

Kearny Financial Corp.
Form 10-Q
February 14, 2011

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended

December 31, 2010

OR

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

For the transition period from

to

Commission File Number 000-51093

KEARNY FINANCIAL CORP.

(Exact name of registrant as specified in its charter)

UNITED STATES
(State or other jurisdiction of
incorporation or
organization)

22-3803741
(I.R.S. Employer
Identification Number)

120 Passaic Ave., Fairfield, New Jersey
(Address of principal executive offices)

07004-3510
(Zip Code)

Registrant's telephone number, including area code

973-244-4500

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

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

Edgar Filing: Kearny Financial Corp. - Form 10-Q

Large accelerated filer []

Accelerated filer [X]

Non-accelerated filer []

Smaller reporting company []

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

The number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: February 8, 2011.

\$0.10 par value common stock - 67,975,477 shares outstanding

KEARNY FINANCIAL CORP. AND SUBSIDIARIES

INDEX

	Page Number
PART I - FINANCIAL INFORMATION	
Item 1: Financial Statements	
Consolidated Statements of Financial Condition at December 31, 2010 and June 30, 2010 (Unaudited)	1
Consolidated Statements of Operations for the Three and Six Months Ended December 31, 2010 and December 31, 2009 (Unaudited)	2-3
Consolidated Statements of Changes in Stockholders' Equity for the Six Months Ended December 31, 2010 and December 31, 2009 (Unaudited)	4-6
Consolidated Statements of Cash Flows for the Six Months Ended December 31, 2010 and December 31, 2009 (Unaudited)	7-8
Notes to Consolidated Financial Statements (Unaudited)	9-40
Item 2: Management's Discussion and Analysis of Financial Condition and Results of Operations	41-59
Item 3: Quantitative and Qualitative Disclosure About Market Risk	60-66
Item 4: Controls and Procedures	67
PART II - OTHER INFORMATION	68-69
SIGNATURES	70

KEARNY FINANCIAL CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION
(In Thousands, Except Share and Per Share Data, Unaudited)

	December 31, 2010	June 30, 2010
Assets		
Cash and amounts due from depository institutions	\$57,670	\$3,286
Interest-bearing deposits in other banks	72,658	178,136
Cash and Cash Equivalents	130,328	181,422
Securities available for sale (amortized cost \$127,157 and \$30,960)	125,569	29,497
Securities held to maturity (estimated fair value \$237,393 and \$256,914)	236,870	255,000
Loans receivable, including unamortized yield adjustments of \$(1,409) and \$564	1,319,354	1,013,713
Less allowance for loan losses	(9,931)	(8,561)
Net Loans Receivable	1,309,423	1,005,152
Mortgage-backed securities available for sale (amortized cost \$845,741 and \$673,414)	862,769	703,455
Mortgage-backed securities held to maturity (estimated fair value \$1,580 and \$1,754)	1,533	1,700
Premises and equipment	39,630	34,989
Federal Home Loan Bank of New York ("FHLB") stock	14,062	12,867
Interest receivable	10,425	8,338
Goodwill	108,543	82,263
Bank owned life insurance	24,099	19,833
Deferred income tax assets, net	5,598	-
Other assets	12,346	5,297
Total Assets	\$2,881,195	\$2,339,813
Liabilities and Stockholders' Equity		
Liabilities		
Deposits:		
Non-interest-bearing	\$96,626	\$53,709
Interest-bearing	2,034,745	1,569,853
Total Deposits	2,131,371	1,623,562
Borrowings	255,202	210,000
Advance payments by borrowers for taxes	5,225	5,699
Deferred income tax liabilities, net	-	4,391
Other liabilities	12,577	10,235

Edgar Filing: Kearny Financial Corp. - Form 10-Q

Total Liabilities	2,404,375	1,853,887
Stockholders' Equity		
Preferred stock \$0.10 par value, 25,000,000 shares authorized; none issued and outstanding	-	-
Common stock \$0.10 par value, 75,000,000 shares authorized; 72,737,500 shares issued; 67,975,477 and 68,344,277 shares outstanding, respectively	7,274	7,274
Paid-in capital	215,212	213,529
Retained earnings	312,442	312,844
Unearned Employee Stock Ownership Plan shares; 897,090 shares and 969,828 shares, respectively	(8,971)	(9,698)
Treasury stock, at cost; 4,762,023 shares and 4,393,223 shares, respectively	(58,054)	(54,738)
Accumulated other comprehensive income	8,917	16,715
Total Stockholders' Equity	476,820	485,926
Total Liabilities and Stockholders' Equity	\$2,881,195	\$2,339,813
See notes to consolidated financial statements.		

-1-

KEARNY FINANCIAL CORP. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

(In Thousands, Except Per Share Data, Unaudited)

	Three Months Ended December 31,		Six Months Ended December 31,	
	2010	2009	2010	2009
Interest Income:				
Loans	\$14,878	\$14,739	\$28,679	\$29,618
Mortgage-backed securities	7,297	8,089	14,695	15,918
Securities:				
Taxable	1,379	454	2,787	514
Tax-exempt	238	158	395	316
Other interest-earning assets	241	215	420	445
Total Interest Income	24,033	23,655	46,976	46,811
Interest Expense:				
Deposits	6,015	7,188	12,338	15,016
Borrowings	2,146	2,075	4,221	4,150
Total Interest Expense	8,161	9,263	16,559	19,166
Net Interest Income	15,872	14,392	30,417	27,645
Provision for Loan Losses	876	605	2,127	1,463
Net Interest Income after Provision for Loan Losses	14,996	13,787	28,290	26,182
Non-Interest Income:				
Fees and service charges	427	350	769	728
Other-than-temporary security impairment:				
Total	-	(65)	-	(360)
Less: Portion recognized in other comprehensive income	-	10	-	207
Portion recognized in earnings	-	(55)	-	(153)
Miscellaneous	347	220	636	460
Total Non-Interest Income	774	515	1,405	1,035
Non-Interest Expenses:				
Salaries and employee benefits	7,397	6,662	14,350	13,344
Net occupancy expense of premises	1,152	988	2,201	2,005
Equipment and systems	1,385	1,117	2,562	2,189
Advertising and marketing	270	226	516	440

Edgar Filing: Kearny Financial Corp. - Form 10-Q

Federal deposit insurance premium	517	393	964	550
Directors' compensation	250	540	808	1,096
Merger-related expenses	3,150	-	3,190	-
Miscellaneous	1,281	1,245	2,455	2,564
Total Non-Interest Expenses	\$15,402	\$11,171	\$27,046	\$22,188

-2-

KEARNY FINANCIAL CORP. AND SUBSIDIARIES
 CONSOLIDATED STATEMENTS OF INCOME (Continued)
 (In Thousands, Except Per Share Data, Unaudited)

	Three Months Ended December 31,		Six Months Ended December 31,	
	2010	2009	2010	2009
Income Before Income Taxes	\$368	\$3,131	\$2,649	\$5,029
Income Taxes	373	1,290	1,319	2,093
Net Income (Loss)	\$(5	) \$1,841	\$1,330	\$2,936
Net Income (Loss) per Common Share (EPS):				
Basic	\$0.00	\$0.03	\$0.02	\$0.04
Diluted	0.00	0.03	0.02	0.04
Weighted Average Number of Common Shares Outstanding:				
Basic	67,042	68,015	67,130	68,045
Diluted	67,042	68,015	67,130	68,045
Dividends Declared Per Common Share (Excluding dividends waived by Kearny MHC)	\$0.05	\$0.05	\$0.10	\$0.10

See notes to consolidated financial statements.

-3-

KEARNY FINANCIAL CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
Six Months Ended December 31, 2009
(In Thousands, Except Per Share Data, Unaudited)

	Common Shares	Stock Amount	Paid-In Capital	Retained Earnings	Unearned ESOP Shares	Treasury Stock	Accumulated Other Comprehensive Income	Total
Balance - June 30, 2009	69,242	\$ 7,274	\$ 208,577	\$ 309,687	\$ (11,153)	\$ (45,985)	\$ 8,320	\$ 476,720
Comprehensive income:								
Net income	-	-	-	2,936	-	-	-	2,936
Unrealized gain on securities available for sale, net of deferred income tax expense of \$1,719	-	-	-	-	-	-	2,489	2,489
Non-credit related other-than- temporary impairment losses on securities held to maturity, net of deferred income tax benefit of \$50	-	-	-	-	-	-	(74)	(74)
Benefit plans, net of deferred income tax expense of \$8	-	-	-	-	-	-	11	11
Total Comprehensive income								5,362
ESOP shares committed to be released (72 shares)	-	-	39	-	727	-	-	766

Edgar Filing: Kearny Financial Corp. - Form 10-Q

Dividends contributed for payment of ESOP loan	-	-	50	-	-	-	-	50
Stock option expense	-	-	953	-	-	-	-	953
Treasury stock purchases	(264)	-	-	-	-	(2,727)	-	(2,727)
Restricted stock plan shares earned (126 shares)	-	-	1,542	-	-	-	-	1,542
See notes to consolidated financial statements.								-4-

KEARNY FINANCIAL CORP. AND SUBSIDIARIES
 CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY (Continued)
 Six Months Ended December 31, 2009
 (In Thousands, Except Per Share Data, Unaudited)

	Common Stock Shares	Common Stock Amount	Paid-In Capital	Retained Earnings	Unearned ESOP Shares	Treasury Stock	Accumulated Other Comprehensive Income	Total
Tax effect from stock based compensation	-	-	(186)	-	-	-	-	(186)
Cash dividends declared (\$0.10/ public share)	-	-	-	(1,694)	-	-	-	(1,694)
Cash dividend to Kearny MHC	-	-	-	(300)	-	-	-	(300)
Balance - December 31, 2009	68,978	\$ 7,274	\$ 210,975	\$ 310,629	\$ (10,426)	\$ (48,712)	\$ 10,746	\$ 480,486

See notes to consolidated financial statements.

