
**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 December 31, 2019
or**

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

**For transition period from to
Commission File Number 001-33390**

TFS FINANCIAL CORPORATION
(Exact Name of Registrant as Specified in its Charter)

United States of America
(State or Other Jurisdiction of
Incorporation or Organization)

52-2054948
(I.R.S. Employer
Identification No.)

7007 Broadway Avenue
Cleveland, Ohio
(Address of Principal Executive Offices)

44105
(Zip Code)

(216) 441-6000

Registrant's telephone number, including area code:

Not Applicable

(Former name, former address and former fiscal year, if changed since last report)

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

<u>Title of each class</u>	<u>Trading Symbol(s)</u>	<u>Name of each exchange in which registered</u>
Common Stock, par value \$0.01 per share	TFSL	The NASDAQ Stock Market, LLC

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes No

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

Large accelerated filer	<input checked="" type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/>	Smaller Reporting Company	<input type="checkbox"/>
Emerging Growth Company	<input type="checkbox"/>		

If an emerging company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

As of February 4, 2020, there were 280,129,198 shares of the Registrant's common stock, par value \$0.01 per share, outstanding, of which 227,119,132 shares, or 81.1% of the Registrant's common stock, were held by Third Federal Savings and Loan Association of Cleveland, MHC, the Registrant's mutual holding company.

TFS Financial Corporation

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GLOSSARY OF TERMS

TFS Financial Corporation provides the following list of acronyms and defined terms as a tool for the reader. The acronyms and defined terms identified below are used throughout the document.

ACT: Tax Cuts and Jobs Act	FICO: Financing Corporation
AOI: Accumulated Other Comprehensive Income	FRB-Cleveland: Federal Reserve Bank of Cleveland
ARM: Adjustable Rate Mortgage	Freddie Mac: Federal Home Loan Mortgage Corporation
ASC: Accounting Standards Codification	FRS: Board of Governors of the Federal Reserve System
ASU: Accounting Standards Update	GAAP: Generally Accepted Accounting Principles
Association: Third Federal Savings and Loan Association of Cleveland	Ginnie Mae: Government National Mortgage Association
BOLI: Bank Owned Life Insurance	GVA: General Valuation Allowances
CDs: Certificates of Deposit	HPI: Home Price Index
CFPB: Consumer Financial Protection Bureau	IRR: Interest Rate Risk
CLTV: Combined Loan-to-Value	IRS: Internal Revenue Service
Company: TFS Financial Corporation and its subsidiaries	IVA: Individual Valuation Allowance
DFA: Dodd-Frank Wall Street Reform and Consumer Protection Act	LIHTC: Low Income Housing Tax Credit
EaR: Earnings at Risk	LIP: Loans-in-Process
EPS: Earnings per Share	LTV: Loan-to-Value
ESOP: Third Federal Employee (Associate) Stock Ownership Plan	MGIC: Mortgage Guaranty Insurance Corporation
EVE: Economic Value of Equity	OCC: Office of the Comptroller of the Currency
Fannie Mae: Federal National Mortgage Association	OCI: Other Comprehensive Income
FASB: Financial Accounting Standards Board	PMI: Private Mortgage Insurance
FDIC: Federal Deposit Insurance Corporation	PMIC: PMI Mortgage Insurance Co.
FHFA: Federal Housing Finance Agency	REMICs: Real Estate Mortgage Investment Conduits
FHLB: Federal Home Loan Bank	SEC: United States Securities and Exchange Commission
	TDR: Troubled Debt Restructuring
	Third Federal Savings, MHC: Third Federal Savings and Loan Association of Cleveland, MHC

Item 1. Financial Statements
**TFS FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CONDITION (unaudited)
(In thousands, except share data)**

	December 31, 2019	September 30, 2019
ASSETS		
Cash and due from banks	\$ 25,935	\$ 31,728
Other interest-earning cash equivalents	255,291	243,415
Cash and cash equivalents	281,226	275,143
Investment securities available for sale (amortized cost \$553,039 and \$550,605, respectively)	553,997	547,864
Mortgage loans held for sale, at lower of cost or market (none measured at fair value)	9,608	3,666
Loans held for investment, net:		
Mortgage loans	13,458,379	13,189,516
Other loans	2,900	3,166
Deferred loan expenses, net	43,785	41,976
Allowance for loan losses	(37,292)	(38,913)
Loans, net	13,467,772	13,195,745
Mortgage loan servicing rights, net	7,142	8,080
Federal Home Loan Bank stock, at cost	101,858	101,858
Real estate owned, net	2,813	2,163
Premises, equipment, and software, net	43,092	61,577
Accrued interest receivable	40,222	40,822
Bank owned life insurance contracts	219,041	217,481
Other assets	79,420	87,957
TOTAL ASSETS	\$ 14,806,191	\$ 14,542,356
LIABILITIES AND SHAREHOLDERS' EQUITY		
Deposits	\$ 9,000,920	\$ 8,766,384
Borrowed funds	3,889,649	3,902,981
Borrowers' advances for insurance and taxes	99,391	103,328
Principal, interest, and related escrow owed on loans serviced	31,503	32,909
Accrued expenses and other liabilities	55,779	40,000
Total liabilities	13,077,242	12,845,602
Commitments and contingent liabilities		
Preferred stock, \$0.01 par value, 100,000,000 shares authorized, none issued and outstanding	—	—
Common stock, \$0.01 par value, 700,000,000 shares authorized; 332,318,750 shares issued; 280,127,221 and 279,962,777 outstanding at December 31, 2019 and September 30, 2019, respectively	3,323	3,323
Paid-in capital	1,736,322	1,734,154
Treasury stock, at cost; 52,191,529 and 52,355,973 shares at December 31, 2019 and September 30, 2019, respectively	(766,492)	(764,589)
Unallocated ESOP shares	(43,334)	(44,417)
Retained earnings—substantially restricted	849,929	837,662
Accumulated other comprehensive income (loss)	(50,799)	(69,379)
Total shareholders' equity	1,728,949	1,696,754
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	\$ 14,806,191	\$ 14,542,356

See accompanying notes to unaudited interim consolidated financial statements.

TFS FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME (unaudited)
(In thousands, except share and per share data)

	For the Three Months Ended	
	December 31,	
	2019	2018
INTEREST AND DIVIDEND INCOME:		
Loans, including fees	\$ 115,225	\$ 112,491
Investment securities available for sale	2,864	3,124
Other interest and dividend earning assets	1,963	2,673
Total interest and dividend income	<u>120,052</u>	<u>118,288</u>
INTEREST EXPENSE:		
Deposits	38,316	32,762
Borrowed funds	17,551	17,714
Total interest expense	<u>55,867</u>	<u>50,476</u>
NET INTEREST INCOME	64,185	67,812
PROVISION (CREDIT) FOR LOAN LOSSES	(3,000)	(2,000)
NET INTEREST INCOME AFTER PROVISION (CREDIT) FOR LOAN LOSSES	<u>67,185</u>	<u>69,812</u>
NON-INTEREST INCOME:		
Fees and service charges, net of amortization	2,146	1,776
Net gain on the sale of loans	2,925	111
Increase in and death benefits from bank owned life insurance contracts	1,561	1,547
Other	5,298	1,242
Total non-interest income	<u>11,930</u>	<u>4,676</u>
NON-INTEREST EXPENSE:		
Salaries and employee benefits	25,885	25,364
Marketing services	4,461	4,797
Office property, equipment and software	6,446	6,986
Federal insurance premium and assessments	2,619	2,766
State franchise tax	1,132	1,262
Other expenses	6,777	6,805
Total non-interest expense	<u>47,320</u>	<u>47,980</u>
INCOME BEFORE INCOME TAXES	31,795	26,508
INCOME TAX EXPENSE	6,153	6,175
NET INCOME	<u>\$ 25,642</u>	<u>\$ 20,333</u>
Earnings per share—basic and diluted	<u>\$ 0.09</u>	<u>\$ 0.07</u>
Weighted average shares outstanding		
Basic	275,578,184	275,376,254
Diluted	<u>277,888,588</u>	<u>277,073,317</u>

See accompanying notes to unaudited interim consolidated financial statements.

TFS FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS) (unaudited)
(In thousands)

	For the Three Months Ended	
	December 31,	
	2019	2018
Net income	\$ 25,642	\$ 20,333
Other comprehensive income (loss), net of tax:		
Net change in unrealized gain (losses) on securities available for sale	2,923	5,097
Net change in cash flow hedges	15,205	(26,822)
Net change in defined benefit plan obligation	452	264
Total other comprehensive income (loss)	18,580	(21,461)
Total comprehensive income (loss)	\$ 44,222	\$ (1,128)

See accompanying notes to unaudited interim consolidated financial statements.

TFS FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY (unaudited)
(In thousands, except share and per share data)

	For the Three Months Ended December 31, 2018						
	Common stock	Paid-in capital	Treasury stock	Unallocated common stock held by ESOP	Retained earnings	Accumulated other comprehensive income (loss)	Total shareholders' equity
Balance at September 30, 2018	\$ 3,323	\$ 1,726,992	\$ (754,272)	\$ (48,751)	\$ 807,890	\$ 23,222	\$ 1,758,404
Net income	—	—	—	—	20,333	—	20,333
Other comprehensive income (loss), net of tax	—	—	—	—	—	(21,461)	(21,461)
ESOP shares allocated or committed to be released	—	581	—	1,084	—	—	1,665
Compensation costs for equity incentive plans	—	1,081	—	—	—	—	1,081
Purchase of treasury stock (242,500 shares)	—	—	(3,776)	—	—	—	(3,776)
Treasury stock allocated to equity incentive plan	—	(745)	584	—	—	—	(161)
Dividends paid to common shareholders (\$0.25 per common share)	—	—	—	—	(12,305)	—	(12,305)
Balance at December 31, 2018	<u>\$ 3,323</u>	<u>\$ 1,727,909</u>	<u>\$ (757,464)</u>	<u>\$ (47,667)</u>	<u>\$ 815,918</u>	<u>\$ 1,761</u>	<u>\$ 1,743,780</u>

	For the Three Months Ended December 31, 2019						
	Common stock	Paid-in capital	Treasury stock	Unallocated common stock held by ESOP	Retained earnings	Accumulated other comprehensive income (loss)	Total shareholders' equity
Balance at September 30, 2019	\$ 3,323	\$ 1,734,154	\$ (764,589)	\$ (44,417)	\$ 837,662	\$ (69,379)	\$ 1,696,754
Net income	—	—	—	—	25,642	—	25,642
Other comprehensive income (loss), net of tax	—	—	—	—	—	18,580	18,580
ESOP shares allocated or committed to be released	—	1,011	—	1,083	—	—	2,094
Compensation costs for equity incentive plans	—	1,189	—	—	—	—	1,189
Purchase of treasury stock (19,500 shares)	—	—	(359)	—	—	—	(359)
Treasury stock allocated to equity incentive plan	—	(32)	(1,544)	—	—	—	(1,576)
Dividends paid to common shareholders (\$0.27 per common share)	—	—	—	—	(13,375)	—	(13,375)
Balance at December 31, 2019	<u>\$ 3,323</u>	<u>\$ 1,736,322</u>	<u>\$ (766,492)</u>	<u>\$ (43,334)</u>	<u>\$ 849,929</u>	<u>\$ (50,799)</u>	<u>\$ 1,728,949</u>

See accompanying notes to unaudited interim consolidated financial statements.

TFS FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS (unaudited) (In thousands)

	For the Three Months Ended December 31,	
	2019	2018
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	\$ 25,642	\$ 20,333
Adjustments to reconcile net income to net cash provided by operating activities:		
ESOP and stock-based compensation expense	3,283	2,746
Depreciation and amortization	7,794	5,406
Deferred income taxes	(64)	434
Provision (credit) for loan losses	(3,000)	(2,000)
Net gain on the sale of loans	(2,925)	(111)
Net gain on sale of commercial property	(4,257)	—
Other net losses	(13)	(293)
Proceeds from sales of loans held for sale	9,753	7,068
Loans originated for sale	(15,606)	(7,287)
Increase in bank owned life insurance contracts	(1,577)	(1,551)
Net (increase) decrease in interest receivable and other assets	(5,705)	6,097
Net increase in accrued expenses and other liabilities	16,066	3,582
Net cash provided by operating activities	<u>29,391</u>	<u>34,424</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Loans originated	(1,055,571)	(647,400)
Principal repayments on loans	583,081	583,980
Proceeds from principal repayments and maturities of:		
Securities available for sale	52,574	31,998
Proceeds from sale of:		
Loans	200,923	13,393
Real estate owned	635	1,423
Premises, Equipment and Other Assets	23,512	—
Purchases of:		
FHLB stock	—	—
Securities available for sale	(56,377)	(59,052)
Premises and equipment	(537)	(917)
Other	16	(310)
Net cash used in investing activities	<u>(251,744)</u>	<u>(76,885)</u>
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net increase in deposits	234,536	105,596
Net decrease in borrowers' advances for insurance and taxes	(3,937)	(6,554)
Net decrease in principal and interest owed on loans serviced	(1,406)	(913)
Net increase(decrease) in short-term borrowed funds	(51,093)	110,031
Proceeds from long-term borrowed funds	150,000	—
Repayment of long-term borrowed funds	(112,239)	(97,401)
Cash collateral/settlements received from (provided to) derivative counterparties (1)	27,921	(35,319)
Purchase of treasury shares	(395)	(3,669)
Acquisition of treasury shares through net settlement of stock benefit plans compensation	(1,576)	(161)
Dividends paid to common shareholders	(13,375)	(12,305)
Net cash provided by financing activities	<u>228,436</u>	<u>59,305</u>
NET INCREASE IN CASH AND CASH EQUIVALENTS	6,083	16,844
CASH AND CASH EQUIVALENTS—Beginning of period	275,143	269,775
CASH AND CASH EQUIVALENTS—End of period	\$ 281,226	\$ 286,619
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Cash paid for interest on deposits	\$ 37,729	\$ 32,368
Cash paid for interest on borrowed funds	19,485	16,450
Cash paid for income taxes	21	42
SUPPLEMENTAL SCHEDULES OF NONCASH INVESTING AND FINANCING ACTIVITIES:		
Transfer of loans to real estate owned	1,277	1,295
Transfer of loans from held for investment to held for sale	198,694	13,382
Treasury stock issued for stock benefit plans	<u>32</u>	<u>746</u>

(1) For the three months ended December 31, 2018, \$35,319 of cash collateral and settlement payments received from derivative counterparties were reclassified from Operating to Financing Activities to conform to ASC 230-10-45-27, which allows cash flows from derivative instruments to be classified in the same category as items hedged.

See accompanying notes to unaudited interim consolidated financial statements.

TFS FINANCIAL CORPORATION AND SUBSIDIARIES

NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands unless otherwise indicated)

1. BASIS OF PRESENTATION

TFS Financial Corporation, a federally chartered stock holding company, conducts its principal activities through its wholly owned subsidiaries. The principal line of business of the Company is retail consumer banking, including mortgage lending, deposit gathering, and, to a much lesser extent, other financial services. As of December 31, 2019, approximately 81% of the Company's outstanding shares were owned by a federally chartered mutual holding company, Third Federal Savings and Loan Association of Cleveland, MHC. The thrift subsidiary of TFS Financial Corporation is Third Federal Savings and Loan Association of Cleveland.

Third Capital, Inc., an operating subsidiary of the Company, was formed to hold non-thrift investments and subsidiaries, which includes a partial ownership of a limited liability company that acquires and manages commercial real estate. On October 31, 2019, the limited liability company sold the remaining two commercial office buildings it owned, which had a net book value of \$19,324 at September 30, 2019 included in premises, equipment and software, net and other assets. A \$4,257 net gain on the sale of those properties was recorded for the quarter ended December 31, 2019, representing the Company's share of the gain on sale. Pending the outcome of various sale escrow reserves, which will not be resolved until later this year, the Company may record additional residual income in 2020.

The accounting and reporting policies followed by the Company conform in all material respects to U.S. GAAP and to general practices in the financial services industry. The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements. Actual results could differ from those estimates. The allowance for loan losses, the valuation of deferred tax assets, and the determination of pension obligations are particularly subject to change.

The unaudited interim consolidated financial statements reflect all adjustments of a normal recurring nature which, in the opinion of management, are necessary to present fairly the consolidated financial condition of the Company at December 31, 2019, and its results of operations and cash flows for the periods presented. Such adjustments are the only adjustments reflected in the unaudited interim financial statements.

In accordance with SEC Regulation S-X for interim financial information, these statements do not include certain information and footnote disclosures required for complete audited financial statements. The Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2019 contains audited consolidated financial statements and related notes, which should be read in conjunction with the accompanying interim consolidated financial statements. The results of operations for the interim periods disclosed herein are not necessarily indicative of the results that may be expected for the fiscal year ending September 30, 2020 or for any other period.

Effective October 1, 2018, the Company adopted ASU 2014-09, Revenue from Contracts with Customers (Topic 606) and all subsequent amendments related to the ASU (collectively, "Topic 606"). The core principle of the guidance requires an entity to recognize revenue to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled to receive in exchange for those goods or services. The adoption did not have a significant impact to the Company's consolidated financial statements, as such, a cumulative effect adjustment to the opening balance of retained earnings at adoption was not necessary. Neither the new standard, nor any of the related amendments, resulted in a material change from our current accounting for revenue because a significant amount of the Company's revenue streams such as interest income, are not within the scope of Topic 606. Two of the Company's revenue streams within scope of Topic 606 are the sales of REO and deposit account and other transaction-based service fee income. Both streams are immaterial and therefore quantitative information regarding these streams were not disclosed.

2. EARNINGS PER SHARE

Basic earnings per share is the amount of earnings available to each share of common stock outstanding during the reporting period. Diluted earnings per share is the amount of earnings available to each share of common stock outstanding during the reporting period adjusted to include the effect of potentially dilutive common shares. For purposes of computing basic earnings per share, outstanding shares include shares held by the public, shares held by the ESOP that have been allocated to participants or committed to be released for allocation to participants, and the 227,119,132 shares held by Third Federal Savings, MHC. For purposes of computing dilutive earnings per share, stock options and restricted and performance stock units

with a dilutive impact are added to the outstanding shares used in the basic earnings per share calculation. Unvested shares awarded pursuant to the Company's restricted stock plans are treated as participating securities in the computation of EPS pursuant to the two-class method as they contain nonforfeitable rights to dividends. The two-class method is an earnings allocation that determines EPS for each class of common stock and participating security. Performance stock units, determined to be contingently issuable and not participating securities, are excluded from the calculation of basic EPS. At December 31, 2019 and 2018, respectively, the ESOP held 4,333,396 and 4,766,736 shares, respectively, that were neither allocated to participants nor committed to be released to participants.

The following is a summary of the Company's earnings per share calculations.

	For the Three Months Ended December 31,					
	2019			2018		
	Income	Shares	Per share amount	Income	Shares	Per share amount
	(Dollars in thousands, except per share data)					
Net income	\$ 25,642			\$ 20,333		
Less: income allocated to restricted stock units	417			372		
Basic earnings per share:						
Income available to common shareholders	\$ 25,225	275,578,184	\$ 0.09	\$ 19,961	275,376,254	\$ 0.07
Diluted earnings per share:						
Effect of dilutive potential common shares	2,310,404			1,697,063		
Income available to common shareholders	\$ 25,225	277,888,588	\$ 0.09	\$ 19,961	277,073,317	\$ 0.07

The following is a summary of outstanding stock options and restricted and performance stock units that are excluded from the computation of diluted earnings per share because their inclusion would be anti-dilutive.

	For the Three Months Ended December 31,	
	2019	2018
Options to purchase shares	293,200	1,885,600
Restricted and performance stock units	136,945	131,500

3. INVESTMENT SECURITIES

Investments available for sale are summarized as follows:

	December 31, 2019			
	Amortized Cost	Gross Unrealized		Fair Value
		Gains	Losses	
REMICs	\$ 546,612	\$ 2,342	\$ (1,612)	\$ 547,342
Fannie Mae certificates	6,427	228	—	6,655
Total	\$ 553,039	\$ 2,570	\$ (1,612)	\$ 553,997

	September 30, 2019			
	Amortized Cost	Gross Unrealized		Fair Value
		Gains	Losses	
REMICs	\$ 544,042	\$ 1,384	\$ (4,384)	\$ 541,042
Fannie Mae certificates	6,563	259	—	6,822
Total	\$ 550,605	\$ 1,643	\$ (4,384)	\$ 547,864

Gross unrealized losses on available for sale securities and the estimated fair value of the related securities, aggregated by the length of time the securities have been in a continuous loss position, at December 31, 2019 and September 30, 2019, were as follows:

	December 31, 2019					
	Less Than 12 Months		12 Months or More		Total	
	Estimated Fair Value	Unrealized Loss	Estimated Fair Value	Unrealized Loss	Estimated Fair Value	Unrealized Loss
Available for sale—						
REMICs	\$ 65,097	\$ 240	\$ 210,075	\$ 1,372	\$ 275,172	\$ 1,612

	September 30, 2019					
	Less Than 12 Months		12 Months or More		Total	
	Estimated Fair Value	Unrealized Loss	Estimated Fair Value	Unrealized Loss	Estimated Fair Value	Unrealized Loss
Available for sale—						
REMICs	\$ 95,751	\$ 488	\$ 292,643	\$ 3,896	\$ 388,394	\$ 4,384

We believe the unrealized losses on investment securities were attributable to interest rate increases. The contractual terms of U.S. government and agency obligations do not permit the issuer to settle the security at a price less than the par value of the investment. The contractual cash flows of mortgage-backed securities are guaranteed by Fannie Mae, Freddie Mac and Ginnie Mae. REMICs are issued by or backed by securities issued by these governmental agencies. It is expected that the securities would not be settled at a price substantially less than the amortized cost of the investment. The U.S. Treasury Department established financing agreements in 2008 to ensure Fannie Mae and Freddie Mac meet their obligations to holders of mortgage-backed securities that they have issued or guaranteed.

Since the decline in value is attributable to changes in interest rates and not credit quality and because the Company has neither the intent to sell the securities nor is it more likely than not the Company will be required to sell the securities for the time periods necessary to recover the amortized cost, these investments are not considered other-than-temporarily impaired.

4. LOANS AND ALLOWANCE FOR LOAN LOSSES

Loans held for investment consist of the following:

	December 31, 2019	September 30, 2019
Real estate loans:		
Residential Core	\$ 11,131,888	\$ 10,903,024
Residential Home Today	82,679	84,942
Home equity loans and lines of credit	2,221,380	2,174,961
Construction	51,404	52,332
Real estate loans	13,487,351	13,215,259
Other loans	2,900	3,166
Add (deduct):		
Deferred loan expenses, net	43,785	41,976
Loans in process ("LIP")	(28,972)	(25,743)
Allowance for loan losses	(37,292)	(38,913)
Loans held for investment, net	<u>\$ 13,467,772</u>	<u>\$ 13,195,745</u>

At December 31, 2019 and September 30, 2019, respectively, \$9,608 and \$3,666 of loans were classified as mortgage loans held for sale.

A large concentration of the Company's lending is in Ohio and Florida. As of December 31, 2019 and September 30, 2019, the percentage of aggregate Residential Core, Home Today and Construction loans held in Ohio was 57% as of both dates

and the percentage held in Florida was 16% as of both dates. As of December 31, 2019 and September 30, 2019, home equity loans and lines of credit were concentrated in Ohio (30% and 31%), Florida (19% as of both dates), and California (16% as of both dates).

Home Today was an affordable housing program targeted to benefit low- and moderate-income home buyers and most loans under the program were originated prior to 2009. No new loans were originated under the Home Today program after September 30, 2016. Through this program the Company provided the majority of loans to borrowers who would not otherwise qualify for the Company's loan products, generally because of low credit scores. Because the Company applied less stringent underwriting and credit standards to the majority of Home Today loans, loans originated under the program have greater credit risk than its traditional residential real estate mortgage loans in the Residential Core portfolio. Since loans are no longer originated under the Home Today program, the Home Today portfolio will continue to decline in balance, primarily due to contractual amortization. To supplant the Home Today product and to continue to meet the credit needs of customers and the communities served, since fiscal 2016 the Company has offered Fannie Mae eligible, Home Ready loans. These loans are originated in accordance with Fannie Mae's underwriting standards. While the Company retains the servicing to these loans, the loans, along with the credit risk associated therewith, are securitized/sold to Fannie Mae. The Company does not offer, and has not offered, loan products frequently considered to be designed to target sub-prime borrowers containing features such as higher fees or higher rates, negative amortization, a LTV ratio greater than 100%, or pay-option adjustable-rate mortgages.

The Company currently offers home equity lines of credit that include monthly principal and interest payments throughout the entire term. Home equity lines of credit originated prior to June 2010 require interest only payments for ten years, with an option to extend the interest only and draw period another ten years. Once the draw period has expired they are included in the home equity loan balance. The recorded investment in interest only loans comprised solely of equity lines of credit with balances of \$3,954 and \$8,231 at December 31, 2019 and September 30, 2019, respectively.

