

FS Bancorp, Inc.  
Form 10-K  
April 01, 2013  
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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-K  
(Mark one)

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

For the fiscal year ended December 31, 2012      OR

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

Commission File Number: 001-35589

FS BANCORP, INC.  
(Exact name of registrant as specified in its charter)

Washington      45-4585178  
(State or other jurisdiction of incorporation or organization)      (I.R.S. Employer Identification Number)

6920 220<sup>th</sup> Street SW, Mountlake Terrace, Washington      98043  
(Address of principal executive offices)      (Zip Code)

Registrant's telephone number, including area code:      (425) 771-5299

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

Securities registered pursuant to Section 12(g) of the Act:      Common Stock, par value \$0.01 per share  
(Title of Each Class)

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

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

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

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

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

Large accelerated filer

Accelerated filer

Non-accelerated filer  (Do not check if a smaller reporting company)

Smaller reporting company

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

As of March 27, 2013, there were 3,240,125 shares of the Registrant's common stock outstanding. The Registrant's common stock is listed on the NASDAQ Capital Market under the symbol "FSBW." The aggregate market value of the common stock held by non affiliates of the Registrant, based on the closing sales price of the Registrant's common stock as quoted on the NASDAQ Capital Market on June 30, 2012, was not applicable as no stock was outstanding. On July 9, 2012 the 1st Security Bank of Washington completed its conversion from a mutual savings bank to a stock savings bank and the Company issued an aggregate of 3,240,125 shares of common stock on that date in connection with the mutual to stock conversion.

#### DOCUMENTS INCORPORATED BY REFERENCE

1. Portions of the Annual Report to Shareholders are incorporated by reference into Part II.
  2. Portions of the definitive Proxy Statement for the 2013 Annual Meeting of Shareholders ("Proxy Statement") are incorporated by reference into Part III.
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As used in this report, the terms “we,” “our,” “us,” and “FS Bancorp” refer to FS Bancorp, Inc. and its consolidated subsidiary, 1st Security Bank of Washington, unless the context indicates otherwise.

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Forward Looking Statements

This Form 10-K contains forward looking statements, which can be identified by the use of words such as “believes,” “expects,” “anticipates,” “estimates” or similar expressions. Forward looking statements include:

- statements of our goals, intentions and expectations;
- statements regarding our business plans, prospects, growth and operating strategies;
- statements regarding the 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 and uncertainties. Actual results may differ materially from those contemplated by the forward looking statements due to, among others, the following factors:

- general economic conditions, either nationally or in our market area, that are worse than expected;
- the credit risks of lending activities, including changes in the level and trend of loan delinquencies and write offs and
- changes in our allowance for loan losses and provision for loan losses that may be impacted by deterioration in the housing and commercial real estate markets;
- fluctuations in the demand for loans, the number of unsold homes, land and other properties and fluctuations in real estate values in our market area;
- increases in premiums for deposit insurance;
- the use of estimates in determining fair value of certain of our assets, which estimates may prove to be incorrect and result in significant declines in valuation;
- changes in the interest rate environment that reduce our interest margins or reduce the fair value of financial instruments;
- increased competitive pressures among financial services companies;
- our ability to execute our plans to grow our residential construction lending, our mortgage banking operations and our warehouse lending and the geographic expansion of our indirect home improvement lending;
- our ability to attract and retain deposits;
- our ability to control operating costs and expenses;
- changes in consumer spending, borrowing and savings habits;
- our ability to successfully manage our growth;
- legislative or regulatory changes that adversely affect our business, including the effect of the Dodd-Frank Wall Street Reform and Consumer Protection Act, changes in regulation policies and principles, or the interpretation of regulatory capital or other rules, including as a result of Basel III;
- adverse changes in the securities markets;
- changes in accounting policies and practices, as may be adopted by the bank regulatory agencies, the Public Company Accounting Oversight Board or the Financial Accounting Standards Board;
- costs and effects of litigation, including settlements and judgments;
- our ability to implement our branch expansion strategy;
- inability of key third-party vendors to perform their obligations to us; and
- other economic, competitive, governmental, regulatory and technical factors affecting our operations, pricing, products and services and other risks described elsewhere in this Form 10-K and our other reports filed with the U.S. Securities and Exchange Commission.

Any of the forward looking statements that we make in this Form 10-K and in other public statements we make may turn out to be wrong because of inaccurate assumptions we might make, because of the factors illustrated above or because of other factors that we cannot foresee. Because of these and other uncertainties, our actual future results may be materially different from the results indicated by these forward looking statements and you should not rely on such statements.