-5-

KEARNY FINANCIAL CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY (Continued)
Six Months Ended December 31, 2010
(In Thousands, Except Per Share Data, Unaudited)

	Common Shares	Stock Amount	Paid-In Capital	Retained Earnings	Unearned ESOP Shares	Treasury Stock	Accumulated Other Comprehensive Income	Total
Balance - June 30, 2010	68,344	\$ 7,274	\$ 213,529	\$ 312,844	\$ (9,698)	\$ (54,738)	\$ 16,715	\$ 485,926
Comprehensive income:								
Net income	-	-	-	1,330	-	-	-	1,330
Unrealized loss on securities available for sale, net of deferred income tax benefit of \$5,342	-	-	-	-	-	-	(7,793)	(7,793)
Benefit plans, net of deferred income tax benefit of \$3	-	-	-	-	-	-	(5)	(5)
Total Comprehensive income								(6,468)
ESOP shares committed to be released (72 shares)	-	-	(84)	-	727	-	-	643
Dividends contributed for payment of ESOP loan	-	-	64	-	-	-	-	64
Stock option expense	-	-	745	-	-	-	-	745
Treasury stock purchases	(369)	-	-	-	-	(3,316)	-	(3,316)

Edgar Filing: Kearny Financial Corp. - Form 10-Q

Restricted stock plan shares earned (111 shares)	-	-	1,198	-	-	-	-	1,198
Tax effect from stock based compensation	-	-	(240)	(124)	-	-	-	(364)
Cash dividends declared (\$0.10/ public share)	-	-	-	(1,608)	-	-	-	(1,608)
Balance - December 31, 2010	67,975	\$ 7,274	\$ 215,212	\$ 312,442	\$ (8,971)	\$ (58,054)	\$ 8,917	\$ 476,820

See notes to consolidated financial statements.

-6-

KEARNY FINANCIAL CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In Thousands, Unaudited)

	Six Months Ended December 31,	
	2010	2009
Cash Flows from Operating Activities:		
Net income	\$1,330	\$2,936
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization of premises and equipment	944	872
Net amortization of premiums, discounts and loan fees and costs	1,681	411
Deferred income taxes	(756)	) 545
Amortization of intangible assets	-	14
Amortization of benefit plans' unrecognized net loss	34	72
Provision for loan losses	2,127	1,463
Realized gain on sale of loans originated for sale	(10))
Proceeds from sales of loans originated for sale	1,046	-
Loss on other-than-temporary impairment of securities	-	153
Increase in cash surrender value of bank owned life insurance	(337)	) (279)
ESOP, stock option plan and restricted stock plan expenses	2,586	3,261
Loss on sale of real estate owned	35	-
Increase in interest receivable	-	) (129)
Increase in other assets	(1,242)	) (5,863)
(Decrease) increase in interest payable	(36)	) 27
Decrease in other liabilities	(1,194)	) (1,959)
 Net Cash Provided by Operating Activities	 6,208	 1,524
Cash Flows from Investing Activities:		
Proceeds from calls and maturities of securities held for sale	405	40
Proceeds from repayments of securities available for sale	585	365
Purchase of securities held to maturity	(65,555)	) (65,000)
Proceeds from calls and maturities of securities held to maturity	115,230	-
Proceeds from repayments of securities held to maturity	148	-
Purchase of loans	(1,437)	) (20,659)
Net decrease in loans receivable	41,223	36,195
Proceeds from sale of real estate owned	60	243
Purchases of mortgage-backed securities available for sale	(245,211)	) (113,682)
Principal repayments on mortgage-backed securities available for sale	105,597	81,768
Principal repayments on mortgage-backed securities held to maturity	181	456
Purchase of Federal Home Loan Bank ("FHLB") stock	(2,250))
Redemption of FHLB stock	2,250	-
Cash paid in merger, net of cash acquired	(24,529))
Additions to premises and equipment	(434)	) (1,001)
 Net Cash Used in Investing Activities	 \$(73,737)	) \$(81,275)

KEARNY FINANCIAL CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS (Continued)
(In Thousands, Unaudited)

	Six Months Ended December 31,	
	2010	2009
Cash Flows from Financing Activities:		
Net increase in deposits	\$31,157	\$75,800
Repayment of long-term FHLB advances	(6)	-
Decrease in other short-term borrowings	(9,009)	-
Decrease in advance payments by borrowers for taxes	(474)	(484)
Dividends paid to stockholders of Kearny Financial Corp.	(1,617)	(1,707)
Purchase of common stock of Kearny Financial Corp. for treasury	(3,316)	(2,727)
Dividends contributed for payment of ESOP loan	64	50
Tax effect from stock based compensation	(364)	(186)
Net Cash Provided by Financing Activities	16,435	70,746
Net Decrease in Cash and Cash Equivalents	(51,094)	(9,005)
Cash and Cash Equivalents – Beginning	181,422	211,525
Cash and Cash Equivalents – Ending	\$130,328	\$202,520
Supplemental Disclosures of Cash Flows Information:		
Cash paid during the year for:		
Income taxes, net of refunds	\$3,603	\$2,606
Interest	\$16,595	\$19,139
Non-cash investing and financing activities:		
Acquisition of real estate owned in settlement of loans	\$435	\$543
Fair value of assets acquired, net of cash and cash equivalents acquired	\$559,113	\$-
Fair value of liabilities assumed	\$534,584	\$-

See notes to consolidated financial statements.

KEARNY FINANCIAL CORP. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

1. PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include the accounts of Kearny Financial Corp. (the “Company”), its wholly-owned subsidiaries, Kearny Federal Savings Bank (the “Bank”) and Kearny Financial Securities, Inc., and the Bank’s wholly-owned subsidiaries, KFS Financial Services, Inc., KFS Investment Corp. and CJB Investment Corp. and its wholly owned subsidiary, Central Delaware Investment Corp. The Company conducts its business principally through the Bank. Management prepared the consolidated financial statements in conformity with accounting principles generally accepted in the United States of America, including the elimination of all significant inter-company accounts and transactions during consolidation.

2. BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements were prepared in accordance with instructions for Form 10-Q and Regulation S-X and do not include information or footnotes necessary for a complete presentation of financial condition, income, changes in stockholders’ equity and cash flows in conformity with generally accepted accounting principles (“GAAP”). However, in the opinion of management, all adjustments (consisting of normal recurring adjustments) necessary for a fair presentation of the consolidated financial statements have been included. The results of operations for the three and six month period ended December 31, 2010, are not necessarily indicative of the results that may be expected for the entire fiscal year or any other period.

The data in the consolidated statements of financial condition for June 30, 2010 was derived from the Company’s annual report on Form 10-K. That data, along with the interim financial information presented in the consolidated statements of financial condition, operations, changes in stockholders’ equity and cash flows should be read in conjunction with the 2010 consolidated financial statements, including the notes thereto included in the Company’s annual report on Form 10-K.

3. NET INCOME PER COMMON SHARE (“EPS”)

Basic EPS is based on the weighted average number of common shares actually outstanding including restricted stock awards (see following paragraph) adjusted for Employee Stock Ownership Plan (“ESOP”) shares not yet committed to be released. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock, such as outstanding stock options, were exercised or converted into common stock or resulted in the issuance of common stock that then shared in the earnings of the Company. Diluted EPS is calculated by adjusting the weighted average number of shares of common stock outstanding to include the effect of contracts or securities exercisable or which could be converted into common stock, if dilutive, using the treasury stock method. Shares issued and reacquired during any period are weighted for the portion of the period they were outstanding.

The Financial Accounting Standards Board (“FASB”) has issued guidance on determining whether instruments granted in share-based payment transactions are participating securities. This guidance clarifies that all outstanding unvested share-based payment awards that contain rights to non-forfeitable dividends participate in undistributed earnings with common shareholders. Awards of this nature are considered participating securities and the two-class method of computing basic and diluted earnings per share must be applied.

Edgar Filing: Kearny Financial Corp. - Form 10-Q

The following is a reconciliation of the numerators and denominators of the basic and diluted earnings per share computations:

	Three Months Ended December 31, 2010			Six Months Ended December 31, 2010		
	Income	Shares	Per Share	Income	Shares	Per Share
	(Numerator) (In Thousands, Except Per Share Data)	(Denominator)	Amount	(Numerator) (In Thousands, Except Per Share Data)	(Denominator)	Amount
Net income (loss)	\$ (5)			\$ 1,330		
Basic earnings per share, income available to c o m m o n stockholders	\$ (5)	67,042	\$ 0.00	\$ 1,330	67,130	\$ 0.02
Effect of dilutive securities:						
Stock options	-	-		-	-	
	\$ (5)	67,042	\$ 0.00	\$ 1,330	67,130	\$ 0.02

	Three Months Ended December 31, 2009			Six Months Ended December 31, 2009		
	Income	Shares	Per Share	Income	Shares	Per Share
	(Numerator) (In Thousands, Except Per Share Data)	(Denominator)	Amount	(Numerator) (In Thousands, Except Per Share Data)	(Denominator)	Amount
Net income	\$1,841			\$2,936		
Basic earnings per share, income available to common stockholders	\$1,841	68,015	\$0.03	\$2,936	68,045	\$0.04
Effect of dilutive securities:						
Stock options	-	-		-	-	
	\$1,841	68,015	\$0.03	\$2,936	68,045	\$0.04

4. SUBSEQUENT EVENTS

The Company has evaluated events and transactions occurring subsequent to the statement of financial condition date of December 31, 2010, for items that should potentially be recognized or disclosed in these financial statements. The evaluation was conducted through the date this document was filed.