An aging analysis of the recorded investment in loan receivables that are past due at December 31, 2019 and September 30, 2019 is summarized in the following tables. When a loan is more than one month past due on its scheduled payments, the loan is considered 30 days or more past due. Balances are adjusted for deferred loan fees, expenses and any applicable loans-in-process.

	30-59 Days Past Due	60-89 Days Past Due	90 Days or More Past Due	Total Past Due	Current	Total
December 31, 2019						
Real estate loans:						
Residential Core	\$ 6,870	\$ 2,938	\$ 8,054	\$ 17,862	\$11,130,929	\$11,148,791
Residential Home Today	2,842	1,272	3,196	7,310	75,030	82,340
Home equity loans and lines of credit	2,422	1,234	5,176	8,832	2,239,799	2,248,631
Construction	—	—	—	—	22,402	22,402
Total real estate loans	12,134	5,444	16,426	34,004	13,468,160	13,502,164
Other loans	—	—	—	—	2,900	2,900
Total	<u>\$ 12,134</u>	<u>\$ 5,444</u>	<u>\$ 16,426</u>	<u>\$ 34,004</u>	<u>\$13,471,060</u>	<u>\$13,505,064</u>

	30-59 Days Past Due	60-89 Days Past Due	90 Days or More Past Due	Total Past Due	Current	Total
September 30, 2019						
Real estate loans:						
Residential Core	\$ 6,824	\$ 4,030	\$ 7,674	\$ 18,528	\$10,900,173	\$10,918,701
Residential Home Today	2,629	1,685	2,623	6,937	77,677	84,614
Home equity loans and lines of credit	3,029	1,158	5,797	9,984	2,191,998	2,201,982
Construction	—	—	—	—	26,195	26,195
Total real estate loans	12,482	6,873	16,094	35,449	13,196,043	13,231,492
Other loans	—	—	—	—	3,166	3,166
Total	<u>\$ 12,482</u>	<u>\$ 6,873</u>	<u>\$ 16,094</u>	<u>\$ 35,449</u>	<u>\$13,199,209</u>	<u>\$13,234,658</u>

At December 31, 2019 and September 30, 2019, real estate loans include \$7,719 and \$7,543, respectively, of loans that were in the process of foreclosure.

Loans are placed in non-accrual status when they are contractually 90 days or more past due. The number of days past due is determined by the number of scheduled payments that remain unpaid, assuming a period of 30 days between each scheduled payment. Loans with a partial charge-off are placed in non-accrual and will remain in non-accrual status until, at a minimum, the impairment is recovered. Loans restructured in TDRs that were in non-accrual status prior to the restructurings remain in non-accrual status for a minimum of six months after restructuring. Loans restructured in TDRs with a high debt-to-income ratio at the time of modification are placed in non-accrual status for a minimum of 12 months. Additionally, home equity loans and lines of credit where the customer has a severely delinquent first mortgage loan and loans in Chapter 7 bankruptcy status where all borrowers have filed, and not reaffirmed or been dismissed, are placed in non-accrual status.

The recorded investment of loan receivables in non-accrual status is summarized in the following table. Balances are adjusted for deferred loan fees and expenses.

	December 31, 2019	September 30, 2019
Real estate loans:		
Residential Core	\$ 33,310	\$ 37,052
Residential Home Today	11,551	12,442
Home equity loans and lines of credit	15,447	21,771
Total non-accrual loans	60,308	71,265

At December 31, 2019 and September 30, 2019, respectively, the recorded investment in non-accrual loans includes \$43,882 and \$55,171 which are performing according to the terms of their agreement, of which \$24,059 and \$25,895 are loans in Chapter 7 bankruptcy status, primarily where all borrowers have filed, and have not reaffirmed or been dismissed. The change in non-accrual from September 30, 2019 was partially impacted by the length of time TDRs with high debt-to-income ratios are retained in non-accrual status. TDRs with high debt-to-income ratios are placed in non-accrual status until they show sustained payment performance.

Interest on loans in accrual status, including certain loans individually reviewed for impairment, is recognized in interest income as it accrues, on a daily basis. Accrued interest on loans in non-accrual status is reversed by a charge to interest income and income is subsequently recognized only to the extent cash payments are received. Cash payments on loans in non-accrual status are applied to the oldest scheduled, unpaid payment first. Cash payments on loans with a partial charge-off are applied fully to principal, then to recovery of the charged off amount prior to interest income being recognized, except cash payments may be applied to interest capitalized in a restructuring when collection of remaining amounts due is considered probable. A non-accrual loan is generally returned to accrual status when contractual payments are less than 90 days past due. However, a loan may remain in non-accrual status when collectability is uncertain, such as a TDR that has not met minimum payment requirements, a loan with a partial charge-off, an equity loan or line of credit with a delinquent first mortgage greater than 90 days past due, or a loan in Chapter 7 bankruptcy status where all borrowers have filed, and have not reaffirmed or been dismissed.

The recorded investment in loan receivables at December 31, 2019 and September 30, 2019 is summarized in the following table. The table provides details of the recorded balances according to the method of evaluation used for determining the allowance for loan losses, distinguishing between determinations made by evaluating individual loans and determinations made by evaluating groups of loans not individually evaluated. Balances of recorded investments are adjusted for deferred loan fees, expenses and any applicable loans-in-process.

	December 31, 2019			September 30, 2019		
	Individually	Collectively	Total	Individually	Collectively	Total
Real estate loans:						
Residential Core	\$ 82,191	\$11,066,600	\$11,148,791	\$ 87,069	\$10,831,632	\$10,918,701
Residential Home Today	36,390	45,950	82,340	36,959	47,655	84,614
Home equity loans and lines of credit	44,668	2,203,963	2,248,631	46,445	2,155,537	2,201,982
Construction	—	22,402	22,402	—	26,195	26,195
Total real estate loans	163,249	13,338,915	13,502,164	170,473	13,061,019	13,231,492
Other loans	—	2,900	2,900	—	3,166	3,166
Total	\$ 163,249	\$13,341,815	\$13,505,064	\$ 170,473	\$13,064,185	\$13,234,658

An analysis of the allowance for loan losses at December 31, 2019 and September 30, 2019 is summarized in the following table. The analysis provides details of the allowance for loan losses according to the method of evaluation, distinguishing between allowances for loan losses determined by evaluating individual loans and allowances for loan losses determined by evaluating groups of loans collectively.

	December 31, 2019			September 30, 2019		
	Individually	Collectively	Total	Individually	Collectively	Total
Real estate loans:						
Residential Core	\$ 7,038	\$ 11,274	\$ 18,312	\$ 7,080	\$ 12,673	\$ 19,753
Residential Home Today	2,447	1,785	4,232	2,422	1,787	4,209
Home equity loans and lines of credit	3,953	10,791	14,744	4,003	10,943	14,946
Construction	—	4	4	—	5	5
Total real estate loans	\$ 13,438	\$ 23,854	\$ 37,292	\$ 13,505	\$ 25,408	\$ 38,913

At December 31, 2019 and September 30, 2019, individually evaluated loans that required an allowance were comprised only of loans evaluated for impairment based on the present value of cash flows, such as performing TDRs, and loans with an indication of further deterioration in the fair value of the property not yet supported by a full review and collateral evaluation. All other individually evaluated loans received a charge-off, if applicable.

Because many variables are considered in determining the appropriate level of general valuation allowances, directional changes in individual considerations do not always align with the directional change in the balance of a particular component of the general valuation allowance. At December 31, 2019 and September 30, 2019, respectively, allowances on individually reviewed loans evaluated for impairment (IVAs) included those based on the present value of cash flows, such as performing TDRs, were \$13,437 and \$13,399, and allowances on loans with further deteriorations in the fair value of the property not yet supported by a full review were \$1 and \$106.

Residential Core mortgage loans represent the largest portion of the residential real estate portfolio. The Company believes overall credit risk is low based on the nature, composition, collateral, products, lien position and performance of the portfolio. The portfolio does not include loan types or structures that have experienced severe performance problems at other financial institutions (sub-prime, no documentation or pay-option adjustable-rate mortgages). The portfolio contains adjustable-rate mortgage loans whereby the interest rate is locked initially for mainly three or five years then resets annually, subject to various re-lock options available to the borrower. Although the borrower is qualified for its loan at a higher rate than the initial one, the adjustable-rate feature may impact a borrower's ability to afford the higher payments upon rate reset during periods of rising interest rates. With limited historical loss experience compared to other types of loans in the portfolio, judgment is required by management in assessing the allowance required. The principal amount of loans in the portfolio that are adjustable-rate mortgage loans was \$5,129,610 and \$5,063,010 at December 31, 2019 and September 30, 2019, respectively.

As described earlier in this footnote, Home Today loans have greater credit risk than traditional residential real estate mortgage loans. At December 31, 2019 and September 30, 2019, respectively, approximately 13% and 14% of Home Today loans include private mortgage insurance coverage. The majority of the coverage on these loans was provided by PMI Mortgage Insurance Co., which was seized by the Arizona Department of Insurance in 2011 and currently pays all claim payments at 74.5%. Appropriate adjustments have been made to the Company's affected valuation allowances and charge-offs, and estimated loss severity factors were adjusted accordingly for loans evaluated collectively. The amount of loans in the Company's total owned residential portfolio covered by mortgage insurance provided by PMIC as of December 31, 2019 and September 30, 2019, respectively, was \$24,518 and \$26,191, of which \$22,684 and \$24,198 was current. The amount of loans in the Company's total owned residential portfolio covered by mortgage insurance provided by Mortgage Guaranty Insurance Corporation as of December 31, 2019 and September 30, 2019, respectively, was \$15,774 and \$17,345, of which \$15,734 and \$17,232 was current. As of December 31, 2019, MGIC's long-term debt rating, as published by the major credit rating agencies, did not meet the requirements to qualify as "high credit quality"; however, MGIC continues to make claim payments in accordance with its contractual obligations and the Company has not increased its estimated loss severity factors related to MGIC's claim paying ability. No other loans were covered by mortgage insurers that were deferring claim payments or which were assessed as being non-investment grade.

Home equity loans and lines of credit, which are comprised primarily of home equity lines of credit, represent a significant portion of the residential real estate portfolio. On home equity lines of credit originated prior to 2012, subsequent deterioration in economic and housing market conditions may impact a borrower's ability to afford the higher payments required during the end of draw repayment period that follows the period of interest only payments, or the ability to secure alternative financing. Beginning in 2013, the terms on new home equity lines of credit included monthly principal and interest payments throughout the entire term to minimize the potential payment differential between the draw and after draw periods.

The Company originates construction loans to individuals for the construction of their personal single-family residence by a qualified builder (construction/permanent loans). The Company's construction/permanent loans generally provide for disbursements to the builder or sub-contractors during the construction phase as work progresses. During the construction phase, the borrower only pays interest on the drawn balance. Upon completion of construction, the loan converts to a permanent amortizing loan without the expense of a second closing. The Company offers construction/permanent loans with fixed or adjustable-rates, and a current maximum loan-to-completed-appraised value ratio of 85%.

Other loans are comprised of loans secured by certificate of deposit accounts, which are fully recoverable in the event of non-payment, and forgivable down payment assistance loans, which are unsecured loans used as down payment assistance to borrowers qualified through partner housing agencies. The Company records a liability for the loans which are forgiven in equal increments over a pre-determined term, subject to residency requirements.

For all classes of loans, 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 and interest according to the contractual terms of the loan agreement. Factors considered in determining that a loan is impaired may include the deteriorating financial condition of the borrower indicated by missed or delinquent payments, a pending legal action, such as bankruptcy or foreclosure, or the absence of adequate security for the loan.

The recorded investment and the unpaid principal balance of impaired loans, including those reported as TDRs, as of December 31, 2019 and September 30, 2019, are summarized as follows. Balances of recorded investments are adjusted for deferred loan fees and expenses.

	December 31, 2019			September 30, 2019		
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Recorded Investment	Unpaid Principal Balance	Related Allowance
With no related IVA recorded:						
Residential Core	\$ 43,815	\$ 59,009	\$ —	\$ 44,122	\$ 59,538	\$ —
Residential Home Today	12,237	32,354	—	12,764	31,958	—
Home equity loans and lines of credit	16,625	21,477	—	18,528	23,935	—
Total	<u>\$ 72,677</u>	<u>\$ 112,840</u>	<u>\$ —</u>	<u>\$ 75,414</u>	<u>\$ 115,431</u>	<u>\$ —</u>
With an IVA recorded:						
Residential Core	\$ 38,376	\$ 38,453	\$ 7,038	\$ 42,947	\$ 43,042	\$ 7,080
Residential Home Today	24,153	24,119	2,447	24,195	24,178	2,422
Home equity loans and lines of credit	28,043	28,042	3,953	27,917	27,924	4,003
Total	<u>\$ 90,572</u>	<u>\$ 90,614</u>	<u>\$ 13,438</u>	<u>\$ 95,059</u>	<u>\$ 95,144</u>	<u>\$ 13,505</u>
Total impaired loans:						
Residential Core	\$ 82,191	\$ 97,462	\$ 7,038	\$ 87,069	\$ 102,580	\$ 7,080
Residential Home Today	36,390	56,473	2,447	36,959	56,136	2,422
Home equity loans and lines of credit	44,668	49,519	3,953	46,445	51,859	4,003
Total	<u>\$ 163,249</u>	<u>\$ 203,454</u>	<u>\$ 13,438</u>	<u>\$ 170,473</u>	<u>\$ 210,575</u>	<u>\$ 13,505</u>

At December 31, 2019 and September 30, 2019, respectively, the recorded investment in impaired loans includes \$151,313 and \$157,408 of loans restructured in TDRs of which \$8,425 and \$8,435 are 90 days or more past due.

The average recorded investment in impaired loans and the amount of interest income recognized during the period that the loans were impaired are summarized below.

	For the Three Months Ended December 31,			
	2019		2018	
	Average Recorded Investment	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized
With no related IVA recorded:				
Residential Core	\$ 43,969	\$ 365	\$ 52,733	\$ 460
Residential Home Today	12,501	48	15,762	72
Home equity loans and lines of credit	17,577	94	22,626	104
Total	<u>\$ 74,047</u>	<u>\$ 507</u>	<u>\$ 91,121</u>	<u>\$ 636</u>
With an IVA recorded:				
Residential Core	\$ 40,662	\$ 296	\$ 38,643	\$ 305
Residential Home Today	24,174	281	25,218	296
Home equity loans and lines of credit	27,980	166	25,762	158
Total	<u>\$ 92,816</u>	<u>\$ 743</u>	<u>\$ 89,623</u>	<u>\$ 759</u>
Total impaired loans:				
Residential Core	\$ 84,631	\$ 661	\$ 91,376	\$ 765
Residential Home Today	36,675	329	40,980	368
Home equity loans and lines of credit	45,557	260	48,388	262
Total	<u>\$ 166,863</u>	<u>\$ 1,250</u>	<u>\$ 180,744</u>	<u>\$ 1,395</u>

Interest on loans in non-accrual status is recognized on a cash basis. The amount of interest income on impaired loans recognized using a cash basis method was \$276 and \$392 for the three months ended December 31, 2019 and December 31, 2018, respectively. Cash payments on loans with a partial charge-off are applied fully to principal, then to recovery of the charged off amount prior to interest income being recognized, except cash payments may be applied to interest capitalized in a restructuring when collection of remaining amounts due is considered probable. Interest income on the remaining impaired loans is recognized on an accrual basis.

Charge-offs on residential mortgage loans, home equity loans and lines of credit, and construction loans are recognized when triggering events, such as foreclosure actions, short sales, or deeds accepted in lieu of repayment, result in less than full repayment of the recorded investment in the loans.

Partial or full charge-offs are also recognized for the amount of impairment on loans considered collateral dependent that meet the conditions described below.

- For residential mortgage loans, payments are greater than 180 days delinquent;
- For home equity lines of credit, equity loans, and residential loans restructured in a TDR, payments are greater than 90 days delinquent;
- For all classes of loans restructured in a TDR with a high debt-to-income ratio at time of modification;
- For all classes of loans, a sheriff sale is scheduled within 60 days to sell the collateral securing the loan;
- For all classes of loans, all borrowers have been discharged of their obligation through a Chapter 7 bankruptcy;
- For all classes of loans, within 60 days of notification, all borrowers obligated on the loan have filed Chapter 7 bankruptcy and have not reaffirmed or been dismissed;
- For all classes of loans, a borrower obligated on a loan has filed bankruptcy and the loan is greater than 30 days delinquent; and
- For all classes of loans, it becomes evident that a loss is probable.

Collateral dependent residential mortgage loans and construction loans are charged off to the extent the recorded investment in the loan, net of anticipated mortgage insurance claims, exceeds the fair value, less costs to dispose of the underlying property. Management can determine if the loan is uncollectible for reasons such as foreclosures exceeding a reasonable time frame and recommend a full charge-off. Home equity loans or lines of credit are charged off to the extent the recorded investment in the loan plus the balance of any senior liens exceeds the fair value, less costs to dispose of the underlying property, or management determines the collateral is not sufficient to satisfy the loan. A loan in any portfolio identified as collateral dependent will continue to be reported as impaired until it is no longer considered collateral dependent, is less than 30 days past due and does not have a prior charge-off. A loan in any portfolio that has a partial charge-off consequent to impairment evaluation will continue to be individually evaluated for impairment until, at a minimum, the impairment has been recovered.

Residential mortgage loans and construction loans restructured in TDRs that are not evaluated based on collateral are separately evaluated for impairment on a loan by loan basis at the time of restructuring and at each subsequent reporting date for as long as they are reported as TDRs. The impairment evaluation is based on the present value of expected future cash flows discounted at the effective interest rate of the original loan. Expected future cash flows include a discount factor representing a potential for default. Valuation allowances are recorded for the excess of the recorded investments over the result of the cash flow analysis. Loans discharged in Chapter 7 bankruptcy are reported as TDRs and also evaluated based on the present value of expected future cash flows unless evaluated based on collateral. We evaluate these loans using the expected future cash flows because we expect the borrower, not liquidation of the collateral, to be the source of repayment for the loan. Other loans are not considered for restructuring. A loan restructured in a TDR is classified as an impaired loan for a minimum of one year. After one year, that loan may be reclassified out of the balance of impaired loans if the loan was restructured to yield a market rate for loans of similar credit risk at the time of restructuring and the loan is not impaired based on the terms of the restructuring agreement. No loans whose terms were restructured in TDRs were reclassified from impaired loans during the three months months ended December 31, 2019 and December 31, 2018.

Initial concessions granted by loans restructured as TDRs can include reduction of interest rate, extension of amortization period, forbearance or other actions. Some TDRs have experienced a combination of concessions. TDRs also can occur as a result of bankruptcy proceedings. Loans discharged in Chapter 7 bankruptcy are classified as multiple restructurings if the loan's original terms had also been restructured by the Company. The recorded investment in TDRs by category as of December 31, 2019 and September 30, 2019 is shown in the tables below.

<u>December 31, 2019</u>	Initial Restructuring	Multiple Restructurings	Bankruptcy	Total
Residential Core	\$ 33,792	\$ 24,865	\$ 17,736	\$ 76,393
Residential Home Today	15,868	16,565	3,098	35,531
Home equity loans and lines of credit	33,072	3,224	3,093	39,389
Total	\$ 82,732	\$ 44,654	\$ 23,927	\$ 151,313

<u>September 30, 2019</u>	Initial Restructuring	Multiple Restructurings	Bankruptcy	Total
Residential Core	\$ 35,829	\$ 24,951	\$ 19,494	\$ 80,274
Residential Home Today	16,233	16,868	3,234	36,335
Home equity loans and lines of credit	34,459	3,115	3,225	40,799
Total	\$ 86,521	\$ 44,934	\$ 25,953	\$ 157,408

TDRs may be restructured more than once. Among other requirements, a subsequent restructuring may be available for a borrower upon the expiration of temporary restructuring terms if the borrower cannot return to regular loan payments. If the borrower is experiencing an income curtailment that temporarily has reduced their capacity to repay, such as loss of employment, reduction of hours, non-paid leave or short-term disability, a temporary restructuring is considered. If the borrower lacks the capacity to repay the loan at the current terms due to a permanent condition, a permanent restructuring is considered. In evaluating the need for a subsequent restructuring, the borrower's ability to repay is generally assessed utilizing a debt to income and cash flow analysis.

For all loans restructured during the three months ended December 31, 2019 and December 31, 2018 (set forth in the tables below), the pre-restructured outstanding recorded investment was not materially different from the post-restructured outstanding recorded investment.

The following tables set forth the recorded investment in TDRs restructured during the periods presented.

For the Three Months Ended December 31, 2019				
	Initial Restructuring	Multiple Restructurings	Bankruptcy	Total
Residential Core	\$ 1,183	\$ 1,771	\$ 178	\$ 3,132
Residential Home Today	306	765	38	1,109
Home equity loans and lines of credit	264	378	280	922
Total	\$ 1,753	\$ 2,914	\$ 496	\$ 5,163

For the Three Months Ended December 31, 2018				
	Initial Restructuring	Multiple Restructurings	Bankruptcy	Total
Residential Core	\$ 2,766	\$ 2	\$ 922	\$ 3,690
Residential Home Today	272	—	125	397
Home equity loans and lines of credit	3,534	—	200	3,734
Total	\$ 6,572	\$ 2	\$ 1,247	\$ 7,821

Below summarizes the information on TDRs restructured within 12 months of the period presented for which there was a subsequent payment default, at least 30 days past due on one scheduled payment, during the period presented.

<u>TDRs That Subsequently Defaulted</u>	For the Three Months Ended December 31,			
	2019		2018	
	Number of Contracts	Recorded Investment	Number of Contracts	Recorded Investment
Residential Core	11	\$ 1,561	10	\$ 1,356
Residential Home Today	15	577	18	875
Home equity loans and lines of credit	7	503	10	661
Total	33	\$ 2,641	38	\$ 2,892

Residential loans are internally assigned a grade that complies with the guidelines outlined in the OCC's Handbook for Rating Credit Risk. Pass loans are assets well protected by the current paying capacity of the borrower. Special Mention loans have a potential weakness, as evaluated based on delinquency status or nature of the product, that the Company feels deserve management's attention and may result in further deterioration in their repayment prospects and/or the Company's credit position. Substandard loans are inadequately protected by the current payment capacity of the borrower or the collateral pledged with a defined weakness that jeopardizes the liquidation of the debt. Also included in Substandard are performing home equity loans and lines of credit where the customer has a severely delinquent first mortgage to which the performing home equity loan or line of credit is subordinate and loans in Chapter 7 bankruptcy status where all borrowers have filed, and have not reaffirmed or been dismissed. Loss loans are considered uncollectible and are charged off when identified. Loss loans are of such little value that their continuance as bankable assets is not warranted even though partial recovery may be effected in the future.

The following tables provide information about the credit quality of residential loan receivables by an internally assigned grade. Balances are adjusted for deferred loan fees, expenses and any applicable loans-in-process.

	Pass	Special Mention	Substandard	Loss	Total
December 31, 2019					
Real estate loans:					
Residential Core	\$ 11,104,802	\$ 4,282	\$ 39,707	\$ —	\$ 11,148,791
Residential Home Today	69,331	—	13,009	—	82,340
Home equity loans and lines of credit	2,228,691	2,391	17,549	—	2,248,631
Construction	22,402	—	—	—	22,402
Total real estate loans	\$ 13,425,226	\$ 6,673	\$ 70,265	\$ —	\$ 13,502,164

	Pass	Special Mention	Substandard	Loss	Total
September 30, 2019					
Real estate loans:					
Residential Core	\$ 10,869,597	\$ 4,348	\$ 44,756	\$ —	\$ 10,918,701
Residential Home Today	70,631	—	13,983	—	84,614
Home equity loans and lines of credit	2,175,341	2,588	24,053	—	2,201,982
Construction	26,195	—	—	—	26,195
Total real estate loans	\$ 13,141,764	\$ 6,936	\$ 82,792	\$ —	\$ 13,231,492

At December 31, 2019 and September 30, 2019, respectively, the recorded investment of impaired loans includes \$96,826 and \$90,295 of TDRs individually evaluated for impairment that have adequately performed under the terms of the restructuring and are classified as Pass loans. At December 31, 2019 and September 30, 2019, respectively, there were \$3,842 and \$2,614 of loans classified Substandard and \$6,673 and \$6,936 of loans designated Special Mention that are not included in the recorded investment of impaired loans; rather, they are included in loans collectively evaluated for impairment. Of the \$6,673 of loans classified Special Mention at December 31, 2019, \$4,282 are residential mortgage loans purchased which were

current and performing at the time of purchase. These loans are designated Special Mention due to the absence of mortgage insurance coverage and potentially weaker repayment prospects when compared with the Company's originated residential Core Portfolio.

Other loans are internally assigned a grade of non-performing when they become 90 days or more past due. At December 31, 2019 and September 30, 2019, no other loans were graded as non-performing.

