tax liabilities and assets. These judgments require us to make projections of future taxable income. The judgments and estimates we make in determining our deferred tax assets, which are inherently subjective, are reviewed on a continual basis as regulatory and business factors change. Any reduction in estimated future taxable income may require us to record a valuation allowance against our deferred tax assets. A valuation allowance would result in additional income tax expense in the period, which would negatively affect earnings. The Company applies the provisions of ASC 275-10-50-8 to account for uncertainty in income taxes. The Company had no unrecognized tax benefits as of September 30, 2010 and June 30, 2010. The Company recognized no interest and penalties on the underpayment of income taxes during the three month periods ended September 30, 2010 and 2009, and had no accrued interest and penalties on the balance sheet as of September 30, 2010 and June 30, 2010. The Company has no tax positions for which it is reasonably possible that the total amounts of unrecognized tax benefits will significantly increase with the next twelve months. The Company is no longer subject to U.S. federal, state and local income tax examinations by tax authorities for tax years before 2007.

Comparison of Financial Condition at September 30, 2010 and June 30, 2010

Total assets were $499.1 million at September 30, 2010, compared to $492.1 million at June 30, 2010. The increase is primarily due to a $12.4 million increase in cash, partially offset by a $4.1 million decrease in loans. The increase in cash is the result of an increase in deposits and in loans sold to Freddie Mac in the current quarter. The decrease in loans is a result of loans sold to Freddie Mac in the current quarter.

Total liabilities were $443.5 million at September 30, 2010, compared to $436.6 million at June 30, 2010. The increase is a result of a $7.0 million increase in deposits. The increase in deposits is attributable to an increase in municipal deposits reflecting the cyclical nature of such deposits, which are affected by the timing of receipt of tax revenues and spending for ongoing civil projects.

Total stockholders' equity was $55.7 million at September 30, 2010, compared to $55.5 million at June 30, 2010. The increase is primarily the result of an increase of $244,000 in unrealized gains on available for sale securities and net income of $271,000, partially offset by dividends paid of $351,000.

Comparison of Operating Results for the Three Months Ended September 30, 2010 and 2009

General. Net income increased $49,000 in the quarter ended September 30, 2010, compared to the prior year quarter. This increase is primarily due to a $279,000 increase in net interest income and a $309,000 increase in noninterest income, partially offset by a $97,000 increase in the provision for loan loss and a $376,000 increase in noninterest expense.

Net Interest Income. Net interest income increased $279,000, or 9.0%, to $3.4 million for the quarter ended September 30, 2010, as compared to $3.1 million for the prior year quarter. The increase is the result of an increase in total loans and a decrease in the average interest rate paid on interest bearing liabilities from 1.99% to 1.50%, partially offset by an increase in total deposits and a decrease in the average rate earned on interest earning assets from 5.10% to 4.34%. Changes in interest rates are reflective of changes in overall market rates. Increases in loans and deposits are primarily due to the acquisition of three branches from Integra Bank on June 4, 2010.

The following table summarizes changes in interest income and interest expense for the three months ended September 30, 2010 and 2009.

	Three Months Ended September 30,		
	2010	2009	% Change
	(Dollars in thousands)		
Interest income:			
Loans	$ 4,327	$ 4,161	4.0%
Investment and mortgage-backed securities	698	655	6.6
Other interest-earning assets	5	5	-
Total interest income	5,030	4,821	4.3
Interest expense:			
NOW and money market deposit accounts	284	256	10.9
Passbook accounts	64	32	100.0
Certificates of deposit	1,265	1,387	(8.8)
Total interest-bearing deposits	1,613	1,675	(3.7)
FHLB advances	22	30	(26.7)
Total interest expense	1,635	1,705	(4.1)
Net interest income	$ 3,395	$ 3,116	9.0

The following table summarizes average balances and average yields and costs of interest-earning assets and interest-bearing liabilities for the three months ended September 30, 2010 and 2009. For the purposes of this table, average balances have been calculated using month-end balances, and nonaccrual loans are included in average balances only. Yields are not presented on a tax equivalent basis.