5. ACQUISITION OF CENTRAL JERSEY BANCORP

On November 30, 2010, the Company completed its acquisition of Central Jersey Bancorp (“Central Jersey”) and its wholly owned subsidiary, Central Jersey Bank, National Association (“Central Jersey Bank”). The transaction qualified as a tax-free reorganization for federal income tax purposes. The final consideration paid in the transaction totaled \$82.1 million which included \$70.5 million paid to stockholders of Central Jersey at a price of \$7.50 per outstanding

Edgar Filing: Kearny Financial Corp. - Form 10-Q

share and \$11.6 million paid to U.S. Department of Treasury (“U.S. Treasury”) for the redemption of the 11,300 shares of Fixed Rate Cumulative Perpetual Preferred Stock, Series A and related warrant originally issued by Central Jersey to the U.S. Treasury under the TARP Capital Purchase Plan.

-10-

The Company accounted for the transaction using applicable accounting guidance regarding business combinations resulting in the recognition of pre-tax merger-related expenses totaling \$3.2 million during the six months ended December 31, 2010. Additionally, the Company recorded the assets acquired and liabilities assumed through the merger at fair value as summarized in the following table (in thousands).

Consideration Paid:	
Cash for outstanding shares paid to Central Jersey shareholders	\$70,455
Cash paid to U.S. Department of Treasury for redemption of Central Jersey preferred shares and related warrant	11,620
Total consideration paid	\$82,075
Recognized amounts of identifiable assets acquired and liabilities assumed, at fair value	
Cash and cash equivalents	\$57,546
Investment securities	128,948
Net loans receivable	347,721
Mortgage-backed securities	34,447
Premises and equipment	5,151
Federal Home Loan Bank ("FHLB") stock	1,195
Interest receivable	2,087
Bank owned life insurance	3,929
Deferred income tax assets, net	3,887
Other assets	5,468
Fair value of assets acquired	590,379
Deposits	476,791
Federal Home Loan Bank advances	11,593
Subordinated debentures	5,155
Other borrowings	37,482
Other liabilities	3,563
Fair value of liabilities assumed	534,584
Total identifiable net assets	55,795
Goodwill	26,280
Total	\$82,075

The fair value amounts included in the table above are preliminary estimates and are subject to adjustment but are not expected to be materially different than those shown. None of the goodwill is deductible for tax purposes.

The Company estimated the fair value of non-impaired loans acquired from Central Jersey by utilizing a methodology wherein loans with comparable characteristics were aggregated by type of collateral, remaining maturity, and repricing terms. Cash flows for each pool were projected using an estimate of future credit losses and rate of prepayments. Projected monthly cash flows were then discounted to present value using a risk-adjusted market rate for similar loans. The portion of the fair valuation attributable to expected future credit losses on non-impaired loans totaled approximately \$3.5 million or 1.05% of their outstanding balances.

To estimate the fair value of impaired loans, the Company analyzed the value of the underlying collateral of the loans, assuming the fair values of the loans are derived from the eventual sale of the collateral. The value of the collateral was generally based on recently completed appraisals. The Company discounted these values using market derived

rates of return, with consideration given to the

-11-

period of time and costs associated with the foreclosure and disposition of the collateral. The portion of the fair valuation attributable to expected future credit losses on impaired loans totaled approximately \$7.6 million.

There was no carryover of Central Jersey's allowance for loan losses associated with the loans acquired as the loans were initially recorded at fair value. Information about the loans acquired from Central Jersey as of November 30, 2010 is as follows (in thousands):

Contractually required principal and interest at acquisition	\$	468,977
Contractual cash flows not expected to be collected		(8,005)
Expected cash flows at acquisition		460,972
Interest component of expected cash flows		(113,251)
 Fair value of acquired loans	 \$	 347,721

The fair values of investment securities, including mortgage-backed and non-mortgage backed securities, were primarily determined by obtaining matrix pricing, which is a mathematical technique widely used in the industry to value debt securities without relying exclusively on quoted prices for the specific securities but rather by relying on the securities' relationship to other benchmark quoted securities.

The fair value of savings and transaction deposit accounts acquired from Central Jersey was assumed to approximate the carrying value as these accounts have no stated maturity and are payable on demand. No core deposit intangible was ascribed to the value of non-maturity deposits due primarily to the comparatively low cost of alternative funding sources available in the marketplace at acquisition. Certificates of deposit accounts were valued utilizing a discounted cash flows analysis based upon the underlying accounts' contractual maturities and interest rates. The present value of the projected cash flow was then determined using discount rates based upon certificate of deposit interest rates available in the marketplace for accounts with similar terms.

The acquired borrowings were valued utilizing a discounted cash flow analysis based upon the underlying contractual maturities, interest rates and, where applicable, repricing and amortization terms applicable to each borrowing. The present value of the projected cash flow for each borrowing was then determined using discount rates based upon interest rates available in the marketplace for borrowings with similar terms.

Direct costs related to the merger were expensed as incurred. During the six months ended December 31, 2010, the Company incurred \$3.2 million in merger-related expenses attributable to the acquisition of Central Jersey. Such costs included legal expenses of \$186,000, investment banking and other professional service fees totaling \$712,000, employment and service provider severance charges totaling \$356,000 and \$1.9 million, respectively, and other merger-related expenses of \$8,000.

The following table presents unaudited pro forma information as if the acquisition of Central Jersey had occurred on July 1, 2009. This pro forma information gives effect to certain adjustments, including purchase accounting fair value adjustments and the related income tax effects. The pro forma information does not necessarily reflect the results of operations that would have occurred had the Company merged with Central Jersey at the beginning of fiscal 2010. In particular, expected cost savings and acquisition integration costs are not fully reflected in the unaudited pro forma amounts.

	December 31, 2010	Pro forma six months ended December 31, 2009
	(in thousands, except per share data)	(in thousands, except per share data)
Net interest income	\$ 38,376	\$ 37,167
Non-interest income	2,290	3,032
Non-interest expense	38,828	30,770
Net income (loss)	(815)	3,082
Net income (loss) per common shares (EPS)		
Basic and diluted	(0.01)	0.05

The amounts of revenue, expense and net income attributable to Central Jersey since the acquisition date included in the consolidated statement of operations for the six months ended December 31, 2010 are not disclosed due to the fact that the information is impracticable to provide.

6. RECENT ACCOUNTING PRONOUNCEMENTS

In June 2009, the FASB issued guidance concerning accounting for transfers of financial assets, an amendment to previous guidance on the topic. This statement prescribes the information that a reporting entity must provide in its financial reports about a transfer of financial assets; the effects of a transfer on its financial position, financial performance and cash flows; and a transferor's continuing involvement in transferred financial assets. Specifically, among other aspects, this guidance amends previous guidance concerning accounting for transfers and servicing of financial assets and extinguishments of liabilities by removing the concept of a qualifying special-purpose entity from previous guidance on transfers and servicing and removes the exception from applying previous guidance on transfers and servicing to variable interest entities that are qualifying special-purpose entities. It also modifies the financial-components approach used in previous guidance. This guidance is effective for fiscal years beginning after November 15, 2009. The implementation of this standard did not have a material impact on the Company's consolidated financial position or results of operations.

In June 2009, the FASB issued guidance concerning consolidation of variable interest entities to require an enterprise to determine whether its variable interest or interests give it a controlling financial interest in a variable interest entity. The primary beneficiary of a variable interest entity is the enterprise that has both (1) the power to direct the activities of a variable interest entity that most significantly impact the entity's economic performance and (2) the obligation to absorb losses of the entity that could potentially be significant to the variable interest entity or the right to receive benefits from the entity that could potentially be significant to the variable interest entity. This guidance also amends previous guidance to require ongoing reassessments of whether an enterprise is the primary beneficiary of a variable interest entity. This guidance is effective for fiscal years beginning after November 15, 2009. The implementation of this standard did not have a material impact on the Company's consolidated financial position or results of operations.

In October 2009, the FASB issued guidance concerning accounting for own-share lending arrangements in contemplation of convertible debt issuance or other financing. The guidance amends earlier guidance and provides direction for accounting and reporting for own-share lending arrangements issued in contemplation of a convertible debt issuance. At the date of issuance, a share-lending arrangement entered into on an entity's own shares should be

measured at fair value in accordance with the guidance on fair value measurements and disclosures and recognized as an issuance cost, with an offset to additional paid-in capital. Loaned shares are excluded from basic and diluted earnings per share unless default of the share-lending arrangement occurs. The amendments also require several disclosures including a description and the terms of the arrangement and the reason for entering into the arrangement. The effective dates of the amendments are dependent upon the date the share-lending arrangement was entered into and include retrospective application for arrangements outstanding as of the beginning of

-13-

fiscal years beginning on or after December 15, 2009. The implementation of this standard did not have a material impact on the Company's consolidated financial position or results of operations.

In January 2010, the FASB issued guidance concerning fair value measurement and disclosures. The guidance mandates additional disclosure requiring that a reporting entity should disclose separately the amounts of significant transfers in and out of Level 1 and Level 2 fair value measurements and describe the reasons for the transfers while also requiring that in the reconciliation for fair value measurements using significant unobservable inputs (Level 3), a reporting entity should present separately information about purchases, sales, issuances, and settlements (that is, on a gross basis rather than as one net number). The guidance clarifies existing fair value disclosure requirements such that a reporting entity should provide fair value measurement disclosures for each class of assets and liabilities. A class is often a subset of assets or liabilities within a line item in the statement of financial position. A reporting entity needs to use judgment in determining the appropriate classes of assets and liabilities. Moreover, a reporting entity should provide disclosures about the valuation techniques and inputs used to measure fair value for both recurring and nonrecurring fair value measurements. Those disclosures are required for fair value measurements that fall in either Level 2 or Level 3. This guidance also includes conforming amendments regarding employers' disclosures about postretirement benefit plan assets. The conforming amendments change the terminology from "major categories" of assets to "classes" of assets and provide a cross reference to the guidance in Subtopic 820-10 on how to determine appropriate classes to present fair value disclosures. The new disclosures and clarifications of existing disclosures are effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosures about purchases, sales, issuances, and settlements in the roll forward of activity in Level 3 fair value measurements. Those disclosures are effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years. The implementation of the new pronouncement during the quarter ended March 31, 2010 did not have a material impact on the Company's consolidated financial position or results of operations. The Company is currently evaluating the potential impact the new pronouncement will have on its consolidated financial statements for those disclosures that go into effect during fiscal 2012.