Activity in the allowance for loan losses is summarized as follows:

	For the Three Months Ended December 31, 2019				
	Beginning Balance	Provisions	Charge-offs	Recoveries	Ending Balance
Real estate loans:					
Residential Core	\$ 19,753	\$ (1,766)	\$ (485)	\$ 810	\$ 18,312
Residential Home Today	4,209	(145)	(359)	527	4,232
Home equity loans and lines of credit	14,946	(1,088)	(745)	1,631	14,744
Construction	5	(1)	—	—	4
Total real estate loans	<u>\$ 38,913</u>	<u>\$ (3,000)</u>	<u>\$ (1,589)</u>	<u>\$ 2,968</u>	<u>\$ 37,292</u>

	For the Three Months Ended December 31, 2018				
	Beginning Balance	Provisions	Charge-offs	Recoveries	Ending Balance
Real estate loans:					
Residential Core	\$ 18,288	\$ 909	\$ (243)	\$ 211	\$ 19,165
Residential Home Today	3,204	317	(241)	468	3,748
Home equity loans and lines of credit	20,921	(3,225)	(843)	2,168	19,021
Construction	5	(1)	—	—	4
Total real estate loans	<u>\$ 42,418</u>	<u>\$ (2,000)</u>	<u>\$ (1,327)</u>	<u>\$ 2,847</u>	<u>\$ 41,938</u>

5. LEASES

On October 1, 2019, the Company adopted ASU 2016-02, Leases (Topic 842) and all related amendments which require lessees to recognize operating leases on the Consolidated Statements of Condition as lease assets (a right-of-use asset) and lease liabilities (a liability to make lease payments), measured on a discounted basis. Prior to October 1, 2019, operating leases were not recorded on the balance sheet. As permitted under ASC 842, the Company has made an accounting policy election to exempt leases with an initial term of twelve months or less from balance sheet recognition and to expense them over the lease term. As of December 31, 2019 the Company has no leases with an initial term of twelve months or less. The Company elected the practical expedient to account for lease and non-lease components as a single lease component for all classes of assets. The Company also elected the package of practical expedients that do not require reassessment of whether any expired or existing contracts are or contain leases, the lease classification for any expired or existing leases, or initial direct costs for any existing leases. The Company also adopted ASU 2018-11, Leases (Topic 842) Targeted Improvements, and elected not to recast comparative periods in the period of adoption of ASU 2016-02. Refer to *Note 15. Recent Accounting Pronouncements*, for further discussions regarding the adoption of this new guidance.

As a lessee, the Company enters into leases of buildings and land. The Company occupies certain banking branches and a disaster recovery site through non-cancellable operating leases with remaining terms ranging from less than one year to 18 years. The Company has no financing leases. Most of the leases have fixed payment terms with annual fixed-escalation clauses. Certain leases have annual rent escalations based on subsequent year-to-year changes in the consumer price index. These year-to-year changes in the consumer price index are excluded from the calculation of right-of-use assets and lease liabilities and recognized as expense in the period in which they are incurred. Additionally, all variable lease costs that are not based on an index or rate, such as "common area maintenance" costs, are expensed as incurred. Most of the Company's leases include options to extend for periods that range from five to 10 years. None of the leases have early-termination options. The Company has not included term extensions in the calculation of the lease term, as the Company does not consider it reasonably certain

that the options will be exercised. As the interest rate implicit in all of the Company's lease contracts is not readily determinable, the Company utilized its incremental borrowing rate, which is the rate that would be incurred to borrow on a collateralized basis over a similar term on an amount equal to the total contractual lease payments in a similar economic environment. The incremental borrowing rate utilized for all the Company's leases is the FHLB Advance rate based on the lease term at commencement in determining the present value of lease payments.

Operating and variable lease expenses for the three months ended December 31, 2019 totaled \$1,295 and \$336, respectively. During the three months ended December 31, 2019, the Company paid \$1,264 in cash for amounts included in the measurement of lease liabilities. As of December 31, 2019, the Company has not entered into any material leases that have not yet commenced.

The following table summarizes information relating to the Company's operating leases as of December 31, 2019:

Right-of-use assets (a)	\$ 18,362
Lease liabilities (b)	\$ 18,708
Weighted Average Remaining Lease Term	6.34 years
Weighted Average Discount Rate	1.92%

(a) Included in other assets in the Consolidated Statements of Condition

(b) Included in accrued expenses and other liabilities in the Consolidated Statements of Condition

The following table summarizes the maturities of lease liabilities as of December 31, 2019:

Maturing in:	Amount
12 months or less	\$ 4,988
13 to 24 months	4,023
25 to 36 months	3,183
37 to 48 months	2,285
49 to 60 months	1,659
over 60 months	3,874
Total minimum lease payments	20,012
Less imputed interest	1,304
Total lease liabilities	\$ 18,708

The following table summarizes the future minimum payments as of September 30, 2019, prior to the date of adoption and as defined by previous lease accounting guidance, ASC 840, with non-cancellable operating lease terms expiring after September 30, 2019:

Maturing in:	Amount
12 months or less	\$ 4,881
13 to 24 months	4,145
25 to 36 months	3,171
37 to 48 months	2,366
49 to 60 months	1,613
over 60 months	4,209
Total minimum lease payments	\$ 20,385

6. DEPOSITS

Deposit account balances are summarized as follows:

	December 31, 2019	September 30, 2019
Checking accounts	\$ 891,780	\$ 862,647
Savings accounts, excluding money market accounts	1,035,394	1,042,357
Money market accounts	469,138	441,843
Certificates of deposit	6,600,307	6,415,824
	<u>8,996,619</u>	<u>8,762,671</u>
Accrued interest	4,301	3,713
Total deposits	<u>\$ 9,000,920</u>	<u>\$ 8,766,384</u>

Brokered certificates of deposit (exclusive of acquisition costs and subsequent amortization), which are used as a cost effective funding alternative, totaled \$501,360 at December 31, 2019 and \$507,800 at September 30, 2019. The FDIC places restrictions on banks with regard to issuing brokered deposits based on the bank's capital classification. As a well-capitalized institution at December 31, 2019 and September 30, 2019, the Association may accept brokered deposits without FDIC restrictions.

7. BORROWED FUNDS

Federal Home Loan Bank borrowings at December 31, 2019 are summarized in the table below. The amount and weighted average rates of certain FHLB Advances maturing in 24 months or less reflect the net impact of deferred penalties discussed below:

	Amount	Weighted Average Rate
Maturing in:		
12 months or less	\$ 3,419,603	1.75%
13 to 24 months	636	1.47%
25 to 36 months	1,800	0.96%
37 to 48 months	165,000	1.90%
49 to 60 months	275,000	1.68%
Over 60 months	20,903	1.68%
Total FHLB Advances	<u>3,882,942</u>	1.75%
Accrued interest	6,707	
Total	<u>\$ 3,889,649</u>	

For the periods ending December 31, 2019 and December 31, 2018 net interest expense related to Federal Home Loan Bank short-term borrowings was \$14,295 and \$14,246, respectively.

Through the use of interest rate swaps discussed in *Note 14. Derivative Instruments*, \$2,800,000 of FHLB advances included in the table above as maturing in 12 months or less, have effective maturities, assuming no early terminations of the swap contracts, as shown below:

	Amount	Swap Adjusted Weighted Average Rate
Effective maturity:		
12 months or less	\$ 125,000	1.25%
13 to 24 months	550,000	1.27%
25 to 36 months	875,000	1.94%
37 to 48 months	175,000	2.66%
49 to 60 months	275,000	1.69%
Over 60 months	800,000	2.34%
Total FHLB Advances under swap contracts	<u>\$ 2,800,000</u>	1.91%

During fiscal year 2016, \$150,000 fixed-rate FHLB advances with remaining terms of approximately four years were prepaid and replaced with new four- and five-year interest rate swap arrangements. The unamortized deferred repayment penalties of \$413 related to the \$150,000 of restructuring are being recognized in interest expense over the remaining term of the swap contracts.

8. OTHER COMPREHENSIVE INCOME (LOSS)

The change in accumulated other comprehensive income (loss) by component is as follows:

	For the Three Months Ended				For the Three Months Ended			
	December 31, 2019				December 31, 2018			
	Unrealized Gains (Losses) on Securities Available for Sale	Cash flow hedges	Defined Benefit Plan	Total	Unrealized Gains (Losses) on Securities Available for Sale	Cash flow hedges	Defined Benefit Plan	Total
Balance at beginning of period	\$ (2,165)	\$(44,915)	\$(22,299)	\$(69,379)	\$ (13,624)	\$ 51,914	\$(15,068)	\$ 23,222
Other comprehensive income (loss) before reclassifications, net of tax expense (benefit) of \$5,022 and \$(5,158)	2,923	15,972	—	18,895	5,097	(24,500)	—	(19,403)
Amounts reclassified, net of tax expense (benefit) of \$(84) and \$(547)	—	(767)	452	(315)	—	(2,322)	264	(2,058)
Other comprehensive income (loss)	2,923	15,205	452	18,580	5,097	(26,822)	264	(21,461)
Balance at end of period	<u>\$ 758</u>	<u>\$(29,710)</u>	<u>\$(21,847)</u>	<u>\$(50,799)</u>	<u>\$ (8,527)</u>	<u>\$ 25,092</u>	<u>\$(14,804)</u>	<u>\$ 1,761</u>

The following table presents the reclassification adjustment out of accumulated other comprehensive income included in net income and the corresponding line item on the consolidated statements of income for the periods indicated:

Details about Accumulated Other Comprehensive Income Components	Amounts Reclassified from Accumulated Other Comprehensive Income		Line Item in the Consolidated Statement of Income
	For the Three Months Ended December 31,		
	2019	2018	
Cash flow hedges:			
Interest (income) expense	\$ (971)	\$ (2,939)	Interest expense
Net income tax effect	204	617	Income tax expense
Net of income tax expense (benefit)	(767)	(2,322)	
Amortization of defined benefit plan:			
Actuarial loss	572	334	(a)
Net income tax effect	(120)	(70)	Income tax expense
Net of income tax expense (benefit)	452	264	
Total reclassifications for the period	\$ (315)	\$ (2,058)	

(a) This item is included in the computation of net periodic pension cost. See *Note 10. Defined Benefit Plan* for additional disclosure.

9. INCOME TAXES

The Company and its subsidiaries file income tax returns in the U.S. federal jurisdiction and in various state and city jurisdictions. The Company is no longer subject to income tax examinations in its major jurisdictions for tax years prior to 2016.

The Company recognizes interest and penalties on income tax assessments or income tax refunds, where applicable, in the financial statements as a component of its provision for income taxes.

The Company's combined federal and state effective income tax rate was 19.4% and 23.3% for the three months ended December 31, 2019 and December 31, 2018, respectively. The decrease in the effective tax rate is primarily due to lower state tax expense and an increase in excess tax benefits associated with equity compensation during the three months ended December 31, 2019 compared to the three months ended December 31, 2018.

The Company makes certain investments in limited partnerships which invest in affordable housing projects that qualify for the Low Income Housing Tax Credit (LIHTC). The Company acts as a limited partner in these investments and does not exert control over the operating or financial policies of the partnership. The Company accounts for its interests in LIHTCs using the proportional amortization method. The impact of the Company's investments in tax credit entities on the provision for income taxes was not material during the three months ended December 31, 2019 and December 31, 2018.

10. DEFINED BENEFIT PLAN

The Third Federal Savings Retirement Plan (the "Plan") is a defined benefit pension plan. Effective December 31, 2002, the Plan was amended to limit participation to employees who met the Plan's eligibility requirements on that date. Effective December 31, 2011, the Plan was amended to freeze future benefit accruals for participants in the Plan. After December 31, 2002, employees not participating in the Plan, upon meeting the applicable eligibility requirements, and those eligible participants who no longer receive service credits under the Plan, participate in a separate tier of the Company's defined contribution 401(k) Savings Plan. Benefits under the Plan are based on years of service and the employee's average annual compensation (as defined in the Plan) through December 31, 2011. The funding policy of the Plan is consistent with the funding requirements of U.S. federal and other governmental laws and regulations.

The components of net periodic cost recognized in other non-interest expense in the unaudited Consolidated Statements of Income are as follows:

	Three Months Ended December 31,	
	2019	2018
Interest cost	\$ 699	\$ 807
Expected return on plan assets	(1,163)	(1,146)
Amortization of net loss	572	334
Net periodic cost (benefit)	<u>\$ 108</u>	<u>\$ (5)</u>

There were no required minimum employer contributions during the three months ended December 31, 2019. There are no required minimum employer contributions expected during the remainder of the fiscal year ending September 30, 2020.

11. EQUITY INCENTIVE PLAN

In December 2019, 73,700 restricted stock units were granted to certain directors and officers of the Company and 51,800 performance stock units were granted to certain officers of the Company. The awards were made pursuant to the Amended and Restated 2008 Equity Incentive Plan, which was approved at the annual meeting of shareholders held on February 22, 2018.

The following table presents share-based compensation expense recognized during the periods presented.

	Three Months Ended December 31,	
	2019	2018
Stock option expense	\$ 188	\$ 237
Restricted stock units expense	860	844
Performance share units expense	141	—
Total stock-based compensation expense	<u>\$ 1,189</u>	<u>\$ 1,081</u>

At December 31, 2019, 3,849,700 shares were subject to options, with a weighted average exercise price of \$13.94 per share and a weighted average grant date fair value of \$2.61 per share. Expected future expense related to the 600,780 non-vested options outstanding as of December 31, 2019 is \$417 over a weighted average period of 0.8 years. At December 31, 2019, 542,276 restricted stock units and 116,300 performance stock units with a weighted average grant date fair value of \$15.60 and \$17.42 per unit, respectively, are unvested. Expected future compensation expense relating to the 1,312,873 restricted stock units and 116,300 performance stock units outstanding as of December 31, 2019 is \$4,012 over a weighted average period of 1.6 years and \$1,472 over a weighted average period of 1.9 years, respectively. Each unit is equivalent to one share of common stock.

12. COMMITMENTS AND CONTINGENT LIABILITIES

In the normal course of business, the Company enters into commitments with off-balance sheet risk to meet the financing needs of its customers. 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 to originate loans generally have fixed expiration dates of 60 to 360 days or other termination clauses and may require payment of a fee. Unfunded commitments related to home equity lines of credit generally expire from five to 10 years following the date that the line of credit was established, subject to various conditions, including compliance with payment obligations, adequacy of collateral securing the line and maintenance of a satisfactory credit profile by the borrower. Since some of the commitments may expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements.

Off-balance sheet commitments to extend credit involve elements of credit risk and interest rate risk in excess of the amount recognized in the consolidated statements of condition. The Company's exposure to credit loss in the event of nonperformance by the other party to the commitment is represented by the contractual amount of the commitment. The Company generally uses the same credit policies in making commitments as it does for on-balance-sheet instruments. Interest rate risk on commitments to extend credit results from the possibility that interest rates may have moved unfavorably from the position of the Company since the time the commitment was made.

At December 31, 2019, the Company had commitments to originate loans as follows:

Fixed-rate mortgage loans	\$ 196,382
Adjustable-rate mortgage loans	266,517
Equity loans and lines of credit	123,540
Total	\$ 586,439

At December 31, 2019, the Company had unfunded commitments outstanding as follows:

Equity lines of credit	\$ 2,298,011
Construction loans	28,972
Total	\$ 2,326,983

At December 31, 2019, the unfunded commitment on home equity lines of credit, including commitments for accounts suspended as a result of material default or a decline in equity, is \$2,310,802.

The above commitments are expected to be funded through normal operations.

The Company and its subsidiaries are subject to various legal actions arising in the normal course of business. In the opinion of management, the resolution of these legal actions is not expected to have a material adverse effect on the Company's consolidated financial condition, results of operation, or statements of cash flows.

13. FAIR VALUE

Under U.S. GAAP, fair value is defined as the price that would be received to sell an asset, or paid to transfer a liability, in an orderly transaction between market participants at the measurement date under current market conditions. A fair value framework is established whereby assets and liabilities measured at fair value are grouped into three levels of a fair value hierarchy, based on the transparency of inputs and the reliability of assumptions used to estimate fair value. The Company's policy is to recognize transfers between levels of the hierarchy as of the end of the reporting period in which the transfer occurs. The three levels of inputs are defined as follows:

- Level 1* – quoted prices (unadjusted) for identical assets or liabilities in active markets.
- Level 2* – quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets with few transactions, or model-based valuation techniques using assumptions that are observable in the market.
- Level 3* – a company's own assumptions about how market participants would price an asset or liability.

As permitted under the fair value guidance in U.S. GAAP, the Company elects to measure at fair value mortgage loans classified as held for sale that are subject to pending agency contracts to securitize and sell loans. This election is expected to reduce volatility in earnings related to market fluctuations between the contract trade and settlement dates. At December 31, 2019 and September 30, 2019, there were no loans held for sale subject to pending agency contracts for which the fair value option was elected.

Presented below is a discussion of the methods and significant assumptions used by the Company to estimate fair value.

Investment Securities Available for Sale—Investment securities available for sale are recorded at fair value on a recurring basis. At December 31, 2019 and September 30, 2019, respectively, this includes \$553,997 and \$547,864 of investments in U.S. government obligations including highly liquid collateralized mortgage obligations issued by Fannie Mae, Freddie Mac and Ginnie Mae, measured using the market approach. The fair values of investment securities represent unadjusted price estimates obtained from third party independent nationally recognized pricing services using pricing models or quoted prices of securities with similar characteristics and are included in Level 2 of the hierarchy. Third party pricing is reviewed on a monthly basis for reasonableness based on the market knowledge and experience of company personnel that interact daily with the markets for these types of securities.

Mortgage Loans Held for Sale—The fair value of mortgage loans held for sale is estimated on an aggregate basis using a market approach based on quoted secondary market pricing for loan portfolios with similar characteristics. Loans held for sale are carried at the lower of cost or fair value except, as described above, the Company elects the fair value measurement option for mortgage loans held for sale subject to pending agency contracts to securitize and sell loans. Loans held for sale are

included in Level 2 of the hierarchy. At December 31, 2019 and September 30, 2019, there were \$9,608 and \$3,666, respectively, of loans held for sale carried at cost.

Impaired Loans—Impaired loans represent certain loans held for investment that are subject to a fair value measurement under U.S. GAAP because they are individually evaluated for impairment and that impairment is measured using a fair value measurement, such as the fair value of the underlying collateral. Impairment is measured using a market approach based on the fair value of the collateral, less estimated costs to dispose, for loans the Company considers to be collateral-dependent due to a delinquency status or other adverse condition severe enough to indicate that the borrower can no longer be relied upon as the continued source of repayment. These conditions are described more fully in *Note 4. Loans and Allowance for Loan Losses*. To calculate impairment of collateral-dependent loans, the fair market values of the collateral, estimated using exterior appraisals in the majority of instances, are reduced by calculated costs to dispose, derived from historical experience and recent market conditions. Any indicated impairment is recognized by a charge to the allowance for loan losses. Subsequent increases in collateral values or principal pay downs on loans with recognized impairment could result in an impaired loan being carried below its fair value. When no impairment loss is indicated, the carrying amount is considered to approximate the fair value of that loan to the Company because contractually that is the maximum recovery the Company can expect. The recorded investment of loans individually evaluated for impairment based on the fair value of the collateral are included in Level 3 of the hierarchy with assets measured at fair value on a non-recurring basis. The range and weighted average impact of estimated costs to dispose on fair values is determined at the time of impairment or when additional impairment is recognized and is included in quantitative information about significant unobservable inputs later in this note.

Loans held for investment that have been restructured in TDRs, are performing according to the restructured terms of the loan agreement and not evaluated based on collateral are individually evaluated for impairment using the present value of future cash flows based on the loan's effective interest rate, which is not a fair value measurement. At December 31, 2019 and September 30, 2019, respectively, this included \$98,227 and \$98,875 in recorded investment of TDRs with related allowances for loss of \$13,437 and \$13,399.

Real Estate Owned—Real estate owned includes real estate acquired as a result of foreclosure or by deed in lieu of foreclosure and is carried at the lower of the cost basis or fair value, less estimated costs to dispose. The carrying amounts of real estate owned at December 31, 2019 and September 30, 2019 were \$2,813 and \$2,163, respectively. Fair value is estimated under the market approach using independent third party appraisals. As these properties are actively marketed, estimated fair values may be adjusted by management to reflect current economic and market conditions. At December 31, 2019 and September 30, 2019, these adjustments were not significant to reported fair values. At December 31, 2019 and September 30, 2019, respectively, \$2,401 and \$987 of real estate owned is included in Level 3 of the hierarchy with assets measured at fair value on a non-recurring basis where the cost basis equals or exceeds the estimate of fair values, less estimated costs to dispose of these properties. Real estate owned, included in other assets in the Consolidated Statements of Condition, includes estimated costs to dispose of \$313 and \$146 related to properties measured at fair value and \$725 and \$1,322 of properties carried at their original or adjusted cost basis at December 31, 2019 and September 30, 2019, respectively.

Derivatives—Derivative instruments include interest rate locks on commitments to originate loans for the held for sale portfolio and interest rate swaps designated as cash flow hedges. Derivatives not designated as cash flow hedges are reported at fair value in other assets or other liabilities on the Consolidated Statement of Condition with changes in value recorded in current earnings. Derivatives qualifying as cash flow hedges, when highly effective, are reported in other assets or other liabilities on the Consolidated Statement of Condition with changes in value recorded in OCI. The fair value of interest rate lock commitments is adjusted by a closure rate based on the estimated percentage of commitments that will result in closed loans. The range and weighted average impact of the closure rate is included in quantitative information about significant unobservable inputs later in this note. A significant change in the closure rate may result in a significant change in the ending fair value measurement of these derivatives relative to their total fair value. Because the closure rate is a significantly unobservable assumption, interest rate lock commitments are included in Level 3 of the hierarchy.

Assets and liabilities carried at fair value on a recurring basis in the Consolidated Statements of Condition at December 31, 2019 and September 30, 2019 are summarized below. There were no liabilities carried at fair value on a recurring basis at either date.

	December 31, 2019	Recurring Fair Value Measurements at Reporting Date Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets				
Investment securities available for sale:				
REMICs	\$ 547,342	\$ —	\$ 547,342	\$ —
Fannie Mae certificates	6,655	—	6,655	—
Derivatives:				
Interest rate lock commitments	54	—	—	54
Total	\$ 554,051	\$ —	\$ 553,997	\$ 54

	September 30, 2019	Recurring Fair Value Measurements at Reporting Date Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets				
Investment securities available for sale:				
REMICs	\$ 541,042	\$ —	\$ 541,042	\$ —
Fannie Mae certificates	6,822	—	6,822	—
Derivatives:				
Interest rate lock commitments	44	—	—	44
Total	\$ 547,908	\$ —	\$ 547,864	\$ 44

The table below presents a reconciliation of the beginning and ending balances and the location within the Consolidated Statements of Income where gains (losses) due to changes in fair value are recognized on interest rate lock commitments which are measured at fair value on a recurring basis using significant unobservable inputs (Level 3).

	Three Months Ended December 31,	
	2019	2018
Beginning balance	\$ 44	\$ (2)
Gain (loss) during the period due to changes in fair value:		
Included in other non-interest income	10	79
Ending balance	\$ 54	\$ 77
Change in unrealized gains for the period included in earnings for assets held at end of the reporting date	\$ 54	\$ 77

Summarized in the tables below are those assets measured at fair value on a nonrecurring basis.

	December 31, 2019	Nonrecurring Fair Value Measurements at Reporting Date Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Impaired loans, net of allowance	\$ 65,021	\$ —	\$ —	\$ 65,021
Real estate owned ⁽¹⁾	2,401	—	—	2,401
Total	\$ 67,422	\$ —	\$ —	\$ 67,422

⁽¹⁾ Amounts represent fair value measurements of properties before deducting estimated costs to dispose.

	September 30, 2019	Nonrecurring Fair Value Measurements at Reporting Date Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Impaired loans, net of allowance	\$ 71,492	\$ —	\$ —	\$ 71,492
Real estate owned ⁽¹⁾	987	—	—	987
Total	\$ 72,479	\$ —	\$ —	\$ 72,479

⁽¹⁾ Amounts represent fair value measurements of properties before deducting estimated costs to dispose.

The following provides quantitative information about significant unobservable inputs categorized within Level 3 of the Fair Value Hierarchy. The interest rate lock commitments include both mortgage origination applications and preapprovals. Preapprovals have a much lower closure rate than origination applications as reflected in the weighted average closure rate.