	Three Months Ended September 30,					
	2010			2009		
	Average Balance	Interest and Dividends	Yield/ Cost	Average Balance	Interest and Dividends	Yield/ Cost
	(Dollars in thousands)					
Assets:						
Interest-earning assets:						
Loans	$ 307,300	$ 4,327	5.63%	$ 273,363	$ 4,161	6.09%
Investment and mortgage-backed securities	121,734	698	2.30	79,437	655	3.30
Other interest-earning assets	35,109	5	0.06	25,295	5	0.08
	464,143	5,030	4.34	378,095	4,821	5.10
Noninterest-earning assets	29,826			23,456		
Total assets	$ 493,969			$ 401,551		
Liabilities and stockholders' equity:						
Interest-bearing liabilities:						
NOW and money market deposit accounts (1)	$ 157,004	$ 284	0.72	$ 127,867	$ 256	0.80
Passbook accounts (1)	55,989	64	0.46	40,569	32	0.32
Certificates of deposit (1)	218,991	1,265	2.31	170,780	1,387	3.25
Total interest-bearing deposits	431,984	1,613	1.49	339,216	1,675	1.98
FHLB advances	2,708	22	3.25	3,708	30	3.24
Total interest-bearing liabilities	434,692	1,635	1.50	342,924	1,705	1.99
Noninterest-bearing liabilities	3,886			3,433		
Total liabilities	438,578			346,357		
Stockholders' equity	55,391			55,194		
Total liabilities and stockholders' equity	$ 493,969			$ 401,551		
Net interest income		$ 3,395			$ 3,116	
Interest rate spread			2.84%			3.11%
Net interest margin (annualized)			2.93%			3.30%
Average interest-earning assets to average interest-bearing liabilities			106.78%			110.26%

(1) Includes municipal deposits

Provision for Loan Losses. The following table summarizes the activity in the allowance for loan losses and provision for loan losses for the three months ended September 30, 2010 and 2009.

	Three Months Ended September 30, 2010	2009
	(Dollars in thousands)	
Allowance at beginning of period	$ 5,681	$ 4,213
Provision for loan losses	719	622
Charge offs:		
One- to four-family residential real estate	155	-
Nonresidential real estate and land	-	-
Multifamily residential real estate	-	831
Consumer and other loans	66	17
Total charge-offs	221	848
Recoveries:		
One- to four-family residential real estate	10	2
Nonresidential real estate and land	-	-
Multifamily residential real estate	-	5
Consumer and other loans	5	4
Total recoveries	15	11
Net charge-offs	206	837
Allowance at end of period	$ 6,194	$ 3,998

The provision for loan losses was $719,000 for the quarter ended September 30, 2010, compared to $622,000 for the same quarter in the prior year. On an ongoing basis, management evaluates the Bank's allowance for loan loss for adequacy. As part of this evaluation, management considers the amounts and types of loans, concentrations, the value of underlying collateral, current economic conditions, and other relevant information, such as the size of the overall portfolio. Based upon this evaluation, management calculates the provision for loan loss in the current period. The increase in the current year quarter is primarily attributable to an increase in nonperforming loans. Nonperforming loans increased from $10.6 million at June 30, 2010 to $18.7 million at September 30, 2010, compared to a decrease in nonperforming loans from $6.0 million at June 30, 2009 to $4.0 million at September 30, 2009. For further discussion of nonperforming loans see analysis on the following table.

For more information on how the Company reviews its allowance for loan losses and determines any necessary provision see, "Critical Accounting Policies – Allowance for Loan Losses."

The following table provides information with respect to our nonperforming assets at the dates indicated. We did not have any accruing loans past due 90 days or more at the dates presented.

	At September 30, 2010	At June 30, 2010	% Change
	(Dollars in thousands)		
Nonaccrual loans:			
Residential real estate:			
One- to-four-family	$ 3,115	$ 2,436	27.9%
Multi-family	8,219	5,245	56.7
Nonresidential real estate and land	6,763	2,738	147.0
Consumer and other loans	599	155	286.5
Total	18,696	10,574	76.8
Real estate owned	297	297	-
Total nonperforming assets	$ 18,993	$ 10,871	74.7
Total nonperforming loans to total loans	6.11%	3.42%	78.7
Total nonperforming loans to total assets	3.74%	2.15%	74.0
Total nonperforming assets to total assets	3.80%	2.21%	71.9

Nonperforming loans increased from $10.6 million at June 30, 2010 to $18.7 million at September 30, 2010, compared to a decrease in nonperforming loans from $6.0 million at June 30, 2009 to $4.0 million at September 30, 2009. The increase in the current year is due to the addition of one $3.0 million multifamily real estate loan, ten one- to four- family mortgage loans totaling $798,000, and three commercial real estate loans, totaling $4.1 million. The three commercial real estate loans are classified as troubled debt restructuring. It is Bank policy to include, as nonaccrual loans, TDRs until a payment history of six months has been established. Once a sufficient payment history is established, the loan classified as a TDR is no longer included in nonaccrual loans. For further information on TDRs, see Note 7 to the Unaudited Consolidated Financial Statements above. Management believes there are adequate allowances and collateral securing these loans to cover losses that may result from these nonperforming loans.