In April 2010, the FASB issued amended guidance that codifies the consensus reached regarding the effect of a loan modification when the loan is part of a pool that is accounted for as a single asset. The amendments to the Codification provide that modifications of loans that are accounted for within a pool under Subtopic 310-30 do not result in the removal of those loans from the pool even if the modification of those loans would otherwise be considered a troubled debt restructuring. An entity will continue to be required to consider whether the pool of assets in which the loan is included is impaired if expected cash flows for the pool change. The amended guidance does not affect the accounting for loans under the scope of Subtopic 310-30 that are not accounted for within pools. Loans accounted for individually under Subtopic 310-30 continue to be subject to the troubled debt restructuring accounting provisions within Subtopic 310-40. The amended guidance is effective prospectively for modifications of loans accounted for within pools under Subtopic 310-30 occurring in the first interim or annual period ending on or after July 15, 2010. Upon initial adoption of ASU 2010-18, an entity may make a one-time election to terminate accounting for loans as a pool under Subtopic 310-30. This election may be applied on a pool-by-pool basis and does not preclude an entity from applying pool accounting to subsequent acquisitions of loans with credit deterioration. The implementation of this standard did not have a material impact on the Company's consolidated financial position or results of operations.

In July 2010, the FASB issued guidance concerning disclosures about the credit quality of financing receivables and the allowance for credit losses that will help investors assess the credit risk of a company's receivables portfolio and the adequacy of its allowance for credit losses held against the portfolios by expanding credit risk disclosures. This guidance requires more information about the credit quality of financing receivables in the disclosures to financial statements, such as aging information and

credit quality indicators. Both new and existing disclosures must be disaggregated by portfolio segment or class. The disaggregation of information is based on how a company develops its allowance for credit losses and how it manages its credit exposure. Financing receivables include loans and trade accounts receivable. However, short-term trade accounts receivable, receivables measured at fair value or lower of cost or fair value, and debt securities are exempt from these disclosure amendments. For public companies, the amendments that require disclosures as of the end of a reporting period are effective for periods ending on or after December 15, 2010. The amendments that require disclosures about activity that occurs during a reporting period are effective for periods beginning on or after December 15, 2010. The implementation of this standard did not have a material impact on the Company's consolidated financial position or results of operations.

In December 2010, the FASB issued amended guidance concerning goodwill impairment testing. The amended guidance modifies Step 1 of the goodwill impairment test for reporting units with zero or negative carrying amounts. For those reporting units, an entity is required to perform Step 2 of the goodwill impairment test if it is more likely than not that a goodwill impairment exists. In determining whether it is more likely than not that a goodwill impairment exists, an entity should consider whether there are any adverse qualitative factors indicating that an impairment may exist. The qualitative factors are consistent with the existing guidance and related examples, which requires that goodwill of a reporting unit be tested for impairment between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount.

These amendments eliminate an entity's ability to assert that a reporting unit is not required to perform Step 2 because the carrying amount of the reporting unit is zero or negative despite the existence of qualitative factors that indicate the goodwill is more likely than not impaired. As a result, goodwill impairments may be reported sooner than under current practice.

For public entities, the amendments in this Update are effective for fiscal years, and interim periods within those years, beginning after December 15, 2010. Early adoption is not permitted.

Upon adoption of the amendments, an entity with reporting units that have carrying amounts that are zero or negative is required to assess whether it is more likely than not that the reporting units' goodwill is impaired. If the entity determines that it is more likely than not that the goodwill of one or more of its reporting units is impaired, the entity should perform Step 2 of the goodwill impairment test for those reporting unit(s). Any resulting goodwill impairment should be recorded as a cumulative-effect adjustment to beginning retained earnings in the period of adoption. Any goodwill impairments occurring after the initial adoption of the amendments should be included in earnings as required by existing guidance. The Company is currently evaluating the potential impact the new pronouncement will have on its consolidated financial statements.

In December 2010, the FASB issued guidance to address diversity in practice about the interpretation of the pro forma revenue and earnings disclosure requirements for business combinations.

Current guidance requires a public entity to disclose pro forma information for business combinations that occurred in the current reporting period. The disclosures include pro forma revenue and earnings of the combined entity for the current reporting period as though the acquisition date for all business combinations that occurred during the year had been as of the beginning of the annual reporting period. If comparative financial statements are presented, the pro forma revenue and earnings of the combined entity for the comparable prior reporting period should be reported as though the acquisition

date for all business combinations that occurred during the current year had been as of the beginning of the comparable prior annual reporting period.

In practice, some preparers have presented the pro forma information in their comparative financial statements as if the business combination that occurred in the current reporting period had occurred as of the beginning of each of the current and prior annual reporting periods. Other preparers have disclosed the pro forma information as if the business combination occurred at the beginning of the prior annual reporting period only, and carried forward the related adjustments, if applicable, through the current reporting period.

The amendments in this Update specify that if a public entity presents comparative financial statements, the entity should disclose revenue and earnings of the combined entity as though the business combination(s) that occurred during the current year had occurred as of the beginning of the comparable prior annual reporting period only.

The amendments in this Update also expand the supplemental pro forma disclosures to include a description of the nature and amount of material, nonrecurring pro forma adjustments directly attributable to the business combination included in the reported pro forma revenue and earnings.

The amendments in this Update are effective prospectively for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2010. Early adoption is permitted, which enabled the Company to adopt the amendment during the current quarter ended December 31, 2010 and apply the guidance for the pro forma operating data included in Note 5 above.

In January 2011, the FASB issued amendments that temporarily delay the effective date of the disclosures about troubled debt restructurings that are required in conjunction with a prior update relating to public entities. Under the existing effective date in that prior update, public-entity creditors would have provided disclosures about troubled debt restructurings for periods beginning on or after December 15, 2010. The delay is intended to allow the Board time to complete its deliberations on what constitutes a troubled debt restructuring. The effective date of the new disclosures about troubled debt restructurings for public entities and the guidance for determining what constitutes a troubled debt restructuring will then be coordinated. Currently, that guidance is anticipated to be effective for interim and annual periods ending after June 15, 2011. The deferral in this amendment is effective upon issuance. The Company will evaluate the potential impact the new pronouncement will have on its consolidated financial statements when updated guidance is issued by the FASB.

7. STOCK REPURCHASE PLANS

On May 26, 2010, the Company announced that the Board of Directors authorized a stock repurchase plan to acquire up to 889,506 shares, or 5% of the Company's outstanding stock held by persons other than Kearny MHC. Through December 31, 2010 the Company has repurchased a total of 730,900 shares in accordance with this repurchase plan at a total cost of \$6,600,000 and at an average cost per share of \$9.03 all of which were repurchased during prior quarters with no additional shares repurchased during the three months ended December 31, 2010.

8. DIVIDEND WAIVER

During the six months ended December 31, 2010, Kearny MHC, the federally chartered mutual holding company of the Company waived its right, in accordance with the non-objection previously granted by the Office of Thrift Supervision (“OTS”), to receive cash dividends of approximately \$5.1 million declared on the 50,916,250 shares of Company common stock it owns.

-17-

9. SECURITIES AVAILABLE FOR SALE

The amortized cost, gross unrealized gains and losses and estimated fair values of securities at December 31, 2010 and June 30, 2010 and stratification by contractual maturity of securities at December 31, 2010 are presented below:

	Amortized Cost	At December 31, 2010		Carrying Value
		Gross Unrealized Gains	Gross Unrealized Losses	
(In Thousands)				
Securities:				
Debt securities:				
Trust preferred securities	\$8,859	\$-	\$2,009	\$6,850
U.S. agency securities	7,299	-	122	7,177
Obligations of state and political subdivisions	110,999	631	88	111,542
Total securities	127,157	631	2,219	125,569
Mortgage-backed securities:				
Collateralized mortgage obligations:				
Federal National Mortgage Association	3,990	-	44	3,946
Total collateralized mortgage obligations	3,990	-	44	3,946
Mortgage pass-through securities:				
Government National Mortgage Association	13,994	1,053	26	15,021
Federal Home Loan Mortgage Corporation	289,918	7,370	1,067	296,221
Federal National Mortgage Association	537,839	13,995	4,253	547,581
Total mortgage pass-through securities	841,751	22,418	5,346	858,823
Total mortgage-backed securities	845,741	22,418	5,390	862,769
Total securities available for sale	\$972,898	\$23,049	\$7,609	\$988,338

	At December 31, 2010	
	Amortized Cost	Carrying Value
(In Thousands)		
Debt securities:		
Due in one year or less	\$84,764	\$84,762
Due after one year through five years	8,714	9,024
Due after five years through ten years	15,450	15,718

Edgar Filing: Kearny Financial Corp. - Form 10-Q

Due after ten years	18,229	16,065
Total	\$127,157	\$125,569

-18-

		At June 30, 2010		
	Amortized	Gross	Gross	Carrying
	Cost	Unrealized	Unrealized	Value
		Gains	Losses	
		(In Thousands)		
Securities:				
Debt securities:				
Trust preferred securities	\$8,855	\$-	\$2,255	\$6,600
U.S. agency securities	3,980	1	39	3,942
Obligations of state and political subdivisions	18,125	830	-	18,955
Total securities	30,960	831	2,294	29,497
Mortgage-backed securities:				
Mortgage pass-through securities:				
Government National Mortgage Association	14,660	999	31	15,628
Federal Home Loan Mortgage Corporation	263,481	10,267	44	273,704
Federal National Mortgage Association	395,273	18,884	34	414,123
Total mortgage-backed securities	673,414	30,150	109	703,455
Total securities available for sale	\$704,374	\$30,981	\$2,403	\$732,952

There were no sales of securities from the available for sale portfolio during the six months ended December 31, 2010 and December 31, 2009.