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Available Information

The Company provides a link on its investor information page at [www.fsbwa.com](http://www.fsbwa.com) to filings with the U.S. Securities and Exchange Commission (“SEC”) for purposes of providing copies of its annual report to shareholders, annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and press releases. Other than an investor’s own internet access charges, these filings are available free of charge and also can be obtained by calling the SEC at 1-800-SEC-0330. The information contained on the Company’s website is not included as part of, or incorporated by reference into, this Annual Report on Form 10-K.

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PART 1

Item 1. Business

General

FS Bancorp, Inc. (“FS Bancorp” or the “Company”), a Washington corporation, was organized in September 2011 for the purpose of becoming the holding company of 1st Security Bank of Washington (“1st Security Bank of Washington” or the “Bank”) upon the Bank’s conversion from a mutual to a stock savings bank (“Conversion”). The Conversion was completed on July 9, 2012. At December 31, 2012, the Company had consolidated total assets of \$359.0 million, total deposits of \$288.9 million and stockholders’ equity of \$59.9 million. The Company has not engaged in any significant activity other than holding the stock of the Bank. Accordingly, the information set forth in this Annual Report on Form 10-K (“Form 10-K”), including the consolidated financial statements and related data, relates primarily to the Bank.

1st Security Bank of Washington is a relationship-driven community bank. The Bank delivers banking and financial services to local families, local and regional businesses and industry niches within distinct Puget Sound area communities. The Bank emphasizes long-term relationships with families and businesses within the communities served, working with them to meet their financial needs. The Bank is also actively involved in community activities and events within these market areas, which further strengthens relationships within these markets. The Bank has been serving the Puget Sound area since 1936. Originally chartered as a credit union, and known as Washington’s Credit Union, the Bank served various select employment groups. On April 1, 2004, the Bank converted from a credit union to a Washington state-chartered mutual savings bank. Upon completion of the Conversion in July 2012, 1st Security Bank of Washington became a Washington state-chartered stock savings bank and the wholly owned subsidiary of the Company. At December 31, 2012, the Bank maintained six bank branch locations and one loan origination branch, along with the headquarters.

1st Security Bank of Washington is a diversified lender with a focus on the origination of home improvement loans, commercial real estate mortgage loans, commercial business loans and second mortgage/home equity loan products. Consumer loans, in particular indirect home improvement loans, represent the largest portion of the loan portfolio and have traditionally been the mainstay of the Bank’s lending strategy, a carryover from its days as a credit union. Going forward, the Bank plans to place more emphasis on certain lending products, such as commercial real estate, commercial business and residential construction lending, while maintaining the current size of the consumer loan portfolio. The Bank also reintroduced in-house originations of residential mortgage loans in 2012, primarily for sale into the secondary market, through a mortgage banking program. Future lending strategies are intended to take advantage of: (1) the Bank’s historical strength in indirect consumer lending, (2) recent market dislocation that has created new lending opportunities, and (3) relationship lending. Retail deposits will continue to serve as an important funding source. For more information regarding the business and operations of 1st Security Bank of Washington, see Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operations.”

1st Security Bank of Washington is examined and regulated by the Washington Department of Financial Institutions (“DFI”), its primary regulator, and by the Federal Deposit Insurance Corporation (“FDIC”). 1st Security Bank of Washington is required to have certain reserves set by the Board of Governors of the Federal Reserve System (“Federal Reserve”) and is a member of the Federal Home Loan Bank of Seattle (“FHLB” or “FHLB of Seattle”), which is one of the 12 regional banks in the Federal Home Loan Bank System.

The principal executive offices of the Company are located at 6920 220th Street SW, Mountlake Terrace, Washington 98043 and its telephone number is (425) 771-5299.

Market Area

The Bank conducts operations out of the main administrative office, one home lending office and six full-service bank branch offices in the Puget Sound region of Washington. The administrative office is located in Mountlake Terrace, in



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Snohomish County, Washington. The home lending office is located in Bellevue, in King County, Washington. Three branch offices are located in Snohomish County, while there is one office each in King and Pierce Counties to the south and Kitsap County to the west. One branch is scheduled to open in the second quarter of 2013 and will be located in Seattle, King County, Washington.

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The primary market area for business operations is the Seattle-Tacoma-Bellevue, WA Metropolitan Statistical Area (the "Seattle MSA"). Kitsap County, though not in the Seattle MSA, is also part of the Bank's market area. This overall region is typically known as the "Puget Sound" region. The population of the Puget Sound region was an estimated 3.8 million in 2011, over half of the state's population, representing a large population base for potential business. The region has a well-developed urban area in the western portion along Puget Sound, with the north, central and eastern portions containing a mixture of developed residential and commercial neighborhoods and undeveloped, rural neighborhoods.