Noninterest Income. The following table summarizes other income for the three months ended September 30, 2010 and 2009.

	Three Months Ended September 30, 2010	Three Months Ended September 30, 2009	% Change
	(Dollars in thousands)		
Service charges	$ 601	$ 482	24.7%
Gain on sale of loans	227	86	164.0
Gain (loss) on sale of investments	44	(12)	466.7
Gain on sale of other real estate owned	2	-	100.0
Income from bank-owned life insurance	69	57	21.1
Other	52	73	(29.7)
Total	$ 995	$ 686	45.0

The increase in service charges is primarily due to an overall increase in deposits. The increase in gain on sale of loans is due to an increase in loans sold to Freddie Mac in the current quarter.

Noninterest Expense. The following table summarizes other expense for the three months ended September 30, 2010 and 2009.

	Three Months Ended September 30, 2010	Three Months Ended September 30, 2009	% Change
	(Dollars in thousands)		
Compensation and employee benefits	$ 1,671	$ 1,471	13.6%
Premises and occupancy expense	309	276	12.0
Deposit insurance premium	228	220	3.6
Advertising expense	101	91	11.0
Data processing expense	84	56	50.0
ATM service fees	138	107	29.0
Provision for loss on sale of other real estate owned	-	100	(100.0)
Acquisition related expenses	38	-	100.0
Other operating expenses	682	554	23.1
Total	$ 3,251	$ 2,875	13.1

Noninterest expense increased $376,000, or 13.1%, to $3.3 million for the quarter ended September 30, 2010, from $2.9 million in the prior year quarter. The increase is primarily the result of higher employee compensation expenses and intangible asset amortization in the current year quarter, partially offset by the absence of a provision for loss on the sale of real estate owned in the current year period compared to a $100,000 provision in the prior year quarter. The increases in employee compensation expenses and intangible asset amortization are due to the Integra branch acquisition.

Income Taxes. The provision for income taxes was $149,000 for the quarter ended September 30, 2010 compared to $83,000 for the same period in 2009. The increase in provision for income taxes is primarily the result of a 115,000 increase in income before income taxes.

Liquidity Management. Liquidity is the ability to meet current and future financial obligations of a short-term nature. Our primary sources of funds consist of deposit inflows, loan repayments, maturities and sales of securities and borrowings from the Federal Home Loan Bank of Indianapolis. While maturities and scheduled amortization of loans and securities are predictable sources of funds, deposit flows and loan prepayments are greatly influenced by general interest rates, economic conditions and competition.

We regularly adjust our investments in liquid assets based upon our assessment of: (1) expected loan demands; (2) expected deposit flows, in particular municipal deposit flows; (3) yields available on interest-earning deposits and securities; and (4) the objectives of our asset/liability management policy.

Our most liquid assets are cash and cash equivalents. The levels of these assets depend on our operating, financing, lending and investing activities during any given period. Cash and cash equivalents totaled $44.4 million at September 30, 2010 and $32.0 million at June 30, 2010. Securities classified as available-for-sale whose market value exceeds our cost, which provide additional sources of liquidity, totaled $97.1 million at September 30, 2010 and $104.1 million at June 30, 2010. Total securities classified as available-for-sale were $118.8 million at September 30, 2010 and $119.3 million at June 30, 2010. In addition, at September 30, 2010 and June 30, 2010, we had the ability to borrow a total of approximately $72.5 million and $83.0 million, respectively, from the Federal Home Loan Bank of Indianapolis.

At September 30, 2010, we had $31.3 million in loan commitments outstanding, consisting of $3.5 million in mortgage loan commitments, $1.8 million in commercial loan commitments, $20.1 million in unused home equity lines of credit, $5.9 million in commercial lines of credit, and $743,000 in letters of credit outstanding. At June 30, 2010, we had $38.7 million in loan commitments outstanding, consisting of $1.1 million in mortgage loan commitments, $4.3 million in commercial loan commitments, $26.6 million in unused home equity lines of credit, $5.8 million in commercial lines of credit, and $856,000 in letters of credit outstanding. Certificates of deposit due within one year of September 30, 2010 totaled $149.4 million. This represented 67.6% of certificates of deposit at September 30, 2010. We believe the large percentage of certificates of deposit that mature within one year reflects customers' hesitancy to invest their funds for long periods in the current low interest rate environment. If these maturing deposits do not remain with us, we will be required to seek other sources of funds, including other certificates of deposit and borrowings. Depending on market conditions, we may be required to pay higher rates on such deposits or other borrowings than we currently pay on the certificates of deposit due on or before September 30, 2010. We believe, however, based on past experience that a significant portion of our certificates of deposit will remain with us. We have the ability to attract and retain deposits by adjusting the interest rates offered.