	Fair Value	Valuation Technique(s)	Unobservable Input	Range	Weighted Average
	December 31, 2019				
Impaired loans, net of allowance	\$65,021	Market comparables of collateral discounted to estimated net proceeds	Discount appraised value to estimated net proceeds based on historical experience:	0 - 30%	6.2%
			• Residential Properties		
Interest rate lock commitments	\$54	Quoted Secondary Market pricing	Closure rate	0 - 100%	58.3%
	Fair Value	Valuation Technique(s)	Unobservable Input	Range	Weighted Average
	September 30, 2019				
Impaired loans, net of allowance	\$71,492	Market comparables of collateral discounted to estimated net proceeds	Discount appraised value to estimated net proceeds based on historical experience:	0 - 30%	6.1%
			• Residential Properties		
Interest rate lock commitments	\$44	Quoted Secondary Market pricing	Closure rate	0 - 100%	65.6%

The following tables present the estimated fair value of the Company’s financial instruments and their carrying amounts as reported in the Statement of Condition.

	December 31, 2019				
	Carrying Amount	Fair Value	Level 1	Level 2	Level 3
Assets:					
Cash and due from banks	\$ 25,935	\$ 25,935	\$ 25,935	\$ —	\$ —
Interest earning cash equivalents	255,291	255,291	255,291	—	—
Investment securities available for sale	553,997	553,997	—	553,997	—
Mortgage loans held for sale	9,608	9,670	—	9,670	—
Loans, net:					
Mortgage loans held for investment	13,464,872	13,597,535	—	—	13,597,535
Other loans	2,900	2,918	—	—	2,918
Federal Home Loan Bank stock	101,858	101,858	N/A	—	—
Accrued interest receivable	40,222	40,222	—	40,222	—
Cash collateral received from or held by counterparty	35,988	35,988	35,988	—	—
Derivatives	54	54	—	—	54
Liabilities:					
Checking and passbook accounts	\$ 2,396,312	\$ 2,396,312	\$ —	\$ 2,396,312	\$ —
Certificates of deposit	6,604,608	6,604,974	—	6,604,974	—
Borrowed funds	3,889,649	3,911,839	—	3,911,839	—
Borrowers’ advances for insurance and taxes	99,391	99,391	—	99,391	—
Principal, interest and escrow owed on loans serviced	31,503	31,503	—	31,503	—

September 30, 2019

	Carrying Amount	Fair Value	Level 1	Level 2	Level 3
Assets:					
Cash and due from banks	\$ 31,728	\$ 31,728	\$ 31,728	\$ —	\$ —
Interest earning cash equivalents	243,415	243,415	243,415	—	—
Investment securities available for sale	547,864	547,864	—	547,864	—
Mortgage loans held for sale	3,666	3,706	—	3,706	—
Loans, net:					
Mortgage loans held for investment	13,192,579	13,716,398	—	—	13,716,398
Other loans	3,166	3,328	—	—	3,328
Federal Home Loan Bank stock	101,858	101,858	N/A	—	—
Accrued interest receivable	40,822	40,822	—	40,822	—
Cash collateral received from or held by counterparty	44,261	44,261	44,261	—	—
Derivatives	44	44	—	—	44
Liabilities:					
Checking and passbook accounts	\$ 2,346,847	\$ 2,346,847	\$ —	\$ 2,346,847	\$ —
Certificates of deposit	6,419,537	6,541,791	—	6,541,791	—
Borrowed funds	3,902,981	3,903,032	—	3,903,032	—
Borrowers' advances for insurance and taxes	103,328	103,328	—	103,328	—
Principal, interest and escrow owed on loans serviced	32,909	32,909	—	32,909	—

Presented below is a discussion of the valuation techniques and inputs used by the Company to estimate fair value.

Cash and Due from Banks, Interest Earning Cash Equivalents, Cash Collateral Received from or Held by Counterparty— The carrying amount is a reasonable estimate of fair value.

Investment and Mortgage-Backed Securities— Estimated fair value for investment and mortgage-backed securities is based on quoted market prices, when available. If quoted prices are not available, management will use as part of their estimation process fair values which are obtained from third party independent nationally recognized pricing services using pricing models, quoted prices of securities with similar characteristics or discounted cash flows.

Mortgage Loans Held for Sale— Fair value of mortgage loans held for sale is based on quoted secondary market pricing for loan portfolios with similar characteristics.

Loans— For mortgage loans held for investment and other loans, fair value is estimated by discounting contractual cash flows adjusted for prepayment estimates using the current rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining term. The use of current rates to discount cash flows reflects current market expectations with respect to credit exposure. See *Item 3. Quantitative and Qualitative Disclosures About Market Risk* for more information on the methodology used to estimate fair value. Impaired loans are measured at the lower of cost or fair value as described earlier in this footnote.

Federal Home Loan Bank Stock— It is not practical to estimate the fair value of FHLB stock due to restrictions on its transferability. The fair value is estimated to be the carrying value, which is par. All transactions in capital stock of the FHLB Cincinnati are executed at par.

Deposits— The fair value of demand deposit accounts is the amount payable on demand at the reporting date. The fair value of fixed-maturity certificates of deposit is estimated using discounted cash flows and rates currently offered for deposits of similar remaining maturities.

Borrowed Funds— Estimated fair value for borrowed funds is estimated using discounted cash flows and rates currently charged for borrowings of similar remaining maturities.

Accrued Interest Receivable, Borrowers' Advances for Insurance and Taxes, and Principal, Interest and Related Escrow Owed on Loans Serviced— The carrying amount is a reasonable estimate of fair value.

Derivatives— Fair value is estimated based on the valuation techniques and inputs described earlier in this footnote.

14. DERIVATIVE INSTRUMENTS

The Company enters into interest rate swaps to add stability to interest expense and manage exposure to interest rate movements as part of an overall risk management strategy. For hedges of the Company's borrowing program, interest rate swaps designated as cash flow hedges involve the receipt of variable amounts from a counterparty in exchange for the Company making fixed payments. These derivatives are used to hedge the forecasted cash outflows associated with the Company's FHLB borrowings. At December 31, 2019 and September 30, 2019, the interest rate swaps used in the Company's asset/liability management strategy have weighted average terms of 3.5 years and 3.7 years and weighted average fixed-rate interest payments of 1.91% and 1.92%, respectively.

Cash flow hedges are initially assessed for effectiveness using regression analysis. The effective portion of changes in the fair value of derivatives designated and that qualify as cash flow hedges is recorded in OCI and is subsequently reclassified into earnings in the period that the hedged forecasted transaction affects earnings. Quarterly, a qualitative analysis is performed to monitor the ongoing effectiveness of the hedging instrument. All derivative positions were initially and continue to be highly effective at December 31, 2019.

The Company enters into forward commitments for the sale of mortgage loans principally to protect against the risk of adverse interest rate movements on net income. The Company recognizes the fair value of such contracts when the characteristics of those contracts meet the definition of a derivative. These derivatives are not designated in a hedging relationship; therefore, gains and losses are recognized immediately in the statement of income. There were no forward commitments for the sale of mortgage loans at December 31, 2019 or September 30, 2019.

In addition, the Company is party to derivative instruments when it enters into commitments to originate a portion of its loans, which when funded, are classified as held for sale. Such commitments are not designated in a hedging relationship; therefore, gains and losses are recognized immediately in the Consolidated Statement of Income.

The following tables provide the locations within the Consolidated Statements of Condition, notional values and fair values, at the reporting dates, for all derivative instruments.

	December 31, 2019		September 30, 2019	
	Notional Value	Fair Value	Notional Value	Fair Value
Derivatives designated as hedging instruments				
Cash flow hedges: Interest rate swaps				
Other Assets	\$ 1,000,000	\$ —	\$ 825,000	\$ —
Other Liabilities	1,800,000	—	1,925,000	—
Total cash flow hedges: Interest rate swaps	\$ 2,800,000	\$ —	\$ 2,750,000	\$ —
Derivatives not designated as hedging instruments				
Interest rate lock commitments				
Other Assets	\$ 9,284	\$ 54	\$ 10,358	\$ 44
Total interest rate lock commitments	\$ 9,284	\$ 54	\$ 10,358	\$ 44

The following tables present the net gains and losses recorded within the Consolidated Statements of Income and the Consolidated Statements of Comprehensive Income relating to derivative instruments.

	Location of Gain or (Loss) Recognized in Income	Three Months Ended	
		December 31,	
		2019	2018
Cash flow hedges			
Amount of gain/(loss) recognized	Other comprehensive income	\$ 20,218	\$ (31,013)
Amount of gain/(loss) reclassified from AOCI	Interest expense: Borrowed funds	971	2,939
Derivatives not designated as hedging instruments			
Interest rate lock commitments	Other non-interest income	\$ 10	\$ 79

The Company estimates that \$5,291 of the amounts reported in AOCI will be reclassified as a debit to interest expense during the twelve months ending December 31, 2020.

Derivatives contain an element of credit risk which arises from the possibility that the Company will incur a loss because a counterparty fails to meet its contractual obligations. The Company's exposure is limited to the replacement value of the contracts rather than the notional or principal amounts. Credit risk is minimized through counterparty margin payments, transaction limits and monitoring procedures. All of the Company's swap transactions are cleared through a registered clearing broker to a central clearing organization. The clearing organization establishes daily cash and upfront cash or securities margin requirements to cover potential exposure in the event of default. This process shifts the risk away from the counterparty, since the clearing organization acts as the middleman on each cleared transaction. For derivative transactions cleared through certain clearing parties, variation margin payments are recognized as settlements. The fair value of derivative instruments are presented on a gross basis, even when the derivative instruments are subject to master netting arrangements.

15. RECENT ACCOUNTING PRONOUNCEMENTS

Adopted during the three months ended December 31, 2019

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842). This guidance changed the accounting treatment of leases by requiring lessees to recognize operating leases on the balance sheet as lease assets (a right-of-use asset) and lease liabilities (a liability to make lease payments), measured on a discounted basis. The guidance requires both quantitative and qualitative disclosure regarding key information about the leasing arrangements. An accounting policy election to not recognize operating leases with terms of 12 months or less as assets and liabilities is permitted. This guidance is effective for fiscal years beginning after December 15, 2018, with early adoption permitted. ASU 2016-02 required entities to adopt the new lease standard using a modified retrospective approach. In July 2018, the FASB issued ASU 2018-11, Leases (Topic 842) Targeted Improvements, which provides entities with an additional (and optional) transition method to adopt the new lease standard. Under this new method, an entity initially applies the new leases standard at the adoption date and recognizes a cumulative-effect adjustment to the opening balance of retained earnings in the period of adoption. In January 2018, the FASB issued ASU 2018-01, Leases (Topic 842) Land Easement Practical Expedient, which allows entities to elect an optional transition practical expedient to not evaluate under Topic 842 land easements that existed or expired before the entity's adoption of Topic 842. In December 2018, the FASB issued ASU 2018-20, Leases (Topic 842) Narrow-Scope Improvements, which addresses lessor stakeholder questions regarding sales tax, certain lessor costs and the recognition of variable payments for contracts with lease and non-lease components. In March 2019, the FASB issued ASU 2019-01, Leases Codification Improvements, which addresses stakeholder questions regarding presentation of cash flows for sales type and direct financing leases, determining the fair value of the underlying asset by lessors that are not manufacturers or dealers, and contain transition disclosures.

The Company adopted ASU 2016-02 and all related amendments on October 1, 2019 utilizing the transition method described in ASU 2018-11. The Company elected the package of practical expedients that does not require reassessment of whether any expired or existing contracts are or contain leases, the lease classification for any expired or existing leases, or initial direct costs for any existing leases. The Company elected the practical expedient to combine both lease and nonlease components as a single component. The Company did not elect the hindsight practical expedient. The Company calculated the impact of adoption using the remaining minimum lease payments and remaining lease term for each contract that was identified as a lease, discounted at the incremental borrowing rate as of the adoption date. The guidance did not result in a cumulative-effect adjustment to beginning retained earnings. Refer to *Note 5. Leases*, for additional disclosures required by ASC 842.

Issued but not yet adopted as of December 31, 2019

In June 2016, the FASB issued ASU 2016-13, Financial Instruments - Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments. The amendments in this Update replace the existing incurred loss impairment methodology with a methodology that reflects the expected credit losses for the remaining life of the asset. This will require consideration of a broader range of information, including reasonably supportable forecasts, in the measurement of expected credit losses. The amendments expand disclosures of credit quality indicators, requiring disaggregation by year of origination (vintage). Additionally, credit losses on available for sale debt securities will be recognized as an allowance rather than a write-down, with reversals permitted as credit loss estimates decline. An entity will apply the amendments in this Update through a modified-retrospective approach, resulting in a cumulative-effect adjustment to retained earnings as of the beginning of the first reporting period in which the guidance is effective. For public business entities that are SEC filers, the amendments are effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. Early adoption is permitted. The Company intends to adopt this guidance effective October 1, 2020. In May 2019, the FASB issued ASU 2019-05, Financial Instruments - Credit Losses (Topic 326) Targeted Transition Relief, which addresses stakeholders' concerns by providing an option to irrevocably elect the fair value option for certain financial assets previously measured at amortized cost basis. Management has formed a working group comprised of associates from across the Company including accounting, risk management, and finance. This group has begun assessing the required changes to the credit loss estimation methodologies and systems, as well as additional data and resources that may be required to comply with this standard. Although the Company is still evaluating CECL, adoption of the standard is expected to increase the overall allowance for loan losses given the change from accounting for losses inherent in the loan portfolio to accounting for losses over the remaining life of the loans. The actual effect on the allowance for loan losses at the adoption date will be dependent upon the nature of the characteristics of the portfolio as well as the macroeconomic conditions and forecasts at that date.

In August 2018, the FASB issued ASU 2018-13, Fair Value Measurement (Topic 820), Disclosure Framework - Changes to the Disclosure Requirements for Fair Value Measurement. The amendments in this Update add, remove and modify the disclosure requirements on fair value measurements in Topic 820. The amendments in this Update are effective for all entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019. Early adoption is permitted upon issuance of this Update. The Company intends to adopt the amendments effective October 1, 2020. The Update is not expected to have a material impact on the Company's consolidated financial condition, results of operations, or disclosures.

In August 2018, the FASB issued ASU 2018-15, Internal-Use Software (Subtopic 350-40) - Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That is a Service Contract. Current GAAP does not specifically address the accounting for implementation costs of a hosting arrangement that is a service contract. Accordingly, the amendments in this Update improve current GAAP because they clarify that accounting and align the accounting for implementation costs for hosting arrangements, regardless of whether they convey a license to the hosted software. The amendments in this Update are effective for public business entities for fiscal years beginning after December 15, 2019, and interim periods within those fiscal years. Early adoption of the amendments in this Update is permitted, including adoption in any interim period, for all entities. The Company intends to adopt the amendments effective October 1, 2020. Management is currently assessing the impact the Update will have on the Company's disclosures.

In April 2019, the FASB issued ASU 2019-04, Codification Improvements to Updates 2016-01, 2016-13 and 2017-12. The Company early adopted the amendments related to Updates 2016-01 and 2017-12 effective July 1, 2019. The amendments related to Update 2016-13 clarify the scope of the credit losses standard and address issues related to accrued interest and recoveries. The amendments are not expected to have a material impact on the Company's consolidated financial condition, results of operation, or disclosure. The Company intends to adopt the credit loss standard amendments concurrently with Update 2016-13 on October 1, 2020.

The Company has determined that all other recently issued accounting pronouncements will not have a material impact on the Company's consolidated financial statements or do not apply to its operations.

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

Forward Looking Statements

This report contains forward-looking statements, which can be identified by the use of such words as estimate, project, believe, intend, anticipate, plan, seek, expect and similar expressions. These forward-looking statements include, among other things:

- statements of our goals, intentions and expectations;
- statements regarding our business plans and prospects and growth and operating strategies;
- statements concerning trends in our provision for loan losses and charge-offs;
- statements regarding the trends in factors affecting our financial condition and results of operations, including asset quality of our loan and investment portfolios; and
- estimates of our risks and future costs and benefits.

These forward-looking statements are subject to significant risks, assumptions and uncertainties, including, among other things, the following important factors that could affect the actual outcome of future events:

- significantly increased competition among depository and other financial institutions;
- inflation and changes in the interest rate environment that reduce our interest margins or reduce the fair value of financial instruments;
- general economic conditions, either globally, nationally or in our market areas, including employment prospects, real estate values and conditions that are worse than expected;
- the strength or weakness of the real estate markets and of the consumer and commercial credit sectors and its impact on the credit quality of our loans and other assets, and changes in estimates of the allowance for loan losses;
- decreased demand for our products and services and lower revenue and earnings because of a recession or other events;
- changes in consumer spending, borrowing and savings habits;
- adverse changes and volatility in the securities markets, credit markets or real estate markets;
- legislative or regulatory changes that adversely affect our business, including changes in regulatory costs and capital requirements and changes related to our ability to pay dividends and the ability of Third Federal Savings, MHC to waive dividends;
- changes in accounting policies and practices, as may be adopted by the bank regulatory agencies, the Financial Accounting Standards Board or the Public Company Accounting Oversight Board;
- the adoption of implementing regulations by a number of different regulatory bodies, and uncertainty in the exact nature, extent and timing of such regulations and the impact they will have on us;
- our ability to enter new markets successfully and take advantage of growth opportunities, and the possible short-term dilutive effect of potential acquisitions or de novo branches, if any;
- future adverse developments concerning Fannie Mae or Freddie Mac;
- changes in monetary and fiscal policy of the U.S. Government, including policies of the U.S. Treasury and the FRS and changes in the level of government support of housing finance;
- the continuing governmental efforts to restructure the U.S. financial and regulatory system;
- the ability of the U.S. Government to remain open, function properly and manage federal debt limits;
- changes in policy and/or assessment rates of taxing authorities that adversely affect us or our customers;
- changes in accounting and tax estimates;
- changes in our organization, or compensation and benefit plans and changes in expense trends (including, but not limited to trends affecting non-performing assets, charge-offs and provisions for loan losses);
- the inability of third-party providers to perform their obligations to us;
- a slowing or failure of the prevailing economic recovery; and
- cyber attacks, computer viruses and other technological risks that may breach the security of our websites or other systems to obtain unauthorized access to confidential information, destroy data or disable our systems.

Because of these and other uncertainties, our actual future results may be materially different from the results indicated by any forward-looking statements. Any forward-looking statement made by us in this report speaks only as of the date on which it is made. We undertake no obligation to publicly update any forward-looking statements, whether as a result of new information, future developments or otherwise, except as may be required by law. Please see **Part II - Other Information Item 1A. Risk Factors** for a discussion of certain risks related to our business.

Overview

Our business strategy is to operate as a well-capitalized and profitable financial institution dedicated to providing exceptional personal service to our customers.

Since being organized in 1938, we grew to become, at the time of our initial public offering of stock in April 2007, the nation's largest mutually-owned savings and loan association based on total assets. We credit our success to our continued emphasis on our primary values: "Love, Trust, Respect, and a Commitment to Excellence, along with Having Fun." Our values are reflected in the design and pricing of our loan and deposit products, as described below. Our values are further reflected in a long-term revitalization program encompassing the three-mile corridor of the Broadway-Slavic Village neighborhood in Cleveland, Ohio where our main office was established and continues to be located and where the educational programs we have established and/or supported are located. We intend to continue to adhere to our primary values and to support our customers and the communities in which we operate.

Management believes that the following matters are those most critical to our success: (1) controlling our interest rate risk exposure; (2) monitoring and limiting our credit risk; (3) maintaining access to adequate liquidity and diverse funding sources to support our growth; and (4) monitoring and controlling our operating expenses.

Controlling Our Interest Rate Risk Exposure. Historically, our greatest risk has been our exposure to changes in interest rates. When we hold longer-term, fixed-rate assets, funded by liabilities with shorter re-pricing characteristics, we are exposed to potentially adverse impacts from changing interest rates, and most notably rising interest rates. Generally, and particularly over extended periods of time that encompass full economic cycles, interest rates associated with longer-term assets, like fixed-rate mortgages, have been higher than interest rates associated with shorter-term funding sources, like deposits. This difference has been an important component of our net interest income and is fundamental to our operations. We manage the risk of holding longer-term, fixed-rate mortgage assets primarily by maintaining regulatory capital in excess of levels required to be well capitalized, by promoting adjustable-rate loans and shorter-term fixed-rate loans, by marketing home equity lines of credit, which carry an adjustable rate of interest indexed to the prime rate and by opportunistically extending the duration of our funding sources.

Levels of Regulatory Capital

At December 31, 2019, the Company's Tier 1 (leverage) capital totaled \$1.75 billion, or 11.99% of net average assets and 21.56% of risk-weighted assets, while the Association's Tier 1 (leverage) capital totaled \$1.48 billion, or 10.19% of net average assets and 18.31% of risk-weighted assets. Each of these measures was more than twice the requirements currently in effect for the Association for designation as "well capitalized" under regulatory prompt corrective action provisions, which set minimum levels of 5.00% of net average assets and 8.00% of risk-weighted assets. Refer to the *Liquidity and Capital Resources* section of this Item 2 for additional discussion regarding regulatory capital requirements.

Promotion of Adjustable-Rate Loans and Shorter-Term Fixed-Rate Loans

We market an adjustable-rate mortgage loan that provides us with improved interest rate risk characteristics when compared to a 30-year, fixed-rate mortgage loan. Our "Smart Rate" adjustable-rate mortgage offers borrowers an interest rate lower than that of a 30-year, fixed-rate loan. The interest rate of the Smart Rate mortgage is locked for three or five years then resets annually. The Smart Rate mortgage contains a feature to re-lock the rate an unlimited number of times at our then-current interest rate and fee schedule, for another three or five years (which must be the same as the original lock period) without having to complete a full refinance transaction. Re-lock eligibility is subject to a satisfactory payment performance history by the borrower (current at the time of re-lock, and no foreclosures or bankruptcies since the Smart Rate application was taken). In addition to a satisfactory payment history, re-lock eligibility requires that the property continues to be the borrower's primary residence. The loan term cannot be extended in connection with a re-lock nor can new funds be advanced. All interest rate caps and floors remain as originated.

We also offer a ten-year, fully amortizing fixed-rate, first mortgage loan. The ten-year, fixed-rate loan has a more desirable interest rate risk profile when compared to loans with fixed-rate terms of 15 to 30 years and can help to more effectively manage interest rate risk exposure, yet provides our borrowers with the certainty of a fixed interest rate throughout the life of the obligation.

The following tables set forth our first mortgage loan production and balances segregated by loan structure at origination.

	For the Three Months Ended December 31, 2019		For the Three Months Ended December 31, 2018	
	Amount	Percent	Amount	Percent
(Dollars in thousands)				
First Mortgage Loan Originations:				
ARM (all Smart Rate) production	\$ 303,720	40.5%	\$ 179,957	46.9%
Fixed-rate production:				
Terms less than or equal to 10 years	63,068	8.4	21,869	5.7
Terms greater than 10 years	383,795	51.1	182,013	47.4
Total fixed-rate production	446,863	59.5	203,882	53.1
Total First Mortgage Loan Originations	\$ 750,583	100.0%	\$ 383,839	100.0%

	December 31, 2019		September 30, 2019	
	Amount	Percent	Amount	Percent
(Dollars in thousands)				
Balance of Residential Mortgage Loans Held For Investment:				
ARM (primarily Smart Rate) Loans	\$ 5,129,610	45.7%	\$ 5,063,010	46.1%
Fixed-rate:				
Terms less than or equal to 10 years	1,435,814	12.8	1,484,403	13.5
Terms greater than 10 years	4,649,143	41.5	4,440,553	40.4
Total fixed-rate	6,084,957	54.3	5,924,956	53.9
Total Residential Mortgage Loans Held For Investment	\$ 11,214,567	100.0%	\$ 10,987,966	100.0%

The following table sets forth the balances as of December 31, 2019 for all ARM loans segregated by the next scheduled interest rate reset date.

<u>During the Fiscal Years Ending September 30,</u>	Current Balance of ARM Loans Scheduled for Interest Rate Reset
	(In thousands)
2020	\$ 302,223
2021	1,101,323
2022	1,397,858
2023	1,069,859
2024	511,129
2025	747,218
Total	\$ 5,129,610

At December 31, 2019 and September 30, 2019, mortgage loans held for sale, all of which were long-term, fixed-rate first mortgage loans and all of which were held for sale to Fannie Mae, totaled \$9.6 million and \$3.7 million, respectively.

Loan Portfolio Yield

The following tables set forth the balance and interest yield as of December 31, 2019 for the portfolio of loans held for investment, by type of loan, structure and geographic location.