The Puget Sound region is the largest business center in both the state of Washington and the Pacific Northwest. Currently, key elements of the economy are aerospace, military bases, clean technology, biotechnology, education, information technology, logistics, international trade and tourism. The region is well known for the long presence of The Boeing Corporation and Microsoft, two major industry leaders, and for its leadership in technology. The workforce in general is well-educated and strong in technology. Washington state's location with regard to the Pacific Rim, along with a deepwater port has made international trade a significant part of the regional economy. Tourism has also developed into a major industry for the area, due to the scenic beauty, temperate climate and easy accessibility. King County, the location of the city of Seattle, has the largest employment base and overall level of economic activity. King County's largest employers include The Boeing Company, Microsoft Corporation, and the University of Washington. Companies that are headquartered in King County include Alaska Airlines, Amazon.com, Costco, Starbucks and Microsoft. Pierce County's economy is also well diversified with the presence of military related government employment (Joint Base Lewis-McChord), along with health care (the Franciscan Health System and the Multicare Health System). In addition, there is a large employment base in the economic sectors of shipping (the Port of Tacoma) and aerospace employment (Boeing). Snohomish County to the north has an economy based on aerospace employment (Boeing), military (the Everett Naval Station) along with additional employment concentrations in biotechnology, electronics/computers, and wood products. Eight of the largest employers in the state are headquartered in King County.

The United States Navy is a key element for Kitsap County's economy. The United States Navy is the largest employer in the county, with installations at Puget Sound Naval Shipyard, Naval Undersea Warfare Center Keyport and Naval Base Kitsap (which comprises former Naval Submarine Base Bangor, and Naval Station Bremerton). The largest private employers in the county are the Harrison Medical Center, Wal-Mart, and Port Madison Enterprises. The 2011 median household income and per capita income levels in King, Snohomish, and Kitsap Counties were higher than the state and national averages, while Pierce County reported income levels slightly below the Washington state average. Approximately 86.6% of King County households had income levels in excess of \$50,000 annually in 2010, compared to 82.5% for the state of Washington and 79.2% for the United States. In 2008, the U.S. Census Bureau determined that Seattle has the highest percentage of college and university graduates of any U.S. city; it was listed as the most literate or second most literate city of the country every year since 2005. Seattle's high income and education levels, especially compared to other major cities, result in King County ranking in the top 100 wealthiest counties in the United States.

Unemployment in Washington was an estimated 7.6% as of December 31, 2012, down from a high of 10.2% in March 2010, closely paralleling national trends. Unemployment rates in Pierce, Kitsap, King, Snohomish counties have improved in the last 24 months after dropping from their 2010 first quarter highs. As of December 2012, Kitsap County and King County reported rates slightly lower than the state and national averages, at 6.1% and 7.0%, respectively. Year end 2012 estimated unemployment in Pierce County was 8.5%, and estimated unemployment in Snohomish County was 6.7%. Of the four counties, Snohomish and King Counties reflected the largest improvement year over year with unemployment dropping 1.3% in Snohomish County and 1.0% in King County.

According to the Washington Center for Real Estate Research, home values in the state of Washington began improving in the first half of 2012. For the quarter ended June 30, 2012, the average home value was \$261,000 in Snohomish County, \$195,000 in Pierce County, \$371,000 in King County, and \$242,000 in Kitsap County. Compared to the statewide average increase in home values of 4.0% over the second quarter, Snohomish and King counties have

performed at the highest level, with 8.2% and 6.5% increases, respectively. Kitsap County increased 3.1% year over year, slightly below the state average. Pierce County continued to experience a slight decline with home prices declining 0.9% year over year. King County has experienced a dramatic increase in building permits with a 100.5% increase year over year as of December 31, 2012.

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For a discussion regarding the competition in the Company’s primary market area, see “—Competition.”

Lending Activities

General. Historically, while operating as a credit union, the primary emphasis was the origination of consumer loans (primarily indirect home improvement and automobile-secured loans), one-to-four-family residential first mortgages, and second mortgage/home equity loan products. More recently, while maintaining the active indirect consumer lending program, the Bank has shifted the lending focus to non-mortgage commercial business loans, as well as commercial real estate and residential construction and development loans. The Bank has also reintroduced in-house originations of residential mortgage loans in 2012, primarily for sale in the secondary market. While maintaining the Bank’s historical strength in consumer lending, the Bank recently added management and personnel in the commercial lending area to take advantage of the relatively favorable long-term business and economic environments prevailing in the markets for small business lending.