At December 31, 2010 and June 30, 2010, securities available for sale with carrying value of approximately \$373.7 million and \$243.7 million, respectively, were utilized as collateral for borrowings through the FHLB of New York. As of those same dates, securities available for sale with carrying values of approximately \$6.8 million and \$1.4 million, respectively, were pledged to secure public funds on deposit.

The Company's available for sale mortgage-backed securities are generally secured by residential mortgage loans with original contractual maturities of ten to thirty years. However, the effective lives of those securities are generally shorter than their contractual maturities due to principal amortization and prepayment of the mortgage loans comprised within those securities. Investors in mortgage pass-through securities generally share in the receipt of principal repayments on a pro-rata basis as paid by the borrowers. By comparison, collateralized mortgage obligations generally represent individual tranches within a larger investment vehicle that is designed to distribute cash flows received on securitized mortgage loans to investors in a manner determined by the overall terms and structure of the investment vehicle and those applying to the individual tranches within that structure.

10. SECURITIES HELD TO MATURITY

The amortized cost, gross unrealized gains and losses and estimated fair values of securities at December 31, 2010 and June 30, 2010 and stratification by contractual maturity of securities at December 31, 2010 are presented below:

	Carrying Value	At December 31, 2010		Fair Value
		Gross Unrealized Gains	Gross Unrealized Losses	
	(In Thousands)			
Securities:				
Debt securities:				
U.S. agency securities	\$234,951	\$959	\$436	\$235,474
Obligations of state and political subdivisions	1,919	-	-	1,919
Total securities	236,870	959	436	237,393
Mortgage-backed securities:				
Collateralized mortgage obligations:				
Federal Home Loan Mortgage Corporation	77	4	-	81
Federal National Mortgage Association	682	57	-	739
Non-agency securities	285	-	27	258
Total collateralized mortgage obligations	1,044	61	27	1,078
Mortgage pass-through securities:				
Federal Home Loan Mortgage Corporation	158	5	-	163
Federal National Mortgage Association	331	8	-	339
Total mortgage pass-through securities	489	13	-	502
Total mortgage-backed securities	1,533	74	27	1,580
Total securities held to maturity	\$238,403	\$1,033	\$463	\$238,973

	At December 31, 2010	
	Carrying Value	Fair Value
	(In Thousands)	
Debt securities:		
Due in one year or less	\$1,810	\$1,810
Due after one year through five years	165,082	165,815

Edgar Filing: Kearny Financial Corp. - Form 10-Q

Due after five years through ten years	20,000	19,845
Due after ten years	49,978	49,923
Total	\$236,870	\$237,393

-20-

Edgar Filing: Kearny Financial Corp. - Form 10-Q

	Carrying Value	At June 30, 2010		Fair Value
		Gross Unrealized Gains	Gross Unrealized Losses	
(In Thousands)				
Securities:				
Debt securities:				
U.S. agency securities	\$255,000	\$1,914	\$-	\$256,914
Total securities	255,000	1,914	-	256,914
Mortgage-backed securities:				
Collateralized mortgage obligations:				
Federal Home Loan Mortgage Corporation	99	12	-	111
Federal National Mortgage Association Non-agency securities	767	71	1	837
	310	2	43	269
Total collateralized mortgage obligations	1,176	85	44	1,217
Mortgage pass-through securities:				
Federal Home Loan Mortgage Corporation	168	5	-	173
Federal National Mortgage Association	356	9	1	364
Total mortgage pass-through securities	524	14	1	537
Total mortgage-backed securities	1,700	99	45	1,754
Total securities held to maturity	\$256,700	\$2,013	\$45	\$258,668

There were no sales of securities from the held to maturity portfolio during the six months ended December 31, 2010 and December 31, 2009. At December 31, 2010 one held to maturity security with a carrying value of approximately \$5.0 million was pledged to secure public funds on deposit. As of that date, held to maturity securities were not utilized as collateral for borrowings.

The Company's held to maturity mortgage-backed securities are generally secured by residential mortgage loans with original contractual maturities of ten to thirty years. However, the effective lives of those securities are generally shorter than their contractual maturities due to principal amortization and prepayment of the mortgage loans comprised within those securities. Investors in mortgage pass-through securities generally share in the receipt of principal repayments on a pro-rata basis as paid by the borrowers. By comparison, collateralized mortgage obligations generally represent individual tranches within a larger investment vehicle that is designed to distribute cash flows received on securitized mortgage loans to investors in a manner determined by the overall terms and structure of the investment vehicle and those applying to the individual tranches within that structure.

11. IMPAIRMENT OF SECURITIES

The following three tables summarize the fair values and gross unrealized losses within the available for sale and held to maturity portfolios at December 31, 2010 and June 30, 2010. The gross unrealized losses, presented by security type, represent temporary impairments of value within each portfolio as of the dates presented. Temporary impairments within the available for sale portfolio have been recognized through other comprehensive income as reductions in stockholders' equity on a tax-effected basis.

The tables are followed by a discussion that summarizes the Company's rationale for recognizing the reported impairments as "temporary" versus "other-than-temporary". Such rationale is presented by investment type and generally applies consistently to both the available for sale and held to maturity portfolios, except where specifically noted.

	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
(In Thousands)						
Securities Available for Sale:						
At December 31, 2010:						
Trust preferred securities	\$-	\$-	\$5,850	\$2,009	\$5,850	\$2,009
U.S. agency securities	3,800	107	3,074	15	6,874	122
Obligations of state and political subdivisions	87,782	88	-	-	87,782	88
Collateralized mortgage obligations	3,946	44	-	-	3,946	44
Mortgage pass-through securities	315,134	5,262	776	84	315,910	5,346
Total	\$410,662	\$5,501	\$9,700	\$2,108	\$420,362	\$7,609
At June 30, 2010:						
Trust preferred securities	\$-	\$-	\$5,600	\$2,255	\$5,600	\$2,255
U.S. agency securities	-	-	3,667	39	3,667	39
Mortgage pass-through securities	559	4	906	105	1,465	109
Total	\$559	\$4	\$10,173	\$2,399	\$10,732	\$2,403

The number of available for sale securities with unrealized losses at December 31, 2010 totaled 130 comprising four single-issuer trust preferred securities, six U.S. agency securities, 51 municipal obligations, one collateralized mortgage obligation and 68 mortgage pass-through securities. The number of available for sale securities with unrealized losses at June 30, 2010 totaled 28 comprising four single-issuer trust preferred securities, six U.S. agency securities and 18 mortgage pass-through securities.

Edgar Filing: Kearny Financial Corp. - Form 10-Q

	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
(In Thousands)						
Securities Held to Maturity:						
At December 31, 2010:						
U.S. agency securities	\$68,565	\$436	\$-	\$-	\$68,565	\$436
Collateralized mortgage obligations	55	3	203	24	258	27
Total	\$68,620	\$439	\$203	\$24	\$68,823	\$463
At June 30, 2010:						
Collateralized mortgage obligations	\$76	\$3	\$218	\$41	\$294	\$44
Mortgage pass-through securities	66	1	-	-	66	1
Total	\$142	\$4	\$218	\$41	\$360	\$45

The number of held to maturity securities with unrealized losses at December 31, 2010 totaled 28 comprising 20 collateralized mortgage obligations and eight U.S. agency securities. The number of held to maturity securities with unrealized losses at June 30, 2010 totaled 23 comprising 22 collateralized mortgage obligations and one mortgage pass-through security.

Mortgage-backed Securities. The carrying value of the Company's mortgage-backed securities totaled \$864.3 million at December 31, 2010 and comprised 70.4% of total investments and 30.0% of total assets as of that date. This category of securities primarily includes mortgage pass-through securities and collateralized mortgage obligations issued by U.S. government-sponsored entities such as Ginnie Mae, Fannie Mae and Freddie Mac who guarantee the contractual cash flows associated with those securities. Those guarantees were strengthened during the 2008-2009 financial crisis during which time Fannie Mae and Freddie Mac were placed into receivership by the federal government. Through those actions, the U.S. government effectively reinforced the guarantees of their agencies thereby assuring the creditworthiness of the mortgage-backed securities issued by those agencies.

With credit risk being reduced to negligible levels due primarily to the U.S. government's support of most of these agencies, the unrealized losses on the Company's investment in U.S. agency mortgage-backed securities are due largely to the combined effects of several market-related factors. First, movements in market interest rates significantly impact the average lives of mortgage-backed securities by influencing the rate of principal prepayment attributable to refinancing activity. Changes in the expected average lives of such securities significantly impact their fair values due to the extension or contraction of the cash flows that an investor expects to receive over the life of the security.

Generally, lower market interest rates prompt greater refinancing activity thereby shortening the average lives of mortgage-backed securities and vice-versa. The historically low mortgage rates currently prevalent in the marketplace have created significant refinancing incentive for qualified borrowers. However, prepayment rates are also influenced by fluctuating real estate values and the overall availability of credit in the marketplace which significantly impacts the ability of borrowers to qualify for refinancing. The deteriorating real estate market values and reduced availability of credit that have characterized the residential real estate marketplace in recent years have stifled demand for

residential

-23-

real estate while reducing the ability of certain borrowers to qualify for the refinancing of existing loans. To some extent, these factors have offset the effects of historically low interest rates on mortgage-backed security prepayment rates.