	December 31, 2019		
	Balance	Percent	Yield
(Dollars in thousands)			
Total Loans:			
Fixed Rate			
Terms less than or equal to 10 years	\$ 1,435,814	10.6%	2.95%
Terms greater than 10 years	4,649,143	34.5%	4.01%
Total Fixed-Rate loans	6,084,957	45.1%	3.76%
ARMs	5,129,610	38.0%	3.16%
Home Equity Loans and Lines of Credit	2,221,380	16.5%	3.97%
Construction and Other Loans	54,304	0.4%	3.87%
Total Loans Receivable, net	\$ 13,490,251	100.0%	3.57%

	December 31, 2019			
	Balance	Fixed Rate Balance	Percent	Yield
(Dollars in thousands)				
Residential Mortgage Loans				
Ohio	\$ 6,457,058	\$ 4,575,776	47.9%	3.68%
Florida	1,772,854	711,182	13.1%	3.46%
Other	2,984,655	797,999	22.1%	3.10%
Total Residential Mortgage Loans	11,214,567	6,084,957	83.1%	3.49%
Home Equity Loans and Lines of Credit				
Ohio	676,085	55,216	5.0%	4.00%
Florida	426,479	35,294	3.2%	3.90%
California	365,474	22,118	2.7%	4.02%
Other	753,342	16,917	5.6%	3.96%
Total Home Equity Loans and Lines of Credit	2,221,380	129,545	16.5%	3.97%
Construction and Other Loans	54,304	54,304	0.4%	3.87%
Total Loans Receivable, net	\$ 13,490,251	\$ 6,268,806	100.0%	3.57%

Marketing Home Equity Lines of Credit

We actively market home equity lines of credit, which carry an adjustable rate of interest indexed to the prime rate which provides interest rate sensitivity to that portion of our assets and is a meaningful strategy to manage our interest rate risk profile. At December 31, 2019, the principal balance of home equity lines of credit totaled \$1.83 billion. Our home equity lending is discussed in the *Allowance for Loan Losses* section of the *Critical Accounting Policies* that follows this *Overview*.

Extending the Duration of Funding Sources

As a complement to our strategies to shorten the duration of our interest earning assets, as described above, we also seek to lengthen the duration of our interest bearing funding sources. These efforts include monitoring the relative costs of alternative funding sources such as retail deposits, brokered certificates of deposit, longer-term (e.g. four to six years) fixed rate advances from the FHLB of Cincinnati, and shorter-term (e.g. three months) advances from the FHLB of Cincinnati, the durations of which are extended by correlated interest rate exchange contracts. Each funding alternative is monitored and evaluated based on its effective interest payment rate, options exercisable by the creditor (early withdrawal, right to call, etc.), and collateral requirements. The interest payment rate is a function of market influences that are specific to the nuances and market competitiveness/breadth of each funding source. Generally, early withdrawal options are available to our retail CD customers but not to holders of brokered CDs; issuer call options are not provided on our advances from the FHLB of Cincinnati; and we are not subject to early termination options with respect to our interest rate exchange contracts. Additionally, collateral pledges are not provided with respect to our retail CDs or our brokered CDs, but are required for our advances from the FHLB of Cincinnati as well as for our interest rate exchange contracts.

During the three months ended December 31, 2019, the balance of deposits increased \$234.5 million, which was comprised of a \$240.9 million increase in the balance of customer retail deposits, partially offset by a \$6.4 million decrease in the balance of brokered CDs (which is inclusive of acquisition costs and subsequent amortization). Additionally, during the three months ended December 31, 2019, we decreased the balance of our short-term advances from the FHLB of Cincinnati by \$100 million; and added \$150 million of new, four- to six-year advances from the FHLB of Cincinnati; and we added \$50 million of new, shorter-term advances from the FHLB of Cincinnati that were matched/correlated to interest rate exchange contracts that extended the effective durations of those shorter-term advances to approximately five to eight years at inception. Interest rate swaps are discussed later in *Part 1, Item 3. Quantitative and Qualitative Disclosures About Market Risk*.

During the three months ended December 31, 2019, these funding source modifications facilitated asset growth of \$263.8 million and funded stock repurchases of \$0.4 million, dividends of \$13.4 million and scheduled repayments of long-term borrowed funds of \$112.2 million.

Other Interest Rate Risk Management Tools

We also manage interest rate risk by selectively selling a small portion of our long-term, fixed-rate mortgage loans in the secondary market. Prior to fiscal 2010, this strategy was used to a greater extent to manage our interest rate risk. At December 31, 2019, we serviced \$1.69 billion of loans for others, of which \$885 million was sold in the secondary market prior to fiscal 2010. While the sales of first mortgage loans remain strategically important for us, since fiscal 2010, they have played only a minor role in our management of interest rate risk. We can also manage interest rate risk by selling non-Fannie Mae compliant mortgage loans to private investors, although those transactions are dependent upon favorable market conditions, including motivated private investors, and involve more complicated negotiations and longer settlement timelines. Loan sales are discussed later in this *Part 1, Item 2. under the heading Liquidity and Capital Resources*, and in *Part 1, Item 3. Quantitative and Qualitative Disclosures About Market Risk*.

Notwithstanding our efforts to manage interest rate risk, should a rapid and substantial increase occur in general market interest rates, or an extended period of a flat or inverted yield curve market persists, it is expected that, prospectively and particularly over a multi-year time horizon, the level of our net interest income would be adversely impacted.

Monitoring and Limiting Our Credit Risk. While, historically, we had been successful in limiting our credit risk exposure by generally imposing high credit standards with respect to lending, the memory of the 2008 housing market collapse and financial crisis is a constant reminder to focus on credit risk. In response to the evolving economic landscape, we continuously revise and update our quarterly analysis and evaluation procedures, as needed, for each category of our lending with the objective of identifying and recognizing all appropriate credit impairments. At December 31, 2019, 91% of our assets consisted of residential real estate loans (both “held for sale” and “held for investment”) and home equity loans and lines of credit, which were originated predominantly to borrowers in Ohio and Florida. Our analytic procedures and evaluations include specific reviews of all home equity loans and lines of credit that become 90 or more days past due, as well as specific reviews of all first mortgage loans that become 180 or more days past due. We transfer performing home equity lines of credit subordinate to first mortgages delinquent greater than 90 days to non-accrual status. We also charge-off performing loans to collateral value and classify those loans as non-accrual within 60 days of notification of all borrowers filing Chapter 7 bankruptcy, that have not reaffirmed or been dismissed, regardless of how long the loans have been performing. Loans where at least one borrower has been discharged of their obligation in Chapter 7 bankruptcy are classified as TDRs. At December 31, 2019, \$20.9 million of loans in Chapter 7 bankruptcy status with no other modification to terms were included in total TDRs. At December 31, 2019, the recorded investment in non-accrual status loans included \$24.1 million of performing loans in Chapter 7 bankruptcy status, of which \$23.4 million were also reported as TDRs.

In an effort to limit our credit risk exposure and improve the credit performance of new customers, since 2009, we have tightened our credit criteria in evaluating a borrower's ability to successfully fulfill its repayment obligation, revised the design of many of our loan products to require higher borrower down-payments, limited the products available for condominiums and eliminated certain product features (such as interest-only, adjustable-rate loans and loans above certain LTV ratios). The delinquency level related to loan originations prior to 2009, compared to originations in 2009 and after, reflects the higher credit standards to which we have subjected all new originations. As of December 31, 2019, loans originated prior to 2009 had a balance of \$766.2 million, of which \$22.0 million, or 2.9%, were delinquent, while loans originated in 2009 and after had a balance of \$12.75 billion, of which \$12.0 million, or 0.1%, were delinquent.

One aspect of our credit risk concern relates to high concentrations of our loans that are secured by residential real estate in specific states, particularly Ohio and Florida, in light of the difficulties that arose in connection with the 2008 housing crisis with respect to the real estate markets in those two states. At December 31, 2019, approximately 57% and 16% of the combined total of our residential Core and construction loans held for investment and approximately 30% and 19% of our home equity loans and lines of credit were secured by properties in Ohio and Florida, respectively. In an effort to moderate the concentration of our credit risk exposure in individual states, particularly Ohio and Florida, we have utilized direct mail marketing, our internet site and our customer service call center to extend our lending activities to other attractive geographic locations. Currently, in addition to Ohio and Florida, we are actively lending in 23 other states and the District of Columbia, and as a result of that activity, the concentration ratios of the combined total of our residential, Core and construction loans held for investment in Ohio and Florida have trended downward from their September 30, 2010 levels when the concentrations were 79.1% in Ohio and 19.0% in Florida. Of the total mortgage and home equity loan originations for the three months ended December 31, 2019, 23.1% are secured by properties in states other than Ohio or Florida.

Our residential Home Today loans are another area of credit risk concern as the majority of these loans were originated under less stringent underwriting and credit standards than our residential Core portfolio. Although we no longer originate loans under this program and the principal balance in these loans had declined to \$82.7 million at December 31, 2019, and constituted only 0.6% of our total "held for investment" loan portfolio balance, they comprised 19.5% and 21.5% of our 90 days or greater delinquencies and our total delinquencies, respectively, at that date. At December 31, 2019, approximately 95% and 5% of our residential Home Today loans were secured by properties in Ohio and Florida, respectively. At December 31, 2019, the percentages of those loans delinquent 30 days or more in Ohio and Florida were 9.0% and 7.3%, respectively. We attempted to manage our Home Today credit risk by requiring private mortgage insurance for some loans. At December 31, 2019, 13.0% of Home Today loans included private mortgage insurance coverage. From a peak recorded investment of \$306.6 million at December 31, 2007, the total recorded investment of the Home Today portfolio has declined to \$82.3 million at December 31, 2019. Since the vast majority of Home Today loans were originated prior to March 2009 and we are no longer originating loans under our Home Today program, the Home Today portfolio will continue to decline in balance, primarily due to contractual amortization. To supplant the Home Today product and to continue to meet the credit needs of our customers and the communities that we serve, we have offered Fannie Mae eligible, Home Ready loans since fiscal 2016. These loans are originated in accordance with Fannie Mae's underwriting standards. While we retain the servicing rights related to these loans, the loans, along with the credit risk associated therewith, are securitized/sold to Fannie Mae.

Maintaining Access to Adequate Liquidity and Diverse Funding Sources to Support our Growth. For most insured depositories, customer and community confidence are critical to their ability to maintain access to adequate liquidity and to conduct business in an orderly manner. We believe that a well capitalized institution is one of the most important factors in nurturing customer and community confidence. Accordingly, we have managed the pace of our growth in a manner that reflects our emphasis on high capital levels. At December 31, 2019, the Association's ratio of Tier 1 (leverage) capital to net average assets (a basic industry measure that deems 5.00% or above to represent a "well capitalized" status) was 10.19%. The Association's Tier 1 (leverage) capital ratio is lower at December 31, 2019 than its ratio at September 30, 2019, which was 10.54%, due primarily to a \$57 million cash dividend payment that the Association made to the Company, its sole shareholder, in December 2019 that reduced the Association's Tier 1 (leverage) capital ratio by an estimated 39 basis points. Because of its intercompany nature, this dividend payment did not impact the Company's consolidated capital ratios which are reported in the *Liquidity and Capital Resources* section of this Item 2. We expect to continue to remain a well capitalized institution.

In managing its level of liquidity, the Company monitors available funding sources, which include attracting new deposits (including brokered CDs), borrowings from others, the conversion of assets to cash and the generation of funds through profitable operations. The Company has traditionally relied on retail deposits as its primary means in meeting its funding needs. At December 31, 2019, deposits totaled \$9.00 billion (including \$501.4 million of brokered CDs), while borrowings totaled \$3.89 billion and borrowers' advances and servicing escrows totaled \$130.9 million, combined. In evaluating funding sources, we consider many factors, including cost, collateral, duration and optionality, current availability, expected sustainability, impact on operations and capital levels.

To attract deposits, we offer our customers attractive rates of interest on our deposit products. Our deposit products typically offer rates that are highly competitive with the rates on similar products offered by other financial institutions. We intend to continue this practice, subject to market conditions.

We preserve the availability of alternative funding sources through various mechanisms. First, by maintaining high capital levels, we retain the flexibility to increase our balance sheet size without jeopardizing our capital adequacy. Effectively, this permits us to increase the rates that we offer on our deposit products thereby attracting more potential customers. Second, we pledge available real estate mortgage loans and investment securities with the FHLB of Cincinnati and the FRB-Cleveland. At December 31, 2019, these collateral pledge support arrangements provided the Association with the ability to immediately borrow an additional \$73.1 million from the FHLB of Cincinnati and \$41.7 million from the FRB-Cleveland Discount Window. From the perspective of collateral value securing FHLB of Cincinnati advances, our capacity limit for additional borrowings beyond the balance outstanding at December 31, 2019 was \$4.27 billion, subject to satisfaction of the FHLB of Cincinnati common stock ownership requirement. To satisfy the common stock ownership requirement for the maximum limit of borrowing, we would need to increase our ownership of FHLB of Cincinnati common stock by an additional \$85.4 million. Third, we invest in high quality marketable securities that exhibit limited market price variability, and to the extent that they are not needed as collateral for borrowings, can be sold in the institutional market and converted to cash. At December 31, 2019, our investment securities portfolio totaled \$554.0 million. Finally, cash flows from operating activities have been a regular source of funds. During the three months ended December 31, 2019 and 2018, cash flows from operations provided \$29.4 million and \$34.4 million, respectively.

First mortgage loans (primarily fixed-rate, mortgage refinances with terms of 15 years or more, and Home Ready) originated under the revised procedures are eligible for sale to Fannie Mae either as whole loans or within mortgage-backed securities. We expect that certain loan types (i.e. our Smart Rate adjustable-rate loans, home purchase fixed-rate loans and 10-year fixed-rate loans) will continue to be originated under our legacy procedures, which are not eligible for sale to Fannie Mae. For loans that are not originated under the revised (Fannie Mae) procedures, the Association's ability to reduce interest rate risk via loan sales is limited to those loans that have established payment histories, strong borrower credit profiles and are supported by adequate collateral values that meet the requirements of the FHLB's Mortgage Purchase Program or of private third-party investors. At December 31, 2019, \$9.6 million of agency eligible, long-term, fixed-rate first mortgage loans were classified as "held for sale." During the three months ended December 31, 2019, \$9.6 million of agency-compliant Home Ready loans and \$99.9 million of long-term, fixed-rate, agency-compliant, non-Home Ready first mortgage loans were sold to Fannie Mae. Additionally, \$99.0 million of fixed-rate loans were sold in a single bulk sale to a private investor.

Overall, while customer and community confidence can never be assured, the Company believes that its liquidity is adequate and that it has access to adequate alternative funding sources.

Monitoring and Controlling Our Operating Expenses. We continue to focus on managing operating expenses. Our ratio of annualized non-interest expense to average assets was 1.30% for the three months ended December 31, 2019 and 1.36% for the three months ended December 31, 2018. As of December 31, 2019, our average assets per full-time employee and our average deposits per full-time employee were \$13.7 million and \$8.3 million, respectively. We believe that each of these measures compares favorably with industry averages. Our relatively high average of deposits (exclusive of brokered CDs) held at our branch offices (\$229.7 million per branch office as of December 31, 2019) contributes to our expense management efforts by limiting the overhead costs of serving our customers. We will continue our efforts to control operating expenses as we grow our business.

Critical Accounting Policies

Critical accounting policies are defined as those that involve significant judgments and uncertainties, and could potentially give rise to materially different results under different assumptions and conditions. We believe that the most critical accounting policies upon which our financial condition and results of operations depend, and which involve the most complex subjective decisions or assessments, are our policies with respect to our allowance for loan losses, income taxes and pension benefits.

Allowance for Loan Losses. We provide for loan losses based on the allowance method. Accordingly, all loan losses are charged to, and all recoveries are credited to, the related allowance. Additions to the allowance for loan losses are provided by charges to income based on various factors which, in our judgment, deserve current recognition in estimating probable losses. We regularly review the loan portfolio and make provisions (or recapture credits) for loan losses in order to maintain the allowance for loan losses in accordance with U.S. GAAP. Our allowance for loan losses consists of two components:

- (1) individual valuation allowances (IVAs) established for any impaired loans dependent on cash flows, such as performing TDRs, and IVAs related to a portion of the allowance on loans individually reviewed that represents further deterioration in the fair value of the collateral not yet identified as uncollectible; and
- (2) general valuation allowances (GVAs), which are comprised of quantitative GVAs, which are general allowances for loan losses for each loan type based on historical loan loss experience and qualitative GVAs, which are adjustments to the quantitative GVAs, maintained to cover uncertainties that affect our estimate of incurred probable losses for each loan type.

The qualitative GVAs expand our ability to identify and estimate probable losses and are based on our evaluation of the following factors, some of which are consistent with factors that impact the determination of quantitative GVAs. For example, delinquency statistics (both current and historical) are used in developing the quantitative GVAs while the trending of the delinquency statistics is considered and evaluated in the determination of the qualitative GVAs. Factors impacting the determination of qualitative GVAs include:

- changes in lending policies and procedures including underwriting standards, collection, charge-off or recovery practices;
- changes in national, regional, and local economic and business conditions and trends including treasury yields, housing market factors and trends, such as the status of loans in foreclosure, real estate in judgment and real estate owned, and unemployment statistics and trends;
- changes in the nature and volume of the portfolios including home equity lines of credit nearing the end of the draw period and adjustable-rate mortgage loans nearing a rate reset;
- changes in the experience, ability or depth of lending management;
- changes in the volume or severity of past due loans, volume of non-accrual loans, or the volume and severity of adversely classified loans including the trending of delinquency statistics (both current and historical), historical loan loss experience and trends, the frequency and magnitude of multiple restructurings of loans previously the subject of TDRs, and uncertainty surrounding borrowers' ability to recover from temporary hardships for which short-term loan restructurings are granted;
- changes in the quality of the loan review system;
- changes in the value of the underlying collateral including asset disposition loss statistics (both current and historical) and the trending of those statistics, and additional charge-offs on individually reviewed loans;
- existence of any concentrations of credit; and
- effect of other external factors such as competition, market interest rate changes or legal and regulatory requirements including market conditions and regulatory directives that impact the entire financial services industry.

When loan restructurings qualify as TDRs and the loans are performing according to the terms of the restructuring, we record an IVA based on the present value of expected future cash flows, which includes a factor for potential subsequent defaults, discounted at the effective interest rate of the original loan contract. Potential defaults are distinguished from multiple restructurings as borrowers who default are generally not eligible for subsequent restructurings. At December 31, 2019, the balance of such individual valuation allowances was \$13.4 million. In instances when loans require multiple restructurings, additional valuation allowances may be required. The new valuation allowance on a loan that has multiple restructurings is calculated based on the present value of the expected cash flows, discounted at the effective interest rate of the original loan contract, considering the new terms of the restructured agreement. Due to the immaterial amount of this exposure to date, we continue to capture this exposure as a component of our qualitative GVA evaluation. The significance of this exposure will be monitored and, if warranted, we will enhance our loan loss methodology to include a new default factor (developed to reflect the estimated impact to the balance of the allowance for loan losses that will occur as a result of subsequent future restructurings) that will be assessed against all loans reviewed collectively. If new default factors are implemented, the qualitative GVA methodology will be adjusted to preclude duplicative loss consideration.

Home equity loans and lines of credit generally have higher credit risk than traditional residential mortgage loans. These loans and credit lines are usually in a second lien position and when combined with the first mortgage, result in generally higher overall loan-to-value ratios. In a stressed housing market with high delinquencies and decreasing housing prices, these higher loan-to-value ratios represent a greater risk of loss to the Company. A borrower with more equity in the property has a vested interest in keeping the loan current when compared to a borrower with little or no equity in the property. In light of the past weakness in the housing market and uncertainty with respect to future employment levels and economic prospects, we conduct an expanded loan level evaluation of our home equity loans and lines of credit, including bridge loans, which are delinquent 90 days or more. This expanded evaluation is in addition to our traditional evaluation procedures. Considering the review process and our suspension program, no allowance is deemed necessary for our unfunded commitments on this

portfolio. Our home equity loans and lines of credit portfolio continues to comprise a significant portion of our gross charge-offs. At December 31, 2019, we had a recorded investment of \$2.25 billion in home equity loans and equity lines of credit outstanding, of which \$5.2 million, or 0.2% were delinquent 90 days or more.

We evaluate the allowance for loan losses based upon the combined total of the quantitative and qualitative GVAs and IVAs. We periodically evaluate the carrying value of loans and the allowance is adjusted accordingly. While we use the best information available to make evaluations, future additions to the allowance may be necessary based on unforeseen changes in loan quality and economic conditions.

The following tables set forth the allowance for loan losses allocated by loan category, the percent of allowance in each category to the total allowance, and the percent of loans in each category to total loans at the dates indicated. The allowance for loan losses allocated to each category is not necessarily indicative of future losses in any particular category and does not restrict the use of the allowance to absorb losses in other categories.

	December 31, 2019		
	Amount	Percent of Allowance to Total Allowance	Percent of Loans in Category to Total Loans
(Dollars in thousands)			
Real estate loans:			
Residential Core	\$ 18,312	49.1%	82.5%
Residential Home Today	4,232	11.4	0.6
Home equity loans and lines of credit	14,744	39.5	16.5
Construction	4	—	0.4
Total allowance	<u>\$ 37,292</u>	<u>100.0%</u>	<u>100.0%</u>

	September 30, 2019			December 31, 2018		
	Amount	Percent of Allowance to Total Allowance	Percent of Loans in Category to Total Loans	Amount	Percent of Allowance to Total Allowance	Percent of Loans in Category to Total Loans
(Dollars in thousands)						
Real estate loans:						
Residential Core	\$ 19,753	50.8%	82.5%	\$ 19,165	45.7%	84.2%
Residential Home Today	4,209	10.8	0.6	3,748	8.9	0.7
Home equity loans and lines of credit	14,946	38.4	16.5	19,021	45.4	14.6
Construction	5	—	0.4	4	—	0.5
Total allowance	<u>\$ 38,913</u>	<u>100.0%</u>	<u>100.0%</u>	<u>\$ 41,938</u>	<u>100.0%</u>	<u>100.0%</u>

The following table sets forth activity in our allowance for loan losses segregated by geographic location for the periods indicated. The majority of our construction loan portfolio is secured by properties located in Ohio and the balances of other loans are considered immaterial, therefore neither was segregated.

	As of and For the Three Months Ended December 31,	
	2019	2018
(Dollars in thousands)		
Allowance balance (beginning of the period)	\$ 38,913	\$ 42,418
Charge-offs:		
Real estate loans:		
Residential Core		
Ohio	274	243
Florida	196	—
Other	15	—
Total Residential Core	485	243
Residential Home Today		
Ohio	359	241
Total Residential Home Today	359	241
Home equity loans and lines of credit		
Ohio	244	290
Florida	352	445
California	—	22
Other	149	86
Total Home equity loans and lines of credit	745	843
Total charge-offs	1,589	1,327
Recoveries:		
Real estate loans:		
Residential Core	810	211
Residential Home Today	527	468
Home equity loans and lines of credit	1,631	2,168
Total recoveries	2,968	2,847
Net recoveries (charge-offs)	1,379	1,520
Provision (Credit) for loan losses	(3,000)	(2,000)
Allowance balance (end of the period)	\$ 37,292	\$ 41,938
Ratios:		
Net recoveries (charge-offs) to average loans outstanding (annualized)	0.04%	0.05%
Allowance for loan losses to non-accrual loans at end of the period	61.84%	54.48%
Allowance for loan losses to the total recorded investment in loans at end of the period	0.28%	0.32%

Net recoveries continued, totaling \$1.4 million during the three months ended December 31, 2019 compared to \$1.5 million during the three months ended December 31, 2018. We reported net recoveries for eleven out of the last twelve quarters, primarily due to improvements in the values of properties used to secure loans that were fully or partially charged off after the 2008 collapse of the housing market. Charge-offs are recognized on loans identified as collateral dependent and subject to individual review when the collateral value does not sufficiently support full repayment of the obligation. Recoveries are recognized on previously charged off loans as borrowers perform their repayment obligations or as loans with improved collateral positions reach final resolution.

With the exception of the Home equity loans and lines of credit portfolio, charge-offs increased slightly, but remained low, during the three months months ended December 31, 2019 when compared to the three months months ended December 31, 2018. We continue to evaluate loans becoming delinquent for potential losses and record provisions for the

estimate of potential losses of those loans. We expect a moderate level of charge-offs to continue as delinquent loans are resolved in the future and uncollected balances are charged against the allowance.