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Loan Portfolio Analysis. The following table sets forth the composition of the loan portfolio by type of loan at the dates indicated.

	December 31,		2011		2010		2009		2008		Percent
	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent	
(Dollars in thousands)											
Real estate loans											
Commercial	\$33,250	11.88 %	\$28,931	13.09 %	\$28,061	11.86 %	\$29,099	12.20 %	\$25,872	11.33 %	
Construction and development	31,893	11.39	10,144	4.59	9,805	4.15	17,390	7.29	23,861	10.45	
Home equity	15,474	5.53	14,507	6.56	15,655	6.62	16,448	6.90	18,689	8.19	
One-to-four-family <sup>(1)</sup>	13,976	4.99	8,752	3.96	13,218	5.59	8,233	3.45	6,969	3.05	
Multi-family	3,202	1.14	1,175	0.53	1,159	0.49	409	0.17	408	0.18	
Total real estate loans	97,795	34.93	63,509	28.73	67,898	28.71	71,579	30.01	75,799	33.20	
Consumer Loans											
Indirect home improvement	86,249	30.82	81,143	36.70	94,833	40.10	89,883	37.68	75,203	32.94	
Recreational	17,968	6.42	24,471	11.07	24,105	10.19	18,011	7.55	12,165	5.33	
Automobile	2,416	0.86	5,832	2.64	12,645	5.35	23,359	9.79	30,514	13.37	
Home improvement	651	0.23	934	0.42	1,295	0.55	1,725	0.72	2,203	0.96	
Other	1,386	0.50	1,826	0.83	2,887	1.21	4,277	1.80	6,190	2.71	
Total consumer loans	108,670	38.83	114,206	51.66	135,765	57.40	137,255	57.54	126,275	55.31	
Commercial business loans	73,465	26.24	43,337	19.61	32,841	13.89	29,699	12.45	26,218	11.49	
Total gross loans receivable	279,930	100.00 %	221,052	100.00 %	236,504	100.00 %	238,533	100.00 %	228,292	100.00 %	
Less:											
Deferred costs, fees and discounts, net	(283 )		424		223		313		280		
Allowance for loan losses	(4,698 )		(4,345 )		(5,905 )		(7,405 )		(5,598 )		
Total loans receivable, net	\$274,949		\$217,131		\$230,822		\$231,441		\$222,974		

(1) Excludes loans held for sale.

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The following table shows the composition of the loan portfolio by fixed- and adjustable-rate loans at the dates indicated.

	December 31, 2012		2011		2010		2009		2008	
	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent
(Dollars in thousands)										
Fixed-rate loans:										
Real estate loans										
Commercial	\$20,947	7.48 %	\$17,578	7.95 %	\$16,333	6.90 %	\$15,729	6.59 %	\$16,449	7.20 %
Construction and development	3,958	1.41	3,407	1.54	1,556	0.66	501	0.21	105	0.05
Home equity	2,557	0.91	2,154	0.97	2,784	1.18	3,839	1.61	5,399	2.36
One-to-four-family <sup>(1)</sup>	8,328	2.98	5,452	2.47	6,585	2.79	4,552	1.91	6,159	2.70
Multi-family	2,053	0.73	1,175	0.53	1,159	0.49	409	0.17	405	0.17
Total real estate loans	37,843	13.51	29,766	13.46	28,417	12.02	25,030	10.49	28,517	12.48
Consumer	108,500	38.76	114,201	51.65	135,752	57.39	137,231	57.53	126,221	55.29
Commercial business	16,959	6.06	8,971	4.07	1,049	0.45	870	0.36	454	0.20
Total fixed-rate loans	163,302	58.33	152,938	69.18	165,218	69.86	163,131	68.38	155,192	67.97
Adjustable-rate loans:										
Real estate loans										
Commercial	12,303	4.40	11,353	5.14	11,728	4.96	13,370	5.61	9,423	4.13
Construction and development	27,935	9.98	6,737	3.05	8,249	3.49	16,889	7.08	23,756	10.40
Home equity	12,917	4.61	12,353	5.59	12,871	5.44	12,609	5.29	13,290	5.83
One-to-four-family <sup>(1)</sup>	5,648	2.02	3,300	1.49	6,633	2.80	3,681	1.54	810	0.35
Multi-family	1,149	0.41	—	—	—	—	—	—	—	—