The market price of mortgage-backed securities, being the key measure of the fair value to an investor in such securities, is also influenced by the overall supply and demand for such securities in the marketplace. Absent other factors, an increase in the demand for, or a decrease in the supply of a security increases its price. Conversely, a decrease in the demand for, or an increase in the supply of a security decreases its price. During fiscal 2008 and fiscal 2009, the volatility and uncertainty in the marketplace had reduced the overall level of demand for mortgage-backed securities which generally had an adverse impact on their prices in the open market. This was further exacerbated by many larger institutions shedding mortgage-related assets to shrink their balance sheets for capital adequacy purposes thereby increasing the supply of such securities.

During fiscal 2010, however, institutional demand for mortgage-backed securities increased reflecting greater stability and liquidity in the financial markets coupled with the intervention of the Federal Reserve as a buyer/holder of such securities. Moreover, many financial institutions, including the Bank, are experiencing the concurrent effects of strong deposit growth and diminished loan origination volume resulting in increased institutional demand for mortgage-backed securities as investment alternatives to loans. These factors have continued into fiscal 2011 with market prices of agency mortgage-backed securities generally reflecting the increased institutional demand for such securities.

In sum, the factors influencing the fair value of the Company's U.S. agency mortgage-backed securities, as described above, generally result from movements in market interest rates and changing real estate and financial market conditions which affect the supply and demand for such securities. Inasmuch as such market conditions fluctuate over time, the impairments of value arising from these changing market conditions are both "noncredit-related" and "temporary" in nature.

The Company has the stated ability and intent to "hold to maturity" those securities so designated. Moreover, the Company has both the ability and intent, as of the periods presented, to hold the temporarily impaired available for sale securities until the fair value of the securities recovers to a level equal to or greater than the Company's amortized cost. As such, the Company has not decided to sell the securities as of December 31, 2010 and has further concluded that the possibility of being required to sell the securities prior to their anticipated recovery is unlikely based upon its strong liquidity, asset quality and capital position as of that date. Moreover, the Company purchased these securities at either par or nominal premiums. Accordingly, the Company expects that the securities will not be settled for a price less than its amortized cost.

In light of the factors noted above, the Company does not consider its U.S. agency mortgage-backed securities with unrealized losses at December 31, 2010 to be "other-than-temporarily" impaired as of that date.

In addition to those mortgage-backed securities issued by U.S. agencies, the Company also maintains a nominal balance of non-agency mortgage-backed securities at December 31, 2010. Unlike agency mortgage-backed securities, non-agency collateralized mortgage obligations are not explicitly guaranteed by a U.S. government sponsored entity. Rather, such securities generally utilize the structure of the larger investment vehicle to reallocate credit risk among the individual tranches comprised within that vehicle. Through this process, investors in different tranches are subject to varying degrees of risk that the cash flows of their tranche will be adversely impacted by borrowers defaulting on the underlying mortgage loans. The creditworthiness of certain tranches may also be further enhanced by additional credit insurance protection embedded within the terms of the total investment vehicle.

The fair values of the non-agency mortgage-backed securities are subject to many of factors applicable to the agency securities that may result in “temporary” impairments in value. However, due to the lack of agency guaranty, the Company also monitors the general level of credit risk for each of its non-agency mortgage-backed securities based upon the ratings assigned to its specific tranches by one or more credit rating agencies. The level of such ratings, and changes thereto, is one of several factors considered by the Company in identifying those securities that may be other-than-temporarily impaired.

At December 31, 2010, the Company's remaining portfolio of non-agency CMOs included 20 held-to-maturity securities totaling \$285,000 all of which are rated as investment grade as of that date. The Company has not decided to sell the securities as of December 31, 2010 and has further concluded that the possibility of being required to sell the securities prior to their anticipated recovery is unlikely based upon its strong liquidity, asset quality and capital position as of that date.

In light of the factors noted above, the Company does not consider its balance of non-agency mortgage-backed securities with unrealized losses at December 31, 2010 to be “other-than-temporarily” impaired as of that date.

U.S. Agency Securities. The carrying value of the Company's U.S. agency debt securities totaled \$242.2 million at December 31, 2010 and comprised 19.7% of total investments and 8.4% of total assets as of that date. Such securities are comprised of \$235.0 million of U.S. agency debentures and \$7.2 million of securitized pools of loans issued and fully guaranteed by the Small Business Administration (“SBA”), a U.S. government sponsored entity.

With credit risk being reduced to negligible levels due to the issuer's guarantee, the unrealized losses on the Company's investment in U.S. agency debt securities are due largely to the combined effects of several market-related factors including movements in market interest rates and general level of liquidity of such securities in the marketplace based on supply and demand.

With regard to interest rates, the Company's SBA securities are variable rate investments whose interest coupons are generally based on the Prime index minus a margin. Based upon the historically low level of short term market interest rates, of which the Prime index is one measure, the current yields on these securities are comparatively low. Consequently, the fair value of the SBA securities, as determined based upon the market price of these securities, reflects the adverse effects of the historically low short term, market interest rates at December 31, 2010.

Like the mortgage-backed securities described earlier, the currently diminished fair value of the Company's SBA securities also reflects the extended average lives of the underlying loans resulting from loan prepayment prohibitions that may be embedded in the underlying loans coupled with the generally reduced availability of credit in the marketplace reducing borrower refinancing opportunities. Such influences extend the timeframe over which an investor would anticipate holding the security at a “below market” yield. Similarly, the price of securitized SBA loan pools also reflects fluctuating supply and demand in the marketplace attributable to similar factors as those applying to mortgage-backed securities, as presented above.

Unlike its SBA securities, the Company's U.S. agency debentures are fixed rate investments whose fair values over time reflect movements in comparatively longer term market interest rates. At December 31, 2010, the unrealized losses applicable to those securities portfolio are generally attributable to movements in longer term market interest rates since their acquisition by the Company.

In sum, the factors influencing the fair value of the Company's U.S. agency securities, as described above, generally result from movements in market interest rates and changing market

conditions which affect the supply and demand for such securities. Inasmuch as such market conditions fluctuate over time, the “noncredit-related” impairments of value arising from these changing market conditions are “temporary” in nature.

The Company has the stated ability and intent to “hold to maturity” those securities so designated. Moreover, the Company has both the ability and intent, as of the periods presented, to hold the temporarily impaired available for sale securities until the fair value of the securities recovers to a level equal to or greater than the Company’s amortized cost. As such, the Company has not decided to sell the securities as of December 31, 2010 and has further concluded that the possibility of being required to sell the securities prior to their anticipated recovery is unlikely based upon its strong liquidity, asset quality and capital position as of that date. Moreover, the Company purchased these securities at either par or nominal premiums. Accordingly, the Company expects that the securities will not be settled for a price less than its amortized cost.

In light of the factors noted above, the Company does not consider its balance of U.S. agency securities with unrealized losses at December 31, 2010 to be “other-than-temporarily” impaired as of that date.

Obligations of States and Political Subdivisions. The outstanding balance of the Company’s securities representing obligations of state and political subdivisions totaled \$113.5 million at December 31, 2010 and comprised 9.2% of total investments and 3.9% of total assets as of that date. Such securities are generally comprised of bank qualified securities issued by New Jersey and Pennsylvania municipalities or the obligations of their related entities such as boards of education or utility authorities. The municipal obligations of New Jersey and Pennsylvania municipalities and their related entities total \$108.1 million and \$5.4 million, respectively.

The portfolio includes \$105.1 million of general obligations of the municipalities and their related entities while \$6.5 million represent revenue obligations funding specific projects. An additional \$1.9 million represent short term obligations negotiated directly with local New Jersey municipalities that are also depository customers of the Bank.

The Company generally evaluates the level of credit risk for the securities within this category based upon ratings assigned by one or more credit rating agencies where such ratings are available. All rated securities within this category totaled \$31.9 million at December 31, 2010 and maintained investment grade ratings of A1 or higher by Moody’s Investors Service (“Moody’s”).

The larger portion of the portfolio totaling \$81.6 million comprises municipal securities for which credit ratings are not available from Moody’s or other rating services utilized by the Company. The non-rated municipal securities, all of which were added to the portfolio through the acquisition of Central Jersey Bank during the quarter ended December 31, 2010, generally represent comparatively shorter duration municipal obligations, the large majority of which have remaining average lives of less than one year.

In light of their strong credit ratings, where available, and consistent payment histories, the unrealized losses on the Company’s investment in municipal obligations are due largely to the combined effects of several market-related factors including movements in market interest rates and general level of liquidity of such securities in the marketplace based on overall supply and demand. Notwithstanding the generally strong credit ratings of the Company’s specific municipal securities, where applicable, the market prices of bank-qualified municipal obligations, in general, currently reflect the effect of reduced demand for such securities. Such reduced demand is attributable, in part, to the overall increased level of credit risk-aversion currently characterizing many financial institutions in the marketplace. More

specifically, however, the reduced demand specifically reflects the state and local economic strains which have adversely affected the financial condition of many municipalities. As noted above, each of the Company's rated municipal obligations retained their investment grade status at December 31, 2010. However, the financial challenges facing certain issuers of the Company's municipal obligations have been evidenced through credit rating downgrades within the investment grade tier. In addition to the affects of reduced demand, municipal obligation prices also reflect the effects of increased supply generally arising from financial institutions selling investments and reducing assets for capital adequacy purposes, as noted earlier.

In sum, the factors influencing the fair value of the Company's municipal obligations, as described above, generally result from movements in market interest rates and changing market conditions which affect the supply and demand for such securities. Inasmuch as such market conditions fluctuate over time, the "noncredit-related" impairments of value arising from these changing market conditions are "temporary" in nature.

While most of its municipal obligations are classified as "available-for-sale", the Company has both the ability and intent to hold temporarily impaired securities until the fair value of the securities recover to a level equal to or greater than the Company's amortized cost. As of December 31, 2010, the Company has not decided to sell the securities. Additionally, the Company has concluded that the possibility of being required to sell the securities prior to their anticipated recovery is unlikely based upon its strong liquidity, asset quality and capital position as of that date. Moreover, the Company purchased these securities at either par or nominal premiums. Call provisions, where applicable, require full repayment of principal at par by the issuer. Accordingly, the Company expects that the securities will not be settled for a price less than its amortized cost.