During the three months ended December 31, 2019, the total allowance for loan losses decreased \$1.6 million, to \$37.3 million from \$38.9 million at September 30, 2019, as we recorded a \$3.0 million credit for loan losses, and had net recoveries of \$1.4 million. The allowance for loan losses related to loans evaluated collectively decreased by \$1.7 million during the three months ended December 31, 2019, and the allowance for loan losses related to loans evaluated individually remained relatively flat. Refer to the "*Activity in the Allowance for Loan Losses*" and "*Analysis of the Allowance for Loan Losses*" tables in *Note 4 of the Notes to the Unaudited Interim Consolidated Financial Statements* for more information. Other than the less significant construction and other loans segments, changes during the three months ended December 31, 2019 in the balances of the GVAs, excluding changes in IVAs, related to the significant loan segments are described as follows:

- **Residential Core** – The recorded investment of this segment increased 2.1%, or \$230.1 million, while its total allowance decreased 7.3% or \$1.4 million. The portion of allowance for this segment that was determined by evaluating groups of loans collectively (i.e. those loans that were not individually evaluated), decreased \$1.4 million, or 11.1%, from \$12.7 million at September 30, 2019, to \$11.3 million at December 31, 2019. The ratio of this portion of the allowance to the total balance of loans in this segment that were evaluated collectively, decreased 0.02% to 0.10% at December 31, 2019 from 0.12% at September 30, 2019. Total delinquencies decreased 3.6% to \$17.9 million at December 31, 2019 from \$18.5 million at September 30, 2019. Delinquencies greater than 90 days slightly increased by 5.0% to \$8.1 million at December 31, 2019 from \$7.7 million at September 30, 2019. There were net recoveries of \$325 thousand for the quarter ended December 31, 2019 compared to net charge-offs of \$32 thousand during the quarter ended December 31, 2018. The decrease in the ratio of the allowance reflected the improved delinquencies and increase in net recoveries when compared to the prior period. The credit profile of this portfolio segment remained strong during the quarter due to the addition of high credit quality residential first mortgage loans.
- **Residential Home Today** – The recorded investment of this segment decreased 2.4%, or \$2.3 million, as we are no longer originating loans under the Home Today program. The total allowance for this segment remained constant at \$4.2 million. Similarly, the portion of allowance that was determined by evaluating groups of loans collectively remained at \$1.8 million during the quarter ended December 31, 2019. The ratio of this portion of the allowance to the total balance of loans in this segment that were evaluated collectively, slightly increased to 3.9% at December 31, 2019 from 3.8% at September 30, 2019. Total delinquencies increased to \$7.3 million at December 31, 2019 from \$6.9 million at September 30, 2019. Delinquencies greater than 90 days increased 21.8% to \$3.2 million from \$2.6 million at September 30, 2019. Net recoveries of \$0.2 million were recorded during the current quarter and during the quarter ended December 31, 2018. This allowance remains relatively flat based on not only the generally declining portfolio balance, but also on the credit profile trends in this portfolio. Risk remains based on the generally less stringent credit requirements that were in place at the time that these borrowers qualified for their loans.
- **Home Equity Loans and Lines of Credit** – The recorded investment of this segment increased 2.1%, or \$46.6 million, to \$2.25 billion at December 31, 2019 from \$2.20 billion at September 30, 2019. The total allowance for this segment decreased 1.35% to \$14.7 million from \$14.9 million at September 30, 2019. During the quarter ended December 31, 2019, the portion of allowance for this segment that was determined by evaluating groups of loans collectively, slightly decreased by \$0.1 million, or 1.4%, from \$10.9 million to \$10.8 million. The ratio of this portion of the allowance to the total balance of loans in this segment that were evaluated collectively remained at 0.5% at December 31, 2019. Total delinquencies for this portfolio segment decreased 11.5% to \$8.8 million at December 31, 2019 as compared to \$10.0 million at September 30, 2019. Delinquencies greater than 90 days decreased 10.7% to \$5.2 million at December 31, 2019 from \$5.8 million at September 30, 2019. Net recoveries for this loan segment during the current quarter were less at \$0.9 million as compared to \$1.3 million for the quarter ended December 31, 2018. The reduction in the allowance is mainly supported by a reduction in the principal balance of home equity lines of credit coming to an end of the draw period. This portion of the allowance addresses exposure from customers whose lines of credit were originated without amortizing payments during the draw period and who could face potential increased payment shock at the end of the draw period. The principal balance of home equity lines of credit originated without amortizing payments during the draw period that are coming to the end of its draw period through fiscal 2020 is \$3.8 million at December 31, 2019 as compared to \$8.1 million at September 30, 2019. As this exposure decreases without incurring significant loss, the portion of the overall allowance allocated to the home equity loans and lines of credit category can be decreased. Originations after February 2013 require an amortizing payment during the draw period and do not face the same end-of-draw increased payment shock risk.

Loan Portfolio Composition

The following table sets forth the composition of the portfolio of loans held for investment, by type of loan segregated by geographic location at the indicated dates, excluding loans held for sale. The majority of our construction loan portfolio is secured by properties located in Ohio and the balances of other loans are immaterial. Therefore, neither was segregated by geographic location.

	December 31, 2019		September 30, 2019		December 31, 2018	
	Amount	Percent	Amount	Percent	Amount	Percent
(Dollars in thousands)						
Real estate loans:						
Residential Core						
Ohio	\$ 6,378,193		\$ 6,197,261		\$ 6,070,710	
Florida	1,769,129		1,748,816		1,755,482	
Other	2,984,566		2,956,947		3,077,639	
Total Residential Core	11,131,888	82.5%	10,903,024	82.5%	10,903,831	84.2%
Residential Home Today						
Ohio	78,866		81,081		88,261	
Florida	3,724		3,771		4,132	
Other	89		90		177	
Total Residential Home Today	82,679	0.6	84,942	0.6	92,570	0.7
Home equity loans and lines of credit						
Ohio	676,085		677,212		660,937	
Florida	426,479		415,849		383,784	
California	365,474		357,550		286,510	
Other	753,342		724,350		566,954	
Total Home equity loans and lines of credit	2,221,380	16.5	2,174,961	16.5	1,898,185	14.6
Total Construction	51,404	0.4	52,332	0.4	59,185	0.5
Other loans	2,900	—	3,166	—	3,000	—
Total loans receivable	13,490,251	100.0%	13,218,425	100.0%	12,956,771	100.0%
Deferred loan expenses, net	43,785		41,976		39,526	
Loans in process	(28,972)		(25,743)		(34,833)	
Allowance for loan losses	(37,292)		(38,913)		(41,938)	
Total loans receivable, net	\$ 13,467,772		\$ 13,195,745		\$ 12,919,526	

At December 31, 2019, the unpaid principal balance of our home equity loans and lines of credit portfolio consisted of \$392.6 million in home equity loans (which included \$249.1 million of home equity lines of credit, which are in the amortization period and no longer eligible to be drawn upon, and \$21.5 million in bridge loans) and \$1.83 billion in home equity lines of credit. The following table sets forth credit exposure, principal balance, percent delinquent 90 days or more, the mean CLTV percent at the time of origination and the current mean CLTV percent of our home equity loans, home equity lines of credit and bridge loan portfolio as of December 31, 2019. Home equity lines of credit in the draw period are reported according to geographic distribution.

	<u>Credit Exposure</u>	<u>Principal Balance</u>	<u>Percent Delinquent 90 Days or More</u>	<u>Mean CLTV Percent at Origination (2)</u>	<u>Current Mean CLTV Percent (3)</u>
(Dollars in thousands)					
Home equity lines of credit in draw period (by state)					
Ohio	\$1,402,991	\$ 537,123	0.10%	60%	51%
Florida	645,437	319,298	0.03%	58%	52%
California	646,128	296,313	0.01%	62%	58%
Other (1)	<u>1,432,235</u>	<u>676,046</u>	0.01%	64%	60%
Total home equity lines of credit in draw period	4,126,791	1,828,780	0.04%	61%	55%
Home equity lines in repayment, home equity loans and bridge loans					
	<u>392,600</u>	<u>392,600</u>	1.08%	65%	46%
Total	<u>\$4,519,391</u>	<u>\$2,221,380</u>	0.23%	61%	53%

- (1) No other individual state has a committed or drawn balance greater than 10% of our total equity lending portfolio and 5% of total loans.
- (2) Mean CLTV percent at origination for all home equity lines of credit is based on the committed amount.
- (3) Current Mean CLTV is based on best available first mortgage and property values as of December 31, 2019. Property values are estimated using HPI data published by the FHFA. Current Mean CLTV percent for home equity lines of credit in the draw period is calculated using the committed amount. Current Mean CLTV on home equity lines of credit in the repayment period is calculated using the principal balance.

At December 31, 2019, 35.6% of our home equity lending portfolio was either in a first lien position (19.7%), in a subordinate (second) lien position behind a first lien that we held (13.2%) or behind a first lien that was held by a loan that we originated, sold and now service for others (2.7%). At December 31, 2019, 13.9% of our home equity line of credit portfolio in the draw period was making only the minimum payment on the outstanding line balance.

The following table sets forth by calendar origination year, the credit exposure, principal balance, percent delinquent 90 days or more, the mean CLTV percent at the time of origination and the current mean CLTV percent of our home equity loans, home equity lines of credit and bridge loan portfolio as of December 31, 2019. Home equity lines of credit in the draw period are included in the year originated:

	Credit Exposure	Principal Balance	Percent Delinquent 90 Days or More	Mean CLTV Percent at Origination (1)	Current Mean CLTV Percent (2)
	(Dollars in thousands)				
Home equity lines of credit in draw period (3)					
2009 and Prior	\$ 4,208	\$ 1,444	—%	49%	45%
2010	9,266	2,508	—%	59%	40%
2013	40	17	—%	79%	54%
2014	92,647	27,679	—%	59%	40%
2015	199,709	74,304	0.06%	60%	43%
2016	379,163	149,765	0.21%	61%	48%
2017	822,411	368,777	0.08%	60%	51%
2018	1,135,453	547,650	0.01%	61%	56%
2019	1,483,894	656,636	0.01%	62%	62%
Total home equity lines of credit in draw period	4,126,791	1,828,780	0.04%	61%	55%
Home equity lines in repayment, home equity loans and bridge loans	392,600	392,600	1.08%	65%	46%
Total	<u>\$ 4,519,391</u>	<u>\$ 2,221,380</u>	0.23%	61%	53%

- (1) Mean CLTV percent at origination for all home equity lines of credit is based on the committed amount.
- (2) Current Mean CLTV is based on best available first mortgage and property values as of December 31, 2019. Property values are estimated using HPI data published by the FHFA. Current Mean CLTV percent for home equity lines of credit in the draw period is calculated using the committed amount. Current Mean CLTV on home equity lines of credit in the repayment period is calculated using the principal balance.
- (3) There are no remaining principal balances of home equity lines of credit for years 2011 and 2012. Those years are excluded from the table above.

In general, the home equity line of credit product originated prior to June 2010 was characterized by a ten year draw period followed by a ten year repayment period; however, there were two types of transactions that could result in a draw period that extended beyond ten years. The first transaction involved customer requests for increases in the amount of their home equity line of credit. When the customer’s credit performance and profile supported the increase, the draw period term was reset for the ten year period following the date of the increase in the home equity line of credit amount. A second transaction that impacted the draw period involved extensions. If the account and customer met certain pre-established criteria, an offer was made to extend the otherwise expiring draw period by ten years from the date of the offer. If the customer chose to accept the extension, the origination date of the account remained unchanged but the account would have a revised draw period that was extended by ten years. As a result of these two programs, the reported draw periods for certain home equity lines of credit accounts exceeded ten years.

The following table sets forth by fiscal year when the draw period expires, the principal balance of home equity lines of credit in the draw period as of December 31, 2019, segregated by the current combined LTV range.

Home equity lines of credit in draw period (by end of draw fiscal year):	Current CLTV Category					Unknown (2)	Total
	< 80%	80 - 89.9%	90 - 100%	>100%			
	(Dollars in thousands)						
2020 (1)	\$ 79,108	\$ 261	\$ —	\$ 13	\$ 42	\$ 79,424	
2021	28,218	68	—	—	—	28,286	
2022	28	—	—	—	—	28	
2023	17	—	—	—	—	17	
2024	17,702	72	—	2	—	17,776	
2025	16,229	45	—	—	19	16,293	
Post 2025	1,678,768	7,783	141	—	264	1,686,956	
Total	<u>\$ 1,820,070</u>	<u>\$ 8,229</u>	<u>\$ 141</u>	<u>\$ 15</u>	<u>\$ 325</u>	<u>\$ 1,828,780</u>	

- (1) Home equity lines of credit whose draw period ends in fiscal year 2020 include \$3.8 million of lines where the customer has an interest only payment during the draw period. All other home equity lines of credit have an amortizing payment during the draw period.
- (2) Market data necessary for stratification is not readily available.

The following table sets forth the breakdown of current mean CLTV percentages for our home equity lines of credit in the draw period as of December 31, 2019.

	Credit Exposure	Principal Balance	Percent of Total Principal Balance	Percent Delinquent 90 Days or More	Mean CLTV Percent at Origination (2)	Current Mean CLTV Percent (3)
	(Dollars in thousands)					
Home equity lines of credit in draw period (by current mean CLTV)						
< 80%	\$ 4,098,628	\$ 1,820,070	99.5%	0.04%	61%	55%
80 - 89.9%	26,912	8,229	0.4%	0.27%	78%	81%
90 - 100%	396	141	—%	—%	69%	93%
> 100%	113	15	—%	—%	39%	114%
Unknown (1)	742	325	0.1%	—%	35%	(1)
	<u>\$ 4,126,791</u>	<u>\$ 1,828,780</u>	<u>100.0%</u>	0.04%	61%	55%

- (1) Market data necessary for stratification is not readily available.
- (2) Mean CLTV percent at origination for all home equity lines of credit is based on the committed amount.
- (3) Current Mean CLTV is based on best available first mortgage and property values as of December 31, 2019. Property values are estimated using HPI data published by the FHFA. Current Mean CLTV percent for home equity lines of credit in the draw period is calculated using the committed amount. Current Mean CLTV on home equity lines of credit in the repayment period is calculated using the principal balance.

Delinquent Loans

The following tables set forth the recorded investment in loan delinquencies by type, segregated by geographic location and severity of delinquency as of the dates indicated.

	Loans Delinquent for		Total
	30-89 Days	90 Days or More	
(Dollars in thousands)			
December 31, 2019			
Real estate loans:			
Residential Core			
Ohio	\$ 6,919	\$ 6,437	\$ 13,356
Florida	1,997	852	2,849
Other	892	765	1,657
Total Residential Core	9,808	8,054	17,862
Residential Home Today			
Ohio	4,003	3,038	7,041
Florida	111	158	269
Total Residential Home Today	4,114	3,196	7,310
Home equity loans and lines of credit			
Ohio	1,358	2,121	3,479
Florida	776	627	1,403
California	569	506	1,075
Other	953	1,922	2,875
Total Home equity loans and lines of credit	3,656	5,176	8,832
Total	\$ 17,578	\$ 16,426	\$ 34,004

	Loans Delinquent for		Total
	30-89 Days	90 Days or More	
(Dollars in thousands)			
September 30, 2019			
Real estate loans:			
Residential Core			
Ohio	\$ 8,519	\$ 5,503	\$ 14,022
Florida	930	1,305	2,235
Other	1,405	866	2,271
Total Residential Core	10,854	7,674	18,528
Residential Home Today			
Ohio	4,155	2,586	6,741
Florida	159	37	196
Total Residential Home Today	4,314	2,623	6,937
Home equity loans and lines of credit			
Ohio	1,746	1,950	3,696
Florida	1,065	1,260	2,325
California	187	552	739
Other	1,189	2,035	3,224
Total Home equity loans and lines of credit	4,187	5,797	9,984
Total	\$ 19,355	\$ 16,094	\$ 35,449

	Loans Delinquent for		Total
	30-89 Days	90 Days or More	
	(Dollars in thousands)		
December 31, 2018			
Real estate loans:			
Residential Core			
Ohio	\$ 7,952	\$ 7,988	\$ 15,940
Florida	1,068	1,543	2,611
Other	1,805	1,283	3,088
Total Residential Core	10,825	10,814	21,639
Residential Home Today			
Ohio	5,284	4,116	9,400
Florida	191	118	309
Total Residential Home Today	5,475	4,234	9,709
Home equity loans and lines of credit			
Ohio	1,821	2,186	4,007
Florida	1,332	1,949	3,281
California	763	524	1,287
Other	1,660	2,099	3,759
Total Home equity loans and lines of credit	5,576	6,758	12,334
Total	\$ 21,876	\$ 21,806	\$ 43,682

Total loans seriously delinquent (i.e. delinquent 90 days or more) were 0.12% of total net loans at December 31, 2019 and September 30, 2019 and were 0.17% at December 31, 2018, a decrease of five basis points from December 31, 2018. Total loans delinquent (i.e. delinquent 30 days or more) were 0.25% of total net loans at December 31, 2019, 0.27% at September 30, 2019 and 0.34% at December 31, 2018.

Non-Performing Assets and Troubled Debt Restructurings

The following table sets forth the recorded investments and categories of our non-performing assets and TDRs at the dates indicated.

	December 31, 2019	September 30, 2019	December 31, 2018
	(Dollars in thousands)		
Non-accrual loans:			
Real estate loans:			
Residential Core	\$ 33,310	\$ 37,052	\$ 41,011
Residential Home Today	11,551	12,442	14,438
Home equity loans and lines of credit	15,447	21,771	21,523
Total non-accrual loans (1)(2)	60,308	71,265	76,972
Real estate owned	2,813	2,163	2,888
Total non-performing assets	\$ 63,121	\$ 73,428	\$ 79,860
Ratios:			
Total non-accrual loans to total loans	0.45%	0.54%	0.59%
Total non-accrual loans to total assets	0.41%	0.49%	0.54%
Total non-performing assets to total assets	0.43%	0.50%	0.56%
TDRs: (not included in non-accrual loans above)			
Real estate loans:			
Residential Core	\$ 48,047	\$ 47,829	\$ 51,116
Residential Home Today	24,878	24,651	25,972
Home equity loans and lines of credit	29,192	24,438	26,857
Total	\$ 102,117	\$ 96,918	\$ 103,945

- (1) At December 31, 2019, September 30, 2019, and December 31, 2018, the totals include \$40.8 million, \$52.1 million, and \$51.2 million, respectively, in TDRs, which are less than 90 days past due but included with non-accrual loans for a minimum period of six months from the restructuring date due to their non-accrual status prior to restructuring, because of a prior partial charge off, or because all borrowers have filed Chapter 7 bankruptcy, and not reaffirmed or been dismissed.
- (2) At December 31, 2019, September 30, 2019, and December 31, 2018 the totals include \$8.4 million, \$8.4 million and \$10.7 million in TDRs that are 90 days or more past due, respectively.

The gross interest income that would have been recorded during the three months ended December 31, 2019 and December 31, 2018 on non-accrual loans, if they had been accruing during the entire period and TDRs if they had been current and performing in accordance with their original terms during the entire period, was \$2.1 million and \$2.3 million, respectively. The interest income recognized on those loans included in net income for the three months ended December 31, 2019 and December 31, 2018 was \$1.3 million and \$1.4 million, respectively.

The recorded investment of impaired loans includes accruing TDRs and loans that are returned to accrual status when contractual payments are less than 90 days past due. These loans continue to be individually evaluated for impairment until, at a minimum, contractual payments are less than 30 days past due. Also, the recorded investment of non-accrual loans includes loans that are not included in the recorded investment of impaired loans because they are included in loans collectively evaluated for impairment.

The table below sets forth a reconciliation of the recorded investments and categories between non-accrual loans and impaired loans at the dates indicated.

	December 31, 2019	September 30, 2019	December 31, 2018
(Dollars in thousands)			
Non-Accrual Loans	\$ 60,308	\$ 71,265	\$ 76,972
Accruing TDRs	102,118	96,917	103,945
Performing Impaired Loans	4,667	4,907	3,800
Less Loans Collectively Evaluated	(3,844)	(2,616)	(4,025)
Total Impaired loans	<u>\$ 163,249</u>	<u>\$ 170,473</u>	<u>\$ 180,692</u>

In response to the economic challenges facing many borrowers, we continue to restructure loans. Loan restructuring is a method used to help families keep their homes and preserve our neighborhoods. This involves making changes to the borrowers' loan terms through interest rate reductions, either for a specific period or for the remaining term of the loan; term extensions including those beyond that provided in the original agreement; principal forgiveness; capitalization of delinquent payments in special situations; or some combination of the above. Loans discharged through Chapter 7 bankruptcy are also reported as TDRs per OCC interpretive guidance. For discussion on impairment measurement, see *Note 4 to the Unaudited Interim Consolidated Financial Statements: LOANS AND ALLOWANCE FOR LOAN LOSSES*. We had \$151.3 million of TDRs (accrual and non-accrual) recorded at December 31, 2019. This was a \$6.1 million decrease in the recorded investment of TDRs from September 30, 2019 and a \$14.5 million decrease from December 31, 2018.

The following table sets forth the recorded investment in accrual and non-accrual TDRs, by the types of concessions granted as of December 31, 2019. Initial concessions granted by loans restructured as TDRs can include reduction of interest rate, extension of amortization period, forbearance or other actions. Some TDRs have experienced a combination of concessions. TDRs also can occur as a result of bankruptcy proceedings. Loans discharged in Chapter 7 bankruptcy are classified as multiple restructurings if the loan's original terms had also been restructured by the Company.

	Initial Restructurings	Multiple Restructurings	Bankruptcy	Total
(In thousands)				
Accrual				
Residential Core	\$ 27,338	\$ 14,544	\$ 6,165	\$ 48,047
Residential Home Today	13,983	9,823	1,072	24,878
Home equity loans and lines of credit	27,865	359	968	29,192
Total	<u>\$ 69,186</u>	<u>\$ 24,726</u>	<u>\$ 8,205</u>	<u>\$ 102,117</u>
Non-Accrual, Performing				
Residential Core	\$ 4,338	\$ 8,532	\$ 10,935	\$ 23,805
Residential Home Today	1,238	4,895	1,847	7,980
Home equity loans and lines of credit	4,503	2,599	1,884	8,986
Total	<u>\$ 10,079</u>	<u>\$ 16,026</u>	<u>\$ 14,666</u>	<u>\$ 40,771</u>
Non-Accrual, Non-Performing				
Residential Core	\$ 2,116	\$ 1,789	\$ 636	\$ 4,541
Residential Home Today	647	1,847	179	2,673
Home equity loans and lines of credit	704	266	241	1,211
Total	<u>\$ 3,467</u>	<u>\$ 3,902</u>	<u>\$ 1,056</u>	<u>\$ 8,425</u>
Total TDRs				
Residential Core	\$ 33,792	\$ 24,865	\$ 17,736	\$ 76,393
Residential Home Today	15,868	16,565	3,098	35,531
Home equity loans and lines of credit	33,072	3,224	3,093	39,389
Total	<u>\$ 82,732</u>	<u>\$ 44,654</u>	<u>\$ 23,927</u>	<u>\$ 151,313</u>

TDRs in accrual status are loans accruing interest and performing according to the terms of the restructuring. To be performing, a loan must be less than 90 days past due as of the report date. Non-accrual, performing status indicates that a loan was not accruing interest at the time of restructuring, continues to not accrue interest and is performing according to the terms of the restructuring, but has not been current for at least six consecutive months since its restructuring, has a partial charge-off, or is being classified as non-accrual per the OCC guidance on loans in Chapter 7 bankruptcy status, where all borrowers have filed and have not reaffirmed or been dismissed. Non-accrual, non-performing status includes loans that are not accruing interest because they are greater than 90 days past due and therefore not performing according to the terms of the restructuring.

Income Taxes. We consider accounting for income taxes a critical accounting policy due to the subjective nature of certain estimates, including the impact of tax rate changes, such as those implemented by the Act signed into law in December 2017, that are involved in the calculation. We use the asset/liability method of accounting for income taxes in which deferred tax assets and liabilities are established for the temporary differences between the financial reporting basis and the tax basis of our assets and liabilities. We must assess the realization of the deferred tax asset and, to the extent that we believe that recovery is not likely, a valuation allowance is established. Adjustments to increase or decrease existing valuation allowances, if any, are charged or credited, respectively, to income tax expense. At December 31, 2019, no valuation allowances were outstanding. Even though we have determined a valuation allowance is not required for deferred tax assets at December 31, 2019, there is no guarantee that those assets, if any, will be recognizable in the future.

Pension Benefits. The determination of our obligations and expense for pension benefits is dependent upon certain assumptions used in calculating such amounts. Key assumptions used in the actuarial valuations include the discount rate and expected long-term rate of return on plan assets. Actual results could differ from the assumptions and market driven rates may fluctuate. Significant differences in actual experience or significant changes in the assumptions could materially affect future pension obligations and expense.

Comparison of Financial Condition at December 31, 2019 and September 30, 2019

Total assets increased \$263.8 million, or 2%, to \$14.81 billion at December 31, 2019 from \$14.54 billion at September 30, 2019. This increase was primarily the result of new loan origination levels exceeding the total of loans sales and principal repayments, as well as increases in cash and cash equivalents and investment securities partially offset by decreases in premises, equipment and software, net and other assets.

Cash and cash equivalents increased \$6.1 million, or 2%, to \$281.2 million at December 31, 2019 from \$275.1 million at September 30, 2019. We manage cash to maintain the level of liquidity described later in the *Liquidity and Capital Resources* section.

Investment securities, all of which are classified as available for sale, increased \$6.1 million, or 1%, to \$554.0 million at December 31, 2019 from \$547.9 million at September 30, 2019. Investment securities increased as \$56.4 million in purchases and a \$3.7 million reduction of unrealized losses exceeded the combined effect of \$52.6 million in principal paydowns, and \$1.4 million of net acquisition premium amortization that occurred in the mortgage-backed securities portfolio during the three months ended December 31, 2019. There were no sales of investment securities during the three months ended December 31, 2019.