Our primary investing activities are the origination and purchase of loans and the purchase of securities. Our primary financing activities consist of activity in deposit accounts and Federal Home Loan Bank advances. Deposit flows are affected by the overall level of interest rates, the interest rates and products offered by us and our local competitors and other factors. We generally manage the pricing of our deposits to be competitive and to increase core deposit relationships. Occasionally, we offer promotional rates on certain deposit products to attract deposits.

Capital Management. The Bank is subject to various regulatory capital requirements administered by the Office of Thrift Supervision, including a risk-based capital measure. The risk-based capital guidelines include both a definition of capital and a framework for calculating risk-weighted assets by assigning balance sheet assets and off-balance sheet items to broad risk categories. At September 30, 2010, the Bank exceeded all of its regulatory capital requirements to be considered "well capitalized" under the FDIC's regulatory framework for prompt corrective action at that date.

The following table summarizes the Bank's capital amounts and the ratios required at September 30, 2010:

	Actual		For capital adequacy purposes		To be well capitalized under prompt corrective action provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
			(in thousands)			
September 30, 2010 (unaudited)						
Tier 1 capital to risk-weighted assets	$ 45,815	15.40%	$ 11,891	4.0%	$ 17,836	6.0%
Total capital to risk-weighted assets	48,968	16.46%	23,782	8.0%	29,727	10.0%
Tier 1 capital to adjusted total assets	45,815	9.31%	19,682	4.0%	24,603	5.0%
Tangible capital to adjusted total assets	45,815	9.31%	7,381	1.5%		

Off-Balance Sheet Arrangements. In the normal course of operations, we engage in a variety of financial transactions that, in accordance with U.S. generally accepted accounting principles, are not recorded in our financial statements.

These transactions involve, to varying degrees, elements of credit, interest rate and liquidity risk. Such transactions are used primarily to manage customers’ requests for funding and take the form of loan commitments, letters of credit and lines of credit. For information about our loan commitments and unused lines of credit, see note 15 of the notes to the consolidated financial statements included in our Annual Report on Form 10-K for the year ended June 30, 2010, as filed with the SEC. We currently have no plans to engage in hedging activities in the future.

For the three months ended September 30, 2010, we engaged in no off-balance sheet transactions reasonably likely to have a material effect on our financial condition, results of operations or cash flows.

Item 3. Quantitative and Qualitative Disclosures about Market Risk.

For a discussion of the Company's asset and liability management policies as well as the potential impact of interest rate changes upon the market value of the Company's portfolio equity, see "Management's Discussion and Analysis of Financial Condition and Results of Operations" in the Company's Annual Report on Form 10-K, filed with the Securities and Exchange Commission on September 28, 2010. The main components of market risk for the Company are interest rate risk and liquidity risk. The Company manages interest rate risk and liquidity risk by establishing and monitoring the volume, maturities, pricing and mix of assets and funding sources with the objective of managing assets and funding sources to provide results that are consistent with liquidity, growth, risk limits and profitability goals. Model simulation is used to measure earnings volatility under both rising and falling rate scenarios.

We use a net portfolio value analysis prepared by the Office of Thrift Supervision to review our level of interest rate risk. This analysis measures interest rate risk by computing changes in net portfolio value of our cash flows from assets, liabilities and off-balance sheet items in the event of a range of assumed changes in market interest rates. Net portfolio value represents the market value of portfolio equity and is equal to the market value of assets minus the market value of liabilities, with adjustments made for off-balance sheet items. This analysis assesses the risk of loss in market risk-sensitive instruments in the event of a sudden and sustained 50 to 300 basis point increase or 50 and 100 basis point decrease in market interest rates with no effect given to any steps that we might take to counter the effect of that interest rate movement. Because of the low level of market interest rates, this analysis is not performed for decreases of more than 200 basis points.

The following table, which is based on information that we provide to the Office of Thrift Supervision (OTS), presents the change in our net portfolio value at June 30, 2010, which is the most recent date for which data is available, that would occur in the event of an immediate change in interest rates based on Office of Thrift Supervision assumptions, with no effect given to any steps that we might take to counteract that change.