In light of the factors noted above, the Company does not consider any of its investments in municipal obligations to be "other-than-temporarily" impaired as of December 31, 2010.

Trust Preferred Securities. The outstanding balance of the Company's trust preferred securities totaled \$6.8 million at December 31, 2010 and comprised less than one percent of total investments and total assets as of that date. The category comprises a total of five "single-issuer" (i.e. non-pooled) trust preferred securities, four of which are impaired as of December 31, 2010, that were originally issued by four separate financial institutions. As a result of bank mergers involving the issuers of these securities, the Company's five trust preferred securities currently represent the de-facto obligations of three separate financial institutions.

The Company generally evaluates the level of credit risk for each of its trust preferred securities based upon ratings assigned by one or more credit rating agencies where such ratings are available. For those trust preferred securities that are impaired, the Company uses such ratings as a practical expedient to identify those securities whose impairments are potentially "credit-related" versus "noncredit-related".

Specifically, impairments associated with investment-grade trust preferred securities are generally categorized as "noncredit-related" given the nominal level of credit losses that would be expected based upon such ratings. At December 31, 2010, the Company owned two securities at an amortized cost of \$2.9 million that were consistently rated as investment grade by Moody's and Standard & Poor's Financial Services ("S&P"). The securities were originally issued through Chase Capital II and currently represent de-facto obligations of JPMorgan Chase & Co.

The Company has attributed the unrealized losses on these securities to the combined effects of several market-related factors including movements in market interest rates and general level of liquidity of such securities in the marketplace based on overall supply and demand.

With regard to interest rates, the Company's impaired trust preferred securities are variable rate securities whose interest rates generally float with three month Libor plus a margin. Based upon the historically low level of short term market interest rates, the current yield on these securities is comparatively low. Consequently, the fair value of the securities, as determined based upon their market price, reflects the adverse effects of the historically low market interest rates at December 31, 2010.

More significantly, the market prices of the impaired trust preferred securities also currently reflect the effect of reduced demand for such securities given the increasingly credit risk-averse nature of financial institutions in the current marketplace. Additionally, such prices reflect the effects of increased supply arising from financial institutions selling such investments and reducing assets for capital adequacy purposes, as noted earlier.

In sum, the factors influencing the fair value of the Company's investment-grade trust preferred securities, as described above, generally result from movements in market interest rates and changing market conditions which affect the supply and demand for such securities. Inasmuch as such market conditions fluctuate over time, the "noncredit-related" impairments of value arising from these changing market conditions are "temporary" in nature.

The impairments of the Company's trust preferred securities with one or more non-investment grade ratings are further evaluated to determine if such impairments are "credit-related". Factors considered in this evaluation include, but may not be limited to, the financial strength and viability of the issuer and its parent company, the security's historical performance through prior business and economic cycles, rating consistency or variability among rating companies, the security's current and anticipated status regarding payment default or deferral of contractual payments to investors and the impact of these factors on the present value of the security's expected future cash flows in relation to its amortized cost basis.

At December 31, 2010, the Company owned two securities at an amortized cost of \$4.9 million that were rated as investment grade by Moody's, but below investment grade by S&P. The securities were originally issued through BankBoston Capital Trust IV and MBNA Capital B and currently represent de-facto obligations of Bank of America Corporation.

In evaluating the impairment associated with these securities, the Company noted the overall financial strength and continuing expected viability of the issuing entity's parent, particularly given their systemically critical role in the marketplace. The Company noted the security's absence of historical defaults or payment deferrals throughout prior business cycles including the recent fiscal crisis that triggered the current economic weaknesses prevalent in the marketplace. The Company also noted the disparity between investment-grade and non-investment grade ratings for the securities among rating companies which demonstrates the current level of uncertainty regarding credit-risk in the marketplace. Given these factors, the Company had no basis upon which to estimate an adverse change in the expected cash flows over the securities' remaining terms to maturity.

While all of its trust preferred securities are classified as available for sale, the Company has both the ability and intent, as of the periods presented, to hold the impaired securities until their fair values recover to a level equal to or greater than the Company's amortized cost. As such, the Company has not decided to sell the securities as of December 31, 2010 and has further concluded that the possibility of being required to sell the securities prior to their anticipated recovery is unlikely based upon its strong liquidity, asset quality and capital position as of that date. Moreover, the Company purchased these securities at nominal discounts. Accordingly, the Company expects that the securities will not be settled for a price less than its amortized cost.

In light of the factors noted above, the Company does not consider its investments in trust preferred securities with unrealized losses at December 31, 2010 to be “other-than-temporarily” impaired as of that date.

The following table presents roll forwards of OTTI recognized in earnings due to credit-related losses on securities still held at the end of each reporting period.

	Activity in credit-related other-than-temporary impairment (“OTTI”) recognized through earnings					Cumulative balance of credit-related OTTI recognized in earnings - ending
	Cumulative balance of credit-related OTTI recognized in earnings - beginning	Additions for newly identified credit-related OTTI	Additions to existing OTTI for further credit-related declines in fair value	Reductions in credit-related OTTI for security sale	Reductions in credit-related OTTI due to accretion of impairment into interest income	
(In Thousands)						
Collateralized mortgage obligations:						
Non-agency securities:						
Three months ended December 31, 2010	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Six months ended December 31, 2010	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Three months ended December 31, 2009	\$ 532	\$ 1	\$ 54	\$ -	\$ -	\$ 587
Six months ended December 31, 2009	\$ 434	\$ 8	\$ 145	\$ -	\$ -	\$ 587

12. LOAN QUALITY AND ALLOWANCE FOR LOAN LOSSES

Loan Review System. The Company maintains a loan review system consisting of several related functions including, but not limited to, classification of assets, calculation of the allowance for loan losses, independent credit file review as well as internal audit and lending compliance reviews. The Company utilizes both internal and external resources, where appropriate, to perform the various loan review functions. For example, the Company has engaged the services of a third party firm specializing in loan review and analysis to perform several loan review functions. This firm reviews the loan portfolio in accordance with the scope and frequency determined by senior management and the Asset Quality Committee of the Board of Directors. The third party loan review firm assists senior management and the board of directors in identifying potential credit weaknesses; in appropriately grading or adversely classifying loans; in identifying relevant trends that affect the collectability of the portfolio and identify segments of the portfolio that are potential problem areas; in verifying the appropriateness of the allowance for loan losses; in evaluating the activities of lending personnel including compliance with lending policies and the quality of their loan approval, monitoring and risk assessment; and by providing an objective assessment of the overall quality of the loan portfolio. Currently, independent loan reviews are being conducted quarterly and include non-performing loans as well as samples of performing loans of varying types within the Company’s portfolio.

The Company's loan review system also includes the internal audit and compliance functions, which operate in accordance with a scope determined by the Audit and Compliance Committees of the Board of Directors. Internal audit resources assess the adequacy of, and adherence to, internal credit policies and loan administration procedures. Similarly, the Company's compliance resources monitor adherence to relevant lending-related and consumer protection-related laws and regulations. The loan review system is structured in such a way that the internal audit function maintains the ability to independently audit other risk monitoring functions without impairing its independence with respect to these other functions.

As noted, the loan review system also comprises the Company's policies and procedures relating to the regulatory classification of assets and the allowance for loan loss functions each of which are described in greater detail below.

Classification of Assets. In compliance with the regulatory guidelines, management maintains an internal loan review program, whereby certain loans exhibiting adverse credit quality characteristics are classified "Special Mention", "Substandard", "Doubtful" or "Loss". It is our policy to review the loan portfolio in accordance with regulatory classification procedures, generally on a monthly basis. Management evaluates loans classified as substandard or doubtful for impairment in accordance with applicable accounting requirements. Management classifies the impaired portion of a loan as "Loss" through which a specific valuation allowance equal to 100% of the impairment is established.

An asset is classified as "Substandard" if it is inadequately protected by the paying capacity and net worth of the obligor or the collateral pledged, if any. Substandard assets include those characterized by the distinct possibility that the insured institution will sustain some loss if the deficiencies are not corrected. Assets classified as "Doubtful" have all of the weaknesses inherent in those classified as "Substandard", with the added characteristic that the weaknesses present make collection or liquidation in full highly questionable and improbable, on the basis of currently existing facts, conditions and values. Assets, or portions thereof, classified as "Loss" are considered uncollectible or of so little value that their continuance as assets is not warranted. Assets classified as "Loss" are either charged off directly against the allowance for loan loss or a specific valuation allowance equal to 100% of the loss is established as noted above.

Assets which do not currently expose the Company to a sufficient degree of risk to warrant an adverse classification but have some credit deficiencies or other potential weaknesses are designated as "Special Mention" by management. Adversely classified assets, together with those rated as "Special Mention", are generally referred to as "Classified Assets". Non-classified assets are internally rated as either "Pass" or "Watch" with the latter denoting a potential deficiency or concern that warrants increased oversight or tracking by management until remediated.

Management performs a classification of assets review, including the regulatory classification of assets, generally on a monthly basis. The results of the classification of assets review are validated by the Company's third party loan review firm during their quarterly, independent review. In the event of a difference in rating or classification between those assigned by the internal and external resources, the Company will generally utilize the more critical or conservative rating or classification. Final loan ratings and regulatory classifications are presented monthly to the Board of Directors and are reviewed by regulators during the examination process.

Allowance for Loan Losses. The allowance for loan losses is a valuation account that reflects the Company's estimation of the losses in its loan portfolio to the extent they are both probable and reasonable to estimate. The balance of the allowance is generally maintained through provisions for loan losses that are charged to income in the period that estimated losses on loans are identified by the

Company's loan review system. The Company charges losses on loans against the allowance as such losses are actually incurred. Recoveries on loans previously charged-off are added back to the allowance.