Loans held for investment, net, increased \$272.0 million, or 2%, to \$13.47 billion at December 31, 2019 from \$13.20 billion at September 30, 2019. This increase was primarily from a \$226.6 million, or 2%, increase in residential mortgage loans to \$11.21 billion at December 31, 2019 from \$10.99 billion at September 30, 2019. Additionally, there was a \$46.4 million increase in the balance of home equity loans and lines of credit during the three months ended December 31, 2019, as new originations and additional draws on existing accounts exceeded repayments. During the three months ended December 31, 2019, \$303.7 million of three- and five-year “SmartRate” loans were originated while \$446.9 million of 10-, 15-, and 30-year fixed-rate first mortgage loans were originated. These originations were offset by paydowns and fixed-rate loan sales. Between September 30, 2019 and December 31, 2019, the total fixed-rate portion of the first mortgage loan portfolio increased \$160.0 million and was comprised of an increase of \$208.6 million in the balance of fixed-rate loans with original terms greater than 10 years partially offset by a decrease of \$48.6 million in the balance of fixed-rate loans with original terms of 10 years or less. During the three months ended December 31, 2019, we completed \$208.5 million in loan sales, which included a \$99.0 million long-term fixed-rate sale to a private investor, and \$9.6 million of agency-compliant Home Ready loans and \$99.9 million of long-term, fixed-rate, agency-compliant, non-Home Ready first mortgage loans sold to Fannie Mae. In addition, during the three months ended December 31, 2019, \$230.3 million of fixed-rate residential mortgage loans, originated and serviced by the Association and sold to an investor in a prior year, were purchased from that investor. Also, during the three months ended December 31, 2019, we purchased long-term, fixed-rate first mortgage loans that have a remaining unpaid principal balance of \$8.0 million.

Commitments originated for home equity lines of credit and equity and bridge loans were \$349.5 million for the three months ended December 31, 2019 compared to \$357.0 million for the three months ended December 31, 2018. At December 31, 2019, pending commitments to originate new home equity lines of credit were \$87.9 million and equity and bridge loans were \$35.7 million. Refer to the *Controlling Our Interest Rate Risk Exposure* section of the *Overview* for additional information.

The total allowance for loan losses decreased \$1.6 million, or 4%, to \$37.3 million at December 31, 2019 from \$38.9 million at September 30, 2019, primarily reflecting improved credit metrics, including continued recoveries of loan amounts previously charged off, low levels of current loan charge-offs and reduced exposure from home equity lines of credit coming to the end of the draw period. Refer to *Note 4. Loans and Allowance for Loan Losses* for additional discussion.

Prepaid expenses and other assets decreased \$8.6 million to \$79.4 million at December 31, 2019 from \$88.0 million at September 30, 2019. This decrease included an \$8.7 million decrease in the initial margin requirement posted on interest rate swap contracts, a \$6.9 million decrease in prepaid taxes, a \$4.6 million decrease in net deferred taxes, a \$3.7 million decrease in receivable due to the ESOP, a decrease of \$1.6 million in deferred leasing costs, and decreases totaling \$0.7 million in prepaid insurance and assessments. These decreases were partially offset by an \$18.4 million right of use asset related to the Company's operating leases due to the adoption of the recently issued accounting guidance on the treatment of leases.

Deposits increased \$234.5 million, or 3%, to \$9.00 billion at December 31, 2019 from \$8.77 billion at September 30, 2019. The increase in deposits resulted primarily from a \$184.5 million increase in CDs, a \$25.6 million increase in our high-yield checking accounts and a \$21.8 million increase in our savings accounts (which included a \$27.4 million increase in money market accounts in the state of Florida and a \$5.6 million decrease in high yield savings accounts). We believe that our savings and checking accounts provide a stable source of funds. In addition, our high-yield savings accounts are expected to reprice in a manner similar to our home equity lending products, and, therefore, assist us in managing interest rate risk. The balance of brokered CDs at December 31, 2019 was \$501.4 million, which was a decrease of \$6.4 million during the three months ended December 31, 2019.

Borrowed funds, all from the FHLB of Cincinnati, decreased \$13.3 million, or less than one percent, to \$3.89 billion at December 31, 2019 from \$3.90 billion at September 30, 2019. Activity included \$50.0 million of new 90-day advances that are hedged by equal notional amounts of new interest rate swaps with initial fixed-pay terms of five to eight years and \$150.0 million of new long-term advances with terms of four to five years, offset by scheduled principal repayments of long-term advances and a \$100.0 million decrease in the balance of short-term advances. The total balance of borrowed funds of \$3.89 billion at December 31, 2019 consisted of overnight and short-term advances of \$400.0 million, long-term advances of \$683.4 million with a remaining weighted average maturity of approximately two years and short-term advances of \$2.80 billion aligned with interest rate swap contracts with a remaining weighted average effective maturity of approximately 3.5 years. Interest rate swaps have been used to extend the duration of short-term borrowings to approximately five to eight years at inception, by paying a fixed rate of interest and receiving the variable rate. Refer to the *Extending the Duration of Funding Sources* section of the *Overview* and *Part 1, Item 3. Quantitative and Qualitative Disclosures About Market Risk* for additional discussion regarding short-term borrowings and interest-rate swaps.

Total shareholders' equity increased \$32.2 million, or 2%, to \$1.73 billion at December 31, 2019 from \$1.70 billion at September 30, 2019. This net increase primarily reflected the effect of a combination of \$25.6 million of net income and an \$18.6 million decrease in accumulated other comprehensive loss, mainly the result of changes in market interest rates related to our interest rate swaps, reduced by \$0.4 million of repurchases of outstanding common stock and \$13.4 million of cash dividend payments. Adjustments of \$3.3 million related to our stock compensation plan and ESOP further offset the decrease. As a result of a July 16, 2019 mutual member vote, Third Federal Savings, MHC, the mutual holding company that owns approximately 81% of the outstanding stock of the Company, waived the receipt of its share of the dividends paid. Refer to *Item 2. Unregistered Sales of Equity Securities and Use of Proceeds* for additional details regarding the repurchase of shares of common stock and the dividend waiver.

Comparison of Operating Results for the Three Months Ended December 31, 2019 and 2018

Average balances and yields. The following table sets forth average balances, average yields and costs, and certain other information for the periods indicated. No tax-equivalent yield adjustments were made, as the effects thereof were not material. Average balances are derived from daily average balances. Non-accrual loans are included in the computation of loan average balances, but only cash payments received on those loans during the period presented are reflected in the yield. The yields set forth below include the effect of deferred fees, deferred expenses, discounts and premiums that are amortized or accreted to interest income or interest expense.

	Three Months Ended December 31, 2019			Three Months Ended December 31, 2018		
	Average Balance	Interest Income/ Expense	Yield/ Cost (1)	Average Balance	Interest Income/ Expense	Yield/ Cost (1)
(Dollars in thousands)						
Interest-earning assets:						
Interest-earning cash equivalents	\$ 229,986	\$ 949	1.65%	\$ 225,748	\$ 1,258	2.23%
Investment securities	—	—	—%	3,971	24	2.42%
Mortgage-backed securities	545,729	2,864	2.10%	537,050	3,100	2.31%
Loans (2)	13,241,863	115,225	3.48%	12,871,771	112,491	3.50%
Federal Home Loan Bank stock	101,858	1,014	3.98%	93,544	1,415	6.05%
Total interest-earning assets	14,119,436	120,052	3.40%	13,732,084	118,288	3.45%
Noninterest-earning assets	489,200			386,086		
Total assets	\$ 14,608,636			\$ 14,118,170		
Interest-bearing liabilities:						
Checking accounts	\$ 867,971	483	0.22%	\$ 898,795	748	0.33%
Savings accounts	1,490,074	3,024	0.81%	1,286,543	2,178	0.68%
Certificates of deposit	6,505,776	34,809	2.14%	6,352,338	29,836	1.88%
Borrowed funds	3,746,170	17,551	1.87%	3,614,231	17,714	1.96%
Total interest-bearing liabilities	12,609,991	55,867	1.77%	12,151,907	50,476	1.66%
Noninterest-bearing liabilities	273,002			192,504		
Total liabilities	12,882,993			12,344,411		
Shareholders' equity	1,725,643			1,773,759		
Total liabilities and shareholders' equity	\$ 14,608,636			\$ 14,118,170		
Net interest income		\$ 64,185			\$ 67,812	
Interest rate spread (1)(3)			1.63%			1.79%
Net interest-earning assets (4)	\$ 1,509,445			\$ 1,580,177		
Net interest margin (1)(5)		1.82%			1.98%	
Average interest-earning assets to average interest-bearing liabilities	111.97%			113.00%		
Selected performance ratios:						
Return on average assets (1)		0.70%			0.58%	
Return on average equity (1)		5.94%			4.59%	
Average equity to average assets		11.81%			12.56%	

- (1) Annualized.
- (2) Loans include both mortgage loans held for sale and loans held for investment.
- (3) Interest rate spread represents the difference between the yield on average interest-earning assets and the cost of average interest-bearing liabilities.
- (4) Net interest-earning assets represent total interest-earning assets less total interest-bearing liabilities.
- (5) Net interest margin represents net interest income divided by total interest-earning assets.

General. Net income increased \$5.3 million to \$25.6 million for the three months ended December 31, 2019 compared to \$20.3 million for the three months ended December 31, 2018. The increase in net income was largely attributable to a gain from the sale of commercial properties, increased gain on the sale of loans and an increase in the credit for loan loss provision, partially offset by a decrease in net interest income when compared to the same period last year.

Interest and Dividend Income. Interest and dividend income increased \$1.8 million, or 2%, to \$120.1 million during the three months ended December 31, 2019 compared to \$118.3 million during the same three months in the prior year. The increase in interest and dividend income resulted primarily from an increase in interest income from loans partially offset by declines in interest income on interest earning cash equivalents and mortgage-backed securities.

Interest income on loans increased \$2.7 million, or 2%, to \$115.2 million for the three months ended December 31, 2019 compared to \$112.5 million for the three months ended December 31, 2018. This increase was attributed mainly to a \$370.1 million increase in the average balance of loans to \$13.24 billion for the current three months compared to \$12.87 billion during the same three months in the prior year as new loan production exceeded repayments and loan sales. The impact from the increase in the average balance of loans was offset by a two basis point decrease in the average yield on loans to 3.48% for the three months ended December 31, 2019 from 3.50% for the same three months in the prior year. Overall, market rate fluctuations during the year have slightly reduced our loan yields, particularly home equity lending products that feature interest rates that reset based on the prime rate.

Interest income on FHLB stock decreased \$0.4 million, or 29% to \$1 million during the current three months compared to \$1.4 million for the three months ended December 31, 2018. This decrease was attributed to a 207 basis point decrease in the average yield on FHLB stock partially offset by an \$8.4 million increase in the average balance of FHLB stock to \$101.9 million compared to \$93.5 million for the same three months in the prior year.

Interest income on other interest earning cash equivalents decreased \$0.3 million or 25%, to \$1.0 million during the current three months compared to \$1.3 million for the three months ended December 31, 2018. The decrease was attributed to a 58 basis point decrease in the average yield partially offset by a \$4.2 million increase in the average balance of other interest earning cash equivalents to \$230.0 million from \$225.7 million for the same three months in the prior year.

Interest income on mortgage-backed securities decreased \$0.2 million, or 6%, to \$2.9 million during the current three months compared to \$3.1 million during the three months ended December 31, 2018. This decrease was attributed to a 21 basis point decrease in the average yield on mortgage-backed securities partially offset by an \$8.6 million increase in the average balance of mortgage-backed securities to \$545.7 million for the current three months compared to \$537.1 million during the same three months in the prior year.

Interest Expense. Interest expense increased \$5.4 million, or 11%, to \$55.9 million during the current three months compared to \$50.5 million during the three months ended December 31, 2018. The increase resulted primarily from an increase in interest expense on deposits partially offset by a decline in interest expense on borrowed funds.

Interest expense on CDs increased \$5.0 million, or 17%, to \$34.8 million during the three months ended December 31, 2019 compared to \$29.8 million during the three months ended December 31, 2018. The increase was attributed primarily to a 26 basis point increase in the average rate we paid on CDs to 2.14% during the current three months from 1.88% during the same three months last year. In addition, there was a \$153.4 million, or 2%, increase in the average balance of CDs to \$6.51 billion from \$6.35 billion during the same three months of the prior year. Interest expense on savings and checking accounts increased \$0.8 million and decreased \$0.2 million, respectively, to \$3.0 million and \$0.5 million during the three months ended December 31, 2019, compared to the same three month period of the prior year. Rates were adjusted on deposits in response to changes in general market rates as well as to changes in the rates paid by our competition. The increase in deposits was used, in combination with an increase in borrowings, to fund our balance sheet growth and our capital management activities, including share repurchases and dividend payments.

Interest expense on borrowed funds, all from the FHLB of Cincinnati, decreased \$0.1 million, or 1%, to \$17.6 million during the three months ended December 31, 2019 from \$17.7 million during the three months ended December 31, 2018. The decrease was attributed to a nine basis point decrease in the average rate paid for these funds to 1.87%, during the three months ended December 31, 2019 from 1.96% for the three months ended December 31, 2018. Partially offsetting the decrease in the rate paid on borrowed funds was a \$131.9 million, or 4%, increase in the average balance of borrowed funds to \$3.75 billion during the current three months from \$3.61 billion during the same three months of the prior year. Refer to the *Extending the Duration of Funding Sources* section of the Overview and *Comparison of Financial Condition* for further discussion.

Net Interest Income. Net interest income decreased \$3.6 million, or 5%, to \$64.2 million during the three months ended December 31, 2019 from \$67.8 million during the three months ended December 31, 2018. Average interest-earning assets

increased during the current three months by \$387.4 million, or 3%, when compared to the three months ended December 31, 2018. The increase in average assets was attributed primarily to the growth of our loan portfolio and to a lesser extent mortgage-backed securities and FHLB stock. The increase in average interest earning assets was partially offset by a five basis point decrease in the yield on those assets to 3.40% from 3.45%. However, average interest-bearing liabilities increased by \$458.1 million and experienced an 11 basis point increase in cost, as our interest rate spread decreased 16 basis points to 1.63% compared to 1.79% during the same three months last year reflecting the flattening yield curve and general interest rate environment. Our net interest margin was 1.82% for the current three months and 1.98% for the same three months in the prior year.

Provision (Credit) for Loan Losses. We recorded a credit for loan losses of \$3.0 million during the three months ended December 31, 2019 and a \$2.0 million credit for loan losses during the three months ended December 31, 2018. Continued recoveries of loan amounts previously charged off, low levels of current loan charge-offs and delinquent loans and reduced exposure from home equity lines of credit coming to the end of the draw period resulted in the loan provision credit during the current period. Nevertheless, we continue our awareness of the relative values of residential properties in comparison to their cyclical peaks. As delinquencies in the portfolio have been resolved through pay-off, short sale or foreclosure, or management determines the collateral is not sufficient to satisfy the loan, uncollected balances have been charged against the allowance for loan losses previously provided. In the current three months, we recorded net recoveries of \$1.4 million, as compared to net recoveries of \$1.5 million for the three months ended December 31, 2018. The credit for loan losses recorded for the current three months, due to net recoveries, resulted in a decrease in the balance of the allowance for loan losses. The allowance for loan losses was \$37.3 million, or 0.28% of the total recorded investment in loans receivable, at December 31, 2019, compared to \$41.9 million, or 0.32% of the total recorded investment in loans receivable, at December 31, 2018. Balances of recorded investments are net of deferred fees, expenses and any applicable loans-in-process. Refer to the *Lending Activities* section of the Overview and *Note 4. Loans and Allowance for Loan Losses* for further discussion.

Non-Interest Income. Non-interest income increased \$7.2 million, or 154%, to \$11.9 million during the three months ended December 31, 2019 compared to \$4.7 million during the three months ended December 31, 2018. The increase in non-interest income was primarily due to a \$4.3 million gain, representing our share of the gain on the sale of the remaining commercial property held by a non-thrift, partially owned subsidiary of the Company. In addition, there was a \$2.8 million increase in the net gain on sale of loans, which was \$2.9 million during the three months ended December 31, 2019 compared to \$0.1 million during the three months ended December 31, 2018. There were loan sales of \$208.5 million at a net gain of 1.44% during the three months ended December 31, 2019, which included a bulk sale of \$99.0 million to a private investor, compared to loan sales of \$20.7 million during the three months ended December 31, 2018.

Non-Interest Expense. Non-interest expense decreased \$0.7 million, or 1%, to \$47.3 million during the three months ended December 31, 2019 compared to \$48.0 million during the three months ended December 31, 2018. This decrease resulted primarily from marginal offsetting fluctuations in office property and equipment expense, marketing expenses, salaries and employee benefits as well as real estate owned expenses.

Income Tax Expense. The provision for income taxes was \$6.2 million during both the three months ended December 31, 2019 and the three months ended December 31, 2018. The provision for the current three months included \$5.8 million of federal income tax provision and \$0.4 million of state income tax provision. The provision for the three months ended December 31, 2018 included \$5.1 million of federal income tax provision and \$1.1 million of state income tax provision. Our effective federal tax rate was 18.5% during the three months ended December 31, 2019 and 20.0% during the three months ended December 31, 2018. Our expected effective federal income tax rate in the current year is lower than the federal statutory rate due to an increase in excess tax benefits associated with stock-based compensation.

Liquidity and Capital Resources

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, advances from the FHLB of Cincinnati, borrowings from the FRB-Cleveland Discount Window, proceeds from brokered CDs transactions, principal repayments and maturities of securities, and sales of loans.

In addition to the primary sources of funds described above, we have the ability to obtain funds through the use of collateralized borrowings in the wholesale markets, and from sales of securities. Also, debt issuance by the Company and access to the equity capital markets via a supplemental minority stock offering or a full conversion (second-step) transaction remain as other potential sources of liquidity, although these channels generally require up to nine months of lead time.

While maturities and scheduled amortization of loans and securities are predictable sources of funds, deposit flows and mortgage prepayments are greatly influenced by interest rates, economic conditions and competition. The Association's Asset/

Liability Management Committee is responsible for establishing and monitoring our liquidity targets and strategies in order to ensure that sufficient liquidity exists for meeting the borrowing needs and deposit withdrawals of our customers as well as unanticipated contingencies. We generally seek to maintain a minimum liquidity ratio of 5% (which we compute as the sum of cash and cash equivalents plus unencumbered investment securities for which ready markets exist, divided by total assets). For the three months ended December 31, 2019, our liquidity ratio averaged 5.42%. We believe that we had sufficient sources of liquidity to satisfy our short- and long-term liquidity needs as of December 31, 2019.

We regularly adjust our investments in liquid assets based upon our assessment of expected loan demand, expected deposit flows, yields available on interest-earning deposits and securities and the objectives of our asset/liability management program. Excess liquid assets are generally invested in interest-earning deposits and short- and intermediate-term securities.

Our most liquid assets are cash and cash equivalents. The levels of these assets are dependent on our operating, financing, lending and investing activities during any given period. At December 31, 2019, cash and cash equivalents totaled \$281.2 million, which represented an increase of 2% from September 30, 2019.

Investment securities classified as available-for-sale, which provide additional sources of liquidity, totaled \$554.0 million at December 31, 2019.

During the three-month period ended December 31, 2019, loan sales totaled \$208.5 million, which included a \$99.0 million sale to a private investor and sales to Fannie Mae, consisting of \$99.9 million of long-term, fixed-rate, agency-compliant and non-Home Ready first mortgage loans and \$9.6 million of loans that qualified under Fannie Mae's Home Ready initiative. Loans originated under the Home Ready initiative are classified as "held for sale" at origination. Loans originated under non-Home Ready, Fannie Mae compliant procedures are classified as "held for investment" until they are specifically identified for sale.

At December 31, 2019, \$9.6 million of long-term, fixed-rate residential first mortgage loans were classified as "held for sale," all of which qualified under Fannie Mae's Home Ready initiative. There were no loan sale commitments outstanding at December 31, 2019.

Our cash flows are derived from operating activities, investing activities and financing activities as reported in our Consolidated Statements of Cash Flows (unaudited) included in the unaudited interim Consolidated Financial Statements.

At December 31, 2019, we had \$586.4 million in outstanding commitments to originate loans. In addition to commitments to originate loans, we had \$2.30 billion in unfunded home equity lines of credit to borrowers. CDs due within one year of December 31, 2019 totaled \$3.53 billion, or 39.3% of total deposits. If these deposits do not remain with us, we will be required to seek other sources of funds, including loan sales, sales of investment securities, other deposit products, including new CDs, brokered CDs, FHLB advances, borrowings from the FRB-Cleveland Discount Window or other collateralized 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 CDs due on or before December 31, 2020. We believe, however, based on past experience, that a significant portion of such deposits will remain with us. Generally, we have the ability to attract and retain deposits by adjusting the interest rates offered.

Our primary investing activities are originating residential mortgage loans, home equity loans and lines of credit and purchasing investments. During the three months ended December 31, 2019, we originated \$750.6 million of residential mortgage loans, and \$349.5 million of commitments for home equity loans and lines of credit, while during the three months ended December 31, 2018, we originated \$383.8 million of residential mortgage loans and \$357.0 million of commitments for home equity loans and lines of credit. We purchased \$56.4 million of securities during the three months ended December 31, 2019, and \$59.1 million during the three months ended December 31, 2018.

Financing activities consist primarily of changes in deposit accounts, changes in the balances of principal and interest owed on loans serviced for others, FHLB advances, including any collateral requirements related to interest rate swap agreements and borrowings from the FRB-Cleveland Discount Window. We experienced a net increase in total deposits of \$234.5 million during the three months ended December 31, 2019, which reflected the active management of the offered rates on maturing CDs, compared to a net increase of \$105.6 million during the three months ended December 31, 2018. Deposit flows are affected by the overall level of interest rates, the interest rates and products offered by us and our local competitors, and by other factors. During the three months ended December 31, 2019, there was a \$6.4 million decrease in the balance of brokered CDs (exclusive of acquisition costs and subsequent amortization), which had a balance of \$501.4 million at December 31, 2019. At December 31, 2018 the balance of brokered CDs was \$576.4 million. Principal and interest owed on loans serviced for others experienced a net decrease of \$1.4 million to \$31.5 million during the three months ended December 31, 2019 compared to a net decrease of \$0.9 million to \$30.6 million during the three months ended December 31, 2018. During the three months ended December 31, 2019 we decreased our advances from the FHLB of Cincinnati by \$13.3

million to manage the funding of new loan originations and our capital initiatives, and actively manage our liquidity ratio. During the three months ended December 31, 2018, our advances from the FHLB of Cincinnati increased by \$12.6 million.

Liquidity management is both a daily and long-term function of business management. If we require funds beyond our ability to generate them internally, borrowing agreements exist with the FHLB of Cincinnati and the FRB-Cleveland Discount Window, each of which provides an additional source of funds. Also, in evaluating funding alternatives, we may participate in the brokered CD market. At December 31, 2019 we had \$3.89 billion of FHLB of Cincinnati advances and no outstanding borrowings from the FRB-Cleveland Discount Window. Additionally, at December 31, 2019, we had \$501.4 million of brokered CDs. During the three months ended December 31, 2019, we had average outstanding advances from the FHLB of Cincinnati of \$3.75 billion as compared to average outstanding advances of \$3.61 billion during the three months ended December 31, 2018. While the net average balance increased during the current three months, the actual balance as of December 31, 2019 was less than the September 30, 2019 balance, reflecting an increase in the use of deposits to fund balance sheet growth and our capital initiatives, and to manage our on-balance sheet liquidity. Refer to the *Extending the Duration of Funding Sources* section of the *Overview* and the *General* section of *Item 3. Quantitative and Qualitative Disclosures About Market Risk* for further discussion. At December 31, 2019, we had the ability to immediately borrow an additional \$73.1 million from the FHLB of Cincinnati and \$41.7 million from the FRB-Cleveland Discount Window. From the perspective of collateral value securing FHLB of Cincinnati advances, our capacity limit for additional borrowings beyond the outstanding balance at December 31, 2019 was \$4.27 billion, subject to satisfaction of the FHLB of Cincinnati common stock ownership requirement. To satisfy the common stock ownership requirement for the maximum limit of borrowing, we would have to increase our ownership of FHLB of Cincinnati common stock by an additional \$85.4 million.

The Association and the Company are subject to various regulatory capital requirements, including a risk-based capital measure. The Basel III capital framework for U.S. banking organizations ("Basel III Rules") includes both a revised definition of capital and guidelines for calculating risk-weighted assets by assigning balance sheet assets and off-balance sheet items to broad risk categories.

The Association is subject to the "capital conservation buffer" requirement level of 2.5%. The requirement limits capital distributions and certain discretionary bonus payments to management if the institution does not hold a "capital conservation buffer" in addition to the minimum capital requirements. At December 31, 2019, the Association exceeded the regulatory requirement for the "capital conservation buffer".