	Net Portfolio Value (Dollars in thousands)			Net Portfolio Value as % of Portfolio Value of Assets	
Basic Point ("bp") Change in Rates	Amount	Change	% Change	NPV Ratio	Change (bp)
300	$ 59,161	$ (1,993)	(3)%	11.86%	(22)bps
200	61,564	409	1%	12.25	16
100	61,698	543	1%	12.23	15
50	61,471	316	1%	12.17	8
0	61,155	-	-	12.08	-
(50)	60,045	(1,110)	(2)%	11.86	(22)
(100)	60,996	(159)	1%	12.01	(7)

The OTS uses various assumptions in assessing interest rate risk. These assumptions relate to interest rates, loan prepayment rates, deposit decay rates and the market values of certain assets under differing interest rate scenarios, among others. As with any method of measuring interest rate risk, certain shortcomings are inherent in the methods of analyses presented in the foregoing tables. For example, although certain assets and liabilities may have similar maturities or periods to repricing, they may react in different degrees to changes in market interest rates. Also, the interest rates on certain types of assets and liabilities may fluctuate in advance of changes in market interest rates, while interest rates on other types may lag behind changes in market rates. Additionally, certain assets, such as adjustable-rate mortgage loans, have features that restrict changes in interest rates on a short-term basis and over the life of the asset. Further, in the event of a change in interest rates, expected rates of prepayments on loans and early withdrawals from certificates could deviate significantly from those assumed in calculating the table. Prepayment rates can have a significant impact on interest income. Because of the large percentage of loans and mortgage-backed securities we hold, rising or falling interest rates have a significant impact on the prepayment speeds of our earning assets that in turn affect the rate sensitivity position. When interest rates rise, prepayments tend to slow. When interest rates fall, prepayments tend to rise. Our asset sensitivity would be reduced if prepayments slow and vice versa. While we believe these assumptions to be reasonable, there can be no assurance that assumed prepayment rates will approximate actual future mortgage-backed security and loan repayment activity.

Item 4. Controls and Procedures.

The Company's management, including the Company's principal executive officer and principal financial officer, have evaluated the effectiveness of the Company's "disclosure controls and procedures," as such term is defined in Rule 13a-15(e) promulgated under the Securities Exchange Act of 1934, as amended, (the "Exchange Act"). Based upon their evaluation, the principal executive officer and principal financial officer concluded that, as of the end of the period covered by this report, the Company's disclosure controls and procedures were effective for the purpose of ensuring that the information required to be disclosed in the reports that the Company files or submits under the Exchange Act with the Securities and Exchange Commission (the "SEC") (1) is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and (2) is accumulated and communicated to the Company's management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure. During the quarterly period ended September 30, 2010, there were no changes in the Company's internal control over financial reporting which materially affected, or are reasonably likely to materially affect, the Company's internal controls over financial reporting.

PART II OTHER INFORMATION

Item 1. LEGAL PROCEEDINGS

Periodically, there have been various claims and lawsuits against us, such as claims to enforce liens and contracts, condemnation proceedings on properties in which we hold security interests, claims involving the making and servicing of real property loans and other issues incident to our business. We are not party to any pending legal proceedings that we believe would have a material adverse effect on our financial condition, results of operations or cash flows.

Item 1A. RISK FACTORS

In addition to the other information set forth in this report, you should carefully consider the factors discussed in Part I, “Item 1A. Risk Factors” in our Annual Report on Form 10-K for the year ended June 30, 2010, which could materially affect our business, financial condition or future results. The risks described in our Annual Report on Form 10-K are not the only risks that we face. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially affect our business, financial condition and/or operating results.

Item 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

There were no repurchases of the Company’s common stock during the quarter ended September 30, 2010.

Item 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable

Item 4. [REMOVED AND RESERVED]

Item 5. OTHER INFORMATION

Not applicable

Item 6. EXHIBITS

Exhibit 31.1	Certification of Chief Executive Officer
Exhibit 31.2	Certification of Chief Financial Officer
Exhibit 32	Section 1305 Certifications

SIGNATURES

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

			UNITED COMMUNITY BANCORP
Date:	November 15, 2010	By:	/s/ William F. Ritzmann William F. Ritzmann President and Chief Executive Officer
Date:	November 15, 2010	By:	/s/ Vicki A. March Vicki A. March Senior Vice President, Chief Financial Officer and Treasurer

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