The Company's allowance for loan loss calculation methodology utilizes a "two-tier" loss measurement process that is performed monthly. Based upon the results of the classification of assets and credit file review processes described earlier, the Company first identifies the loans that must be reviewed individually for impairment. Loans eligible for individual impairment review generally represent the Company's larger and/or more complex loans including commercial mortgage loans, comprising multi-family and nonresidential real estate loans, as well as construction loans and commercial business loans. However, the Company may also evaluate certain individual one-to-four family mortgage loans, home equity loans and home equity lines of credit for impairment based upon certain risk factors. Factors considered in identifying individual loans to be reviewed include, but may not be limited to, delinquency status, size of loan, type and condition of collateral and the financial condition of the borrower.

A reviewed loan is deemed to be impaired when, based on current information and events, it is probable that we will be unable to collect all amounts due according to the contractual terms of the loan agreement. Once a loan is determined to be impaired, management measures the amount of impairment associated with that loan. Impairment is generally defined as the difference between the carrying value and fair value of a loan where former exceeds the latter. For the collateral dependent mortgage loans, the fair value of the real estate collateralizing the loan serves as a practical expedient for that of the impaired loan itself. Such values are generally determined based upon a discounted market value obtained through an automated valuation module or prepared by a qualified, independent real estate appraiser. As supported by the accounting and regulatory guidance, the fair value of the collateral is further reduced by estimated selling costs when such costs are expected to reduce the cash flows available to repay the loan.

The Company establishes specific valuation allowances in the fiscal period during which the loan impairments are identified. The results of management's specific loan impairment evaluation are validated by the Company's third party loan review firm during their quarterly, independent review. Such valuation allowances are adjusted in subsequent fiscal periods, where appropriate, to reflect any changes in carrying value or fair value identified during subsequent impairment evaluations which are updated monthly by management.

The second tier of the loss measurement process involves estimating the probable and estimable losses which addresses loans not otherwise reviewed individually for impairment. Such loans generally comprise large groups of smaller-balance homogeneous loans, such as one-to-four family mortgage loans, home equity loans and home equity lines of credit and other consumer loans, that may generally be excluded from individual impairment analysis and instead collectively evaluated for impairment. Such loans also include the remaining non-impaired loans of the larger and/or more complex types, such as the Company's commercial mortgage, construction and business loans, which were not individually reviewed for impairment.

Valuation allowances established through the second tier of the loss measurement process utilize historical and environmental loss factors to collectively estimate the level of probable losses within defined segments of the Company's loan portfolio. These segments aggregate homogeneous subsets of loans with similar risk characteristics based upon loan type. For allowance for loan loss calculation and reporting purposes, the Company currently stratifies its loan portfolio into five primary categories: residential mortgage loans, commercial mortgage loans, construction loans, commercial business loans and consumer loans. Within the consumer loan category, the Company distinguishes between home equity loans, home equity lines of credit and other consumer loans. Beyond these primary categories, the Company further delineates commercial business loans into secured and unsecured loans while loans may

also be identified and grouped based on origination source to distinguish those with unique risk characteristics associated with certain purchased loans and participations.

In regard to historical loss factors, the Company's allowance for loan loss calculation calls for an analysis of historical charge-offs and recoveries for each of the defined segments within the loan portfolio. The Company currently utilizes a two-year moving average of annual net charge-off rates (charge-offs net of recoveries) by loan segment, where available, to calculate its actual, historical loss experience. The Company utilizes a two-year "look-back" period to determine the average charge-off history used in the calculation of historical loss. The outstanding principal balance of each loan segment is multiplied by the applicable historical loss factor to estimate the level of probable losses based upon the Company's historical loss experience.

As noted, the Company's allowance for loan loss calculation also utilizes environmental loss factors to estimate the probable losses within the loan portfolio. Environmental loss factors are based upon specific qualitative criteria representing key sources of risk within the loan portfolio. Such risk criteria includes the level of and trends in delinquencies and non-accrual loans; the effects of changes in credit policy; the experience, ability and depth of the lending function's management and staff; national and local economic trends and conditions; credit risk concentrations and changes in local and regional real estate values. For each segment of the loan portfolio, a level of risk, developed from a number of internal and external resources, is assigned to each of the qualitative criteria utilizing a scale ranging from zero (negligible risk) to 15 (high risk). The sum of the risk values, expressed as a whole number, is multiplied by .01% to arrive at an overall environmental loss factor, expressed in basis points, for each segment. The outstanding principal balance of each loan segment is multiplied by the applicable environmental loss factor to estimate the level of probable losses based upon the qualitative risk criteria.

The sum of the probable and estimable loan losses calculated through the first and second tiers of the loss measurement processes as described above, represents the total targeted balance for the Company's allowance for loan losses at the end of a fiscal period. As noted earlier, the Company establishes all additional specific valuation allowances in the fiscal period during which additional loan impairments are identified. This step is generally performed by transferring the required additions to specific valuation allowances on impaired loans from the balance of Company's general valuation allowances. After establishing all specific valuation allowances relating to impaired loans, the Company then compares the remaining actual balance of its general valuation allowance to the targeted balance calculated at the end of the fiscal period. The Company adjusts its balance of general valuation allowances through the provision for loan losses as required to ensure that the balance of the allowance for loan losses reflects all probable and estimable loans losses at the close of the fiscal period. Any balance of general valuation allowances in excess of the targeted balance is reported as unallocated with such balances attributable to probable losses within the loan portfolio relating to environmental factors within one or more non-specified loan segments. Notwithstanding calculation methodology and the noted distinction between specific and general valuation allowances, the Company's entire allowance for loan losses is available to cover all charge-offs that arise from the loan portfolio.

Although management believes that specific and general loan losses are established in accordance with management's best estimate, actual losses are dependent upon future events and, as such, further additions to the level of loan loss allowances may be necessary.

Edgar Filing: Kearny Financial Corp. - Form 10-Q

The following table presents the balance of the allowance for loan losses based upon the calculation methodology described above. The table identifies the specific valuation allowances attributable to identified impairments on individually evaluated loans, as well as those acquired with deteriorated credit quality, and the general valuation allowances for impairments on loans evaluated collectively. The underlying balance of loans receivable applicable to each category is also presented. The balance of loans receivable reported in the tables below excludes yield adjustments and the allowance for loan loss.

Allowance for Loan Losses and Loans Receivable
at December 31, 2010

	Residential Mortgage (In Thousands)	Commercial Mortgage	Commercial Construction	Commercial Business	Home Equity Loans	Home Equity Lines of Credit	Other Consumer	Total
Balance of allowance for loan losses based on:								
Loans individually evaluated for impairment	\$ 3,114	\$ 1,750	\$ 598	\$ -	\$ -	\$ -	\$ -	\$ 5,462
Loans acquired with deteriorated credit quality	-	-	-	-	-	-	-	-
Loans collectively evaluated for impairment	2,065	1,656	93	111	271	30	12	4,238
Total allocated allowance for loan losses	5,179	3,406	691	111	271	30	12	9,700
Unallocated allowance								231
Total allowance for loan losses	\$ 5,179	\$ 3,406	\$ 691	\$ 111	\$ 271	\$ 30	\$ 12	\$ 9,931
Balance of loans receivable:								
Loans individually evaluated for impairment	\$ 11,622	\$ 11,631	\$ 2,142	\$ 3,342	\$ -	\$ -	\$ -	\$ 28,737

Edgar Filing: Kearny Financial Corp. - Form 10-Q

Loans acquired with deteriorated credit quality	-	2,742	1,597	8,194	-	-	-	12,533
Loans collectively evaluated for impairment	620,431	374,130	29,809	93,936	123,578	32,482	5,127	1,279,493
Total loans	\$ 632,053	\$ 388,503	\$ 33,548	\$ 105,472	\$ 123,578	\$ 32,482	\$ 5,127	\$ 1,320,763

-33-

Edgar Filing: Kearny Financial Corp. - Form 10-Q

The following tables present key indicators of credit quality regarding the Company's loan portfolio based upon loan classification and contractual payment status at December 31, 2010.

Credit-Rating Classification of Loans Receivable
at December 31, 2010

	Residential Mortgage (In Thousands)	Commercial Mortgage	Construction	Commercial Business	Home Equity Loans	Home Equity Lines of Credit	Other Consumer	Total
Loan classification								
Non-classified	\$613,396	\$ 368,120	\$ 28,114	\$ 83,758	\$122,335	\$32,326	\$ 5,123	\$1,253,172
Classified:								
Special mention	1,215	2,913	895	9,286	980	58	4	15,351
Substandard	14,328	15,720	3,941	11,643	263	98	-	45,993
Doubtful	-	-	-	785	-	-	-	785
Loss	3,114	1,750	598	-	-	-	-	5,462
Total loans	\$632,053	\$ 388,503	\$ 33,548	\$ 105,472	\$123,578	\$32,482	\$ 5,127	\$1,320,763

Contractual Payment Status of Loans Receivable
at December 31, 2010

	Residential Mortgage (In Thousands)	Commercial Mortgage	Construction	Commercial Business	Home Equity Loans	Home Equity Lines of Credit	Other Consumer	Total
Contractual payment status:								
Current	\$613,007	\$ 376,889	\$ 28,053	\$ 98,776	\$122,738	\$32,360	\$ 5,048	\$1,276,871
Past due:								
30-59 days	2,365	2,883	695	1,114	160	24	59	7,300
60-89 days	746	451	1,390	1,560	417	-	20	4,584
90+ days	15,935	8,280	3,410	4,022	263	98	-	32,008
Total past due	19,046	11,614	5,495	6,696	840	122	79	43,892
Total loans	\$632,053	\$ 388,503	\$ 33,548	\$ 105,472	\$123,578	\$32,482	\$ 5,127	