As of December 31, 2019, the Association exceeded all regulatory requirements to be considered "Well Capitalized" as presented in the table below (dollar amounts in thousands).

	Actual		Well Capitalized Levels	
	Amount	Ratio	Amount	Ratio
Total Capital to Risk-Weighted Assets	\$ 1,522,034	18.77%	\$ 811,017	10.00%
Tier 1 (Leverage) Capital to Net Average Assets	1,484,739	10.19%	728,372	5.00%
Tier 1 Capital to Risk-Weighted Assets	1,484,739	18.31%	648,813	8.00%
Common Equity Tier 1 Capital to Risk-Weighted Assets	1,484,725	18.31%	527,161	6.50%

The capital ratios of the Company as of December 31, 2019 are presented in the table below (dollar amounts in thousands).

	Actual	
	Amount	Ratio
Total Capital to Risk-Weighted Assets	\$ 1,787,553	22.02%
Tier 1 (Leverage) Capital to Net Average Assets	1,750,261	11.99%
Tier 1 Capital to Risk-Weighted Assets	1,750,261	21.56%
Common Equity Tier 1 Capital to Risk-Weighted Assets	1,750,261	21.56%

In addition to the operational liquidity considerations described above, which are primarily those of the Association, the Company, as a separate legal entity, also monitors and manages its own, parent company-only liquidity, which provides the source of funds necessary to support all of the parent company's stand-alone operations, including its capital distribution strategies which encompass its share repurchase and dividend payment programs. The Company's primary source of liquidity is dividends received from the Association. The amount of dividends that the Association may declare and pay to the Company in any calendar year, without the receipt of prior approval from the OCC but with prior notice to the FRB-Cleveland, cannot exceed net income for the current calendar year-to-date period plus retained net income (as defined) for the preceding two

calendar years, reduced by prior dividend payments made during those periods. In December 2019, the Company received a \$57.0 million cash dividend from the Association. Because of its intercompany nature, this dividend payment had no impact on the Company's capital ratios or its consolidated statement of condition but reduced the Association's reported capital ratios. At December 31, 2019, the Company had, in the form of cash and a demand loan from the Association, \$222.8 million of funds readily available to support its stand-alone operations.

The Company's eighth stock repurchase program, which authorized the repurchase of up to 10,000,000 shares of the Company's outstanding common stock was approved by the Board of Directors on October 27, 2016 and repurchases began on January 6, 2017. There were 4,107,921 shares repurchased under that program between its start date and December 31, 2019. During the three months ended December 31, 2019, the Company repurchased \$0.4 million of its common stock.

On July 16, 2019, Third Federal Savings, MHC received the approval of its members with respect to the waiver of dividends, and subsequently received the non-objection of the FRB-Cleveland, to waive receipt of dividends on the Company's common stock the MHC owns up to a total of \$1.10 per share, to be declared on the Company's common stock during the 12 months subsequent to the members' approval (*i.e.*, through July 16, 2020). The members approved the waiver by casting 62% of the eligible votes in favor of the waiver. Of the votes cast, 97% were in favor of the proposal. Third Federal Savings, MHC waived its right to receive a \$0.27 per share dividend payment on September 17, 2019 and December 17, 2019.

The payment of dividends, support of asset growth and strategic stock repurchases are planned to continue in the future as the focus for future capital deployment activities.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

General. The majority of our assets and liabilities are monetary in nature. Consequently, our most significant form of market risk has historically been interest rate risk. In general, our assets, consisting primarily of mortgage loans, have longer maturities than our liabilities, consisting primarily of deposits and advances from the FHLB of Cincinnati. As a result, a fundamental component of our business strategy is to manage interest rate risk and limit the exposure of our net interest income to changes in market interest rates. Accordingly, our Board of Directors has established risk parameter limits deemed appropriate given our business strategy, operating environment, capital, liquidity and performance objectives. Additionally, our Board of Directors has authorized the formation of an Asset/Liability Management Committee comprised of key operating personnel, which is responsible for managing this risk in a manner that is consistent with the guidelines and risk limits approved by the Board of Directors. Further, the Board has established the Directors Risk Committee, which, among other responsibilities, conducts regular oversight and review of the guidelines, policies and deliberations of the Asset/Liability Management Committee. We have sought to manage our interest rate risk in order to control the exposure of our earnings and capital to changes in interest rates. As part of our ongoing asset-liability management, we use the following strategies to manage our interest rate risk:

- (i) marketing adjustable-rate and shorter-maturity (10-year, fixed-rate mortgage) loan products;
- (ii) lengthening the weighted average remaining term of major funding sources, primarily by offering attractive interest rates on deposit products, particularly longer-term certificates of deposit, and through the use of longer-term advances from the FHLB of Cincinnati (or shorter-term advances converted to longer-term durations via the use of interest rate exchange contracts that qualify as cash flow hedges) and longer-term brokered certificates of deposit;
- (iii) investing in shorter- to medium-term investments and mortgage-backed securities;
- (iv) maintaining the levels of capital required for "well capitalized" designation; and
- (v) securitizing and/or selling long-term, fixed-rate residential real estate mortgage loans.

During the three months ended December 31, 2019, \$109.5 million of agency-compliant, long-term, fixed-rate mortgage loans were sold to Fannie Mae on a servicing retained basis. Additionally, during the three months ended December 31, 2019, \$99.0 million of fixed-rate loans were sold, on a servicing retained basis, in a single bulk sale to a private investor. At December 31, 2019, \$9.6 million of agency-compliant, long-term, fixed-rate residential first mortgage loans that qualified under Fannie Mae's Home Ready program, were classified as "held for sale." Of the agency-compliant loan sales during the three months ended December 31, 2019, \$9.6 million was comprised of long-term (15 to 30 years), fixed-rate first mortgage loans which were sold under Fannie Mae's Home Ready program, and \$99.9 million was comprised of long-term (15 to 30 years), fixed-rate first mortgage loans which had been originated under our revised procedures and were sold to Fannie Mae under our reinstated seller contract, as described in the next paragraph. At December 31, 2019, we did not have any outstanding loan sales commitments.

First mortgage loans (primarily fixed-rate, mortgage refinances with terms of 15 years or more, and Home Ready) are originated under Fannie Mae procedures and are eligible for sale to Fannie Mae either as whole loans or within mortgage-

backed securities. We expect that certain loan types (i.e. our Smart Rate adjustable-rate loans, home purchase fixed-rate loans and 10-year fixed-rate loans) will continue to be originated under our legacy procedures, which are not eligible for sale to Fannie Mae. For loans that are not originated under Fannie Mae procedures, the Association's ability to reduce interest rate risk via loan sales is limited to those loans that have established payment histories, strong borrower credit profiles and are supported by adequate collateral values that meet the requirements of the FHLB's Mortgage Purchase Program or of private third-party investors.

The Association actively markets equity lines of credit, an adjustable-rate mortgage loan product and a 10-year fixed-rate mortgage loan product. Each of these products provides us with improved interest rate risk characteristics when compared to longer-term, fixed-rate mortgage loans. Shortening the average maturity of our interest-earning assets by increasing our investments in shorter-term loans and investments, as well as loans and investments with variable rates of interest, helps to better match the maturities and interest rates of our assets and liabilities, thereby reducing the exposure of our net interest income to changes in market interest rates.

The Association evaluates funding source alternatives as it seeks to extend its liability duration. Extended duration funding sources that are currently considered include: retail certificates of deposit (which, subject to a fee, generally provide depositors with an early withdrawal option, but do not require pledged collateral); brokered certificates of deposit (which generally do not provide an early withdrawal option and do not require collateral pledges); collateralized borrowings which are not subject to creditor call options (generally advances from the FHLB of Cincinnati); and interest rate exchange contracts ("swaps") which are subject to collateral pledges and which require specific structural features to qualify for hedge accounting treatment (hedge accounting treatment directs that periodic mark-to-market adjustments be recorded in other comprehensive income (loss) in the equity section of the balance sheet rather than being included in operating results of the income statement). The Association's intent is that any swap to which it may be a party will qualify for hedge accounting treatment. The Association attempts to be opportunistic in the timing of its funding duration deliberations and when evaluating alternative funding sources, compares effective interest rates, early withdrawal/call options and collateral requirements.

The Association is a party to interest rate swap agreements. Each of the Association's swap agreements is registered on the Chicago Mercantile Exchange and involves the exchange of interest payment amounts based on a notional principal balance. No exchange of principal amounts occur and the notional principal amount does not appear on our balance sheet. The Association uses swaps to extend the duration of its funding sources. In each of the Association's agreements, interest paid is based on a fixed rate of interest throughout the term of each agreement while interest received is based on an interest rate that resets at a specified interval (generally three months) throughout the term of each agreement. On the initiation date of the swap, the agreed upon exchange interest rates reflect market conditions at that point in time. Swaps generally require counterparty collateral pledges that ensure the counterparties' ability to comply with the conditions of the agreement. The notional amount of the Association's swap portfolio at December 31, 2019 was \$2.80 billion. The swap portfolio's weighted average fixed pay rate was 1.91% and the weighted average remaining term was 3.5 years. Concurrent with the execution of each swap, the Association entered into a short-term borrowing from the FHLB of Cincinnati in an amount equal to the notional amount of the swap and with interest rate resets aligned with the reset interval of the swap. Each individual swap agreement has been designated as a cash flow hedge of interest rate risk associated with the Company's variable rate borrowings from the FHLB of Cincinnati.

Economic Value of Equity. Using customized modeling software, the Association prepares periodic estimates of the amounts by which the net present value of its cash flows from assets, liabilities and off-balance sheet items (the institution's economic value of equity or EVE) would change in the event of a range of assumed changes in market interest rates. The simulation model uses a discounted cash flow analysis and an option-based pricing approach in measuring the interest rate sensitivity of EVE. The model estimates the economic value of each type of asset, liability and off-balance sheet contract under the assumption that instantaneous changes (measured in basis points) occur at all maturities along the United States Treasury yield curve and other relevant market interest rates. A basis point equals one, one-hundredth of one percent, and 100 basis points equals one percent. An increase in interest rates from 2% to 3% would mean, for example, a 100 basis point increase in the "Change in Interest Rates" column below. The model is tailored specifically to our organization, which, we believe, improves its predictive accuracy. The following table presents the estimated changes in the Association's EVE at December 31, 2019 that would result from the indicated instantaneous changes in the United States Treasury yield curve and other relevant market interest rates. Computations of prospective effects of hypothetical interest rate changes are based on numerous assumptions, including relative levels of market interest rates, loan prepayments and deposit decay, and should not be relied upon as indicative of actual results.

Change in Interest Rates (basis points) (1)	Estimated EVE (2)	Estimated Increase (Decrease) in EVE		EVE as a Percentage of Present Value of Assets (3)	
		Amount	Percent	EVE Ratio (4)	Increase (Decrease) (basis points)
+300	\$ 1,363,208	\$ (402,171)	(22.78)%	9.83%	(199)
+200	1,516,548	(248,831)	(14.10)%	10.65%	(117)
+100	1,651,271	(114,108)	(6.46)%	11.31%	(51)
0	1,765,379	—	—	11.82%	—
-100	1,717,147	(48,232)	(2.73)%	11.29%	(53)

- (1) Assumes an instantaneous uniform change in interest rates at all maturities.
- (2) EVE is the discounted present value of expected cash flows from assets, liabilities and off-balance sheet contracts.
- (3) Present value of assets represents the discounted present value of incoming cash flows on interest-earning assets.
- (4) EVE Ratio represents EVE divided by the present value of assets.

The table above indicates that at December 31, 2019, in the event of an increase of 200 basis points in all interest rates, the Association would experience a 14.10% decrease in EVE. In the event of a 100 basis point decrease in interest rates, the Association would experience a 2.73% decrease in EVE.

The following table is based on the calculations contained in the previous table, and sets forth the change in the EVE at a +200 basis point rate of shock at December 31, 2019, with comparative information as of September 30, 2019. The Association changed the software model used to measure its interest rate risk during the three months ended December 31, 2019, which included the use of different valuation approaches and assumptions inherent in the software. By regulation, the Association must measure and manage its interest rate risk for interest rate shocks relative to established risk tolerances in EVE.

Risk Measure (+200 Basis Points Rate Shock)

	At December 31, 2019	At September 30, 2019
Pre-Shock EVE Ratio	11.82 %	14.93 %
Post-Shock EVE Ratio	10.65 %	13.26 %
Sensitivity Measure in basis points	(117)	(167)
Percentage Change in EVE	(14.10)%	(15.78)%

Certain shortcomings are inherent in the methodologies used in measuring interest rate risk through changes in EVE. Modeling changes in EVE require making certain assumptions that may or may not reflect the manner in which actual yields and costs respond to changes in market interest rates. In this regard, the EVE tables presented above assume:

- no new growth or business volumes;
- that the composition of our interest-sensitive assets and liabilities existing at the beginning of a period remains constant over the period being measured, except for reductions to reflect mortgage loan principal repayments along with modeled prepayments and defaults; and
- that a particular change in interest rates is reflected uniformly across the yield curve regardless of the duration or repricing of specific assets and liabilities.

Accordingly, although the EVE tables provide an indication of our interest rate risk exposure as of the indicated dates, such measurements are not intended to and do not provide a precise forecast of the effect of changes in market interest rates on our EVE and will differ from actual results. In addition to our core business activities, which primarily sought to originate Smart Rate (adjustable), home equity lines of credit (adjustable) and 10-year fixed-rate loans funded by borrowings from the FHLB and intermediate term CDs (including brokered CDs), and which are intended to have a favorable impact on our IRR profile, the impact of several other items and events resulted in the 1.68% improvement in the Percentage Change in EVE measure at December 31, 2019 when compared to the measure at September 30, 2019. Factors contributing to this improvement included changes in market rates, capital actions by the Association, assumption and modeling changes, including a change in the software model used, and changes due to business activity. Movement in market interest rates included a decrease of five basis points for the two-year term, an increase of 15 basis points for the five-year term and an increase of 25 basis points for the ten-year term. Negatively impacting the Percentage Change in EVE was a \$57.0 million cash dividend that

the Association paid to the Company. Because of its intercompany nature, this payment had no impact on the Company's capital position, or the Company's overall IRR profile, but reduced the Association's regulatory capital and regulatory capital ratios and negatively impacted the Association's Percentage Change in EVE by approximately 0.44%. Additionally, modifications and enhancements to our modeling assumptions and methodologies, as a result of the model software change, impacted the Association's Percentage Change in EVE. While our core business activities, as described at the beginning of this paragraph, are generally intended to have a positive impact on our IRR profile, the actual impact is determined by a number of factors, including the pace of mortgage asset additions to our balance sheet (including consideration of outstanding commitments to originate those assets) in comparison to the pace of the addition of duration extending funding sources. The IRR simulation results presented above were in line with management's expectations and were within the risk limits established by our Board of Directors.

Our simulation model possesses random patterning capabilities and accommodates extensive regression analytics applicable to the prepayment and decay profiles of our borrower and depositor portfolios. The model facilitates the generation of alternative modeling scenarios and provides us with timely decision making data that is integral to our IRR management processes. Modeling our IRR profile and measuring our IRR exposure are processes that are subject to continuous revision, refinement, modification, enhancement, back testing and validation. We continually evaluate, challenge and update the methodology and assumptions used in our IRR model, including behavioral equations that have been derived based on third-party studies of our customer historical performance patterns. Changes to the methodology and/or assumptions used in the model will result in reported IRR profiles and reported IRR exposures that will be different, and perhaps significantly, from the results reported above.

Earnings at Risk. In addition to EVE calculations, we use our simulation model to analyze the sensitivity of our net interest income to changes in interest rates (the institution's EaR). Net interest income is the difference between the interest income that we earn on our interest-earning assets, such as loans and securities, and the interest that we pay on our interest-bearing liabilities, such as deposits and borrowings. In our model, we estimate what our net interest income would be for prospective 12 and 24 month periods using customized (based on our portfolio characteristics) assumptions with respect to loan prepayment rates, default rates and deposit decay rates, and the implied forward yield curve as of the market date for assumptions as to projected interest rates. We then calculate what the estimated net interest income would be for the same period under numerous interest rate scenarios. The simulation process is subject to continual enhancement, modification, refinement and adaptation, including the replacement of the software model used during the current quarter, in order that it might most accurately reflect our current circumstances, factors and expectations. As of December 31, 2019, we estimated that our EaR for the 12 months ending December 31, 2020 would increase by 0.50% in the event that market interest rates used in the simulation were adjusted in equal monthly amounts (termed a "ramped" format) during the 12 month measurement period to an aggregate increase in 200 basis points. The Association uses the "ramped" assumption in preparing the EaR simulation estimates for use in its public disclosures. In addition to conforming to predominate industry practice, the Association also believes that the ramped assumption provides a more probable/plausible scenario for net interest income simulations than instantaneous shocks which provide a theoretical analysis but a much less credible economic scenario. The Association continues to calculate instantaneous scenarios, and as of December 31, 2019, we estimated that our EaR for the 12 months ending December 31, 2020, would decrease by 3.15% in the event of an instantaneous 200 basis point increase in market interest rates.

Certain shortcomings are also inherent in the methodologies used in determining interest rate risk through changes in EaR. Modeling changes in EaR require making certain assumptions that may or may not reflect the manner in which actual yields and costs respond to changes in market interest rates. In this regard, the interest rate risk information presented above assumes that a particular change in interest rates is reflected uniformly across the yield curve regardless of the duration or repricing of specific assets and liabilities. Accordingly, although interest rate risk calculations provide an indication of our interest rate risk exposure at a particular point in time, such measurements are not intended to and do not provide a precise forecast of the effect of changes in market interest rates on our net interest income and will differ from actual results. In addition to the preparation of computations as described above, we also formulate simulations based on a variety of non-linear changes in interest rates and a variety of non-constant balance sheet composition scenarios.

Other Considerations. The EVE and EaR analyses are similar in that they both start with the same month end balance sheet amounts, weighted average coupon and maturity. The underlying prepayment, decay and default assumptions are also the same and they both start with the same month end "markets" (Treasury and Libor yield curves, etc.). From that similar starting point, the models follow divergent paths. EVE is a stochastic model using 100 different interest rate paths to compute market value at the account level for each of the categories on the balance sheet whereas EaR uses the implied forward curve to compute interest income/expense at the account level for each of the categories on the balance sheet.

EVE is considered as a point in time calculation with a "liquidation" view of the Association where all the cash flows (including interest, principal and prepayments) are modeled and discounted using discount factors derived from the current

market yield curves. It provides a long term view and helps to define changes in equity and duration as a result of changes in interest rates. On the other hand, EaR is based on balance sheet projections going one year and two years forward and assumes new business volume and pricing to calculate net interest income under different interest rate environments. EaR is calculated to determine the sensitivity of net interest income under different interest rate scenarios. With each of these models, specific policy limits have been established that are compared with the actual month end results. These limits have been approved by the Association's Board of Directors and are used as benchmarks to evaluate and moderate interest rate risk. In the event that there is a breach of policy limits that extends beyond two consecutive quarter end measurement periods, management is responsible for taking such action, similar to those described under the preceding heading of *General*, as may be necessary in order to return the Association's interest rate risk profile to a position that is in compliance with the policy. At December 31, 2019, the IRR profile as disclosed above was within our internal limits.

Item 4. Controls and Procedures

Under the supervision of and with the participation of the Company's management, including our principal executive officer and principal financial officer, we have evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) or 15d-15(e) under the Exchange Act) as of the end of the period covered by this report. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by an issuer in the reports that it files or submits under the Act is accumulated and communicated to the issuer's management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure. Based upon that evaluation, our principal executive officer and principal financial officer concluded that, as of the end of the period covered by this report, our disclosure controls and procedures were effective to ensure that information required to be disclosed in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms.

No change in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) occurred during the most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Part II — Other Information

Item 1. Legal Proceedings

The Company and its subsidiaries are subject to various legal actions arising in the normal course of business. In the opinion of management as of December 31, 2019, the resolution of these legal actions is not expected to have a material adverse effect on the Company's financial condition or results of operations.

Item 1A. Risk Factors

There have been no material changes in the "Risk Factors" previously disclosed in our Annual Report on Form 10-K, filed with the SEC on November 26, 2019 (File No. 001-33390).

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

- (a) Not applicable
- (b) Not applicable
- (c) The following table summarizes our stock repurchase activity during the quarter ended December 31, 2019.

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans (1)	Maximum Number of Shares that May Yet be Purchased Under the Plans
October 1, 2019 through October 31, 2019	19,500	\$ 18.35	19,500	5,892,079
November 1, 2019 through November 30, 2019	—	—	—	5,892,079
December 1, 2019 through December 31, 2019	—	—	—	5,892,079
	<u>19,500</u>	18.35	<u>19,500</u>	

- (1) On October 27, 2016, the Company announced that the Board of Directors approved the Company's eighth stock repurchase program, which authorized the repurchase of up to 10,000,000 shares of the Company's outstanding common stock. Purchases under the program will be on an ongoing basis and subject to the availability of stock, general market conditions, the trading price of the stock, alternative uses of capital, and our financial performance. Repurchased shares will be held as treasury stock and be available for general corporate use. The repurchase program commenced in January 2017.

On July 16, 2019, at a special meeting of Third Federal Savings, MHC, the members (depositors and certain loan customers of the Association) voted to approve Third Federal Savings, MHC's proposed waiver of dividends, aggregating up to \$1.10 per share, to be declared on the Company's common stock during the four quarterly periods ending June 30, 2020. The members approved the waiver by casting 62% of the eligible votes in favor of the waiver. Of the votes cast, 97% were in favor of the proposal. Third Federal Savings, MHC is the 81% majority shareholder of the Company.

Following the receipt of the members' approval at the July 16, 2019 special meeting, Third Federal Savings, MHC filed a notice with, and subsequently received the non-objection of the FRB-Cleveland for the proposed dividend waivers.

Item 3. Defaults Upon Senior Securities

Not applicable

Item 4. Mine Safety Disclosures

Not applicable

Item 5. Other Information

Not applicable

Item 6.

(a) Exhibits

[31.1 Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002](#)

[31.2 Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002](#)

[32 Certification of Chief Executive Officer and Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002](#)

The following unaudited financial statements from TFS Financial Corporation's Quarterly Report on Form 10-Q for the quarter ended December 31, 2019, filed on February 6, 2020, formatted in Inline XBRL (Extensible Business Reporting Language) includes: (i) Consolidated Statements of Condition, (ii) Consolidated Statements of Income, (iii) Consolidated Statements of Comprehensive Income, (iv) Consolidated Statements of Shareholders' Equity, (v) Consolidated Statements of Cash Flows, (vi) Notes to Unaudited Interim Consolidated Financial Statements.

101.INS	Interactive datafile	XBRL Instance Document - the instance document does not appear in the Interactive Data File because its XBRL tags are embedded within the Inline XBRL document.
101.SCH	Interactive datafile	Inline XBRL Taxonomy Extension Schema Document
101.CAL	Interactive datafile	Inline XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	Interactive datafile	Inline XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	Interactive datafile	Inline XBRL Taxonomy Extension Label Linkbase
101.PRE	Interactive datafile	Inline XBRL Taxonomy Extension Presentation Linkbase Document

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.

TFS Financial Corporation

Dated: February 6, 2020

/s/ Marc A. Stefanski

Marc A. Stefanski

**Chairman of the Board, President
and Chief Executive Officer**

Dated: February 6, 2020

/s/ Paul J. Huml

Paul J. Huml

Chief Financial Officer

Exhibit 31.1

Certification of Chief Executive Officer

Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Marc A. Stefanski, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of TFS Financial Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Dated: February 6, 2020

/S/ MARC A. STEFANSKI

Marc A. Stefanski

**Chairman of the Board, President
and Chief Executive Officer**

Exhibit 31.2

**Certification of Chief Financial Officer
Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002**

I, Paul J. Huml, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of TFS Financial Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Dated: February 6, 2020

/S/ PAUL J. HUML

Paul J. Huml
Chief Financial Officer

Exhibit 32

**Certification of Chief Executive Officer and Chief Financial Officer
Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002**

Marc A. Stefanski, Chairman of the Board, President and Chief Executive Officer, and Paul J. Huml, Chief Financial Officer of TFS Financial Corporation (the "Company") each certify in his capacity as an officer of the Company that he has reviewed the quarterly Report on Form 10-Q for the quarter ended December 31, 2019 and that to the best of his knowledge:

- (1) the report fully complies with the requirements of Sections 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) the information contained in the report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: February 6, 2020

/S/ MARC A. STEFANSKI

Marc A. Stefanski

**Chairman of the Board, President
and Chief Executive Officer**

Dated: February 6, 2020

/S/ PAUL J. HUML

Paul J. Huml

Chief Financial Officer

A signed original of this written statement required by Section 906 has been provided to TFS Financial Corporation and will be retained by TFS Financial Corporation and furnished to the Securities and Exchange Commission or its staff upon request.
