

Bankwell Financial Group, Inc.
Form 10-Q
November 14, 2014

UNITED STATES
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 September 30, 2014

- 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: 001-36448

Bankwell Financial Group, Inc.
(Exact Name of Registrant as specified in its Charter)

Connecticut
(State or other jurisdiction of
Incorporation or organization)

20-8251355
(I.R.S. Employer
Identification No.)

220 Elm Street
New Canaan, Connecticut 06840
(203) 652-0166

(Address, including zip code, and telephone number, including area code, of registrant's principal executive offices)

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

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

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

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

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

As of October 31, 2014, there were 7,068,382 shares of the registrant's common stock outstanding.

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PART 1 – FINANCIAL INFORMATION

Item 1. Financial Statements

Bankwell Financial Group, Inc.

Consolidated Balance Sheets - (Unaudited)

(Dollars in thousands, except share data)

	September 30, 2014	December 31, 2013
ASSETS		
Cash and due from banks	\$35,566	\$82,013
Held to maturity investment securities, at amortized cost (Note 2)	11,502	13,816
Available for sale investment securities, at fair value (Note 2)	67,537	28,597
Loans held for sale	-	100
Loans receivable (net of allowance for loan losses of \$9,552 at September 30, 2014 and \$8,382 at December 31, 2013) (Note 3)	730,148	621,830
Foreclosed real estate	829	829
Accrued interest receivable	2,670	2,360
Federal Home Loan Bank stock, at cost	4,834	4,834
Premises and equipment, net	7,787	7,060
Bank-owned life insurance	22,837	10,031
Other intangible assets	401	481
Deferred income taxes, net	5,804	5,845
Other assets	5,600	1,822
Total assets	\$895,515	\$779,618
LIABILITIES AND SHAREHOLDERS' EQUITY		
Liabilities		
Deposits		
Noninterest bearing deposits	\$151,146	\$118,618
Interest bearing deposits	544,117	542,927
Total deposits	695,263	661,545
Advances from the Federal Home Loan Bank	77,000	44,000
Accrued expenses and other liabilities	4,755	4,588
Total liabilities	777,018	710,133
Shareholders' equity (Notes 4, 5 and 7)		
Preferred stock, senior noncumulative perpetual, Series C, no par; 10,980 shares issued at September 30, 2014 and December 31, 2013, respectively; liquidation value of \$1,000 per share	10,980	10,980
Common stock, no par value; 10,000,000 shares authorized, 6,559,995 and 3,876,393 shares issued at September 30, 2014 and December 31, 2013, respectively	97,180	52,105
Retained earnings	9,735	5,976
Accumulated other comprehensive income	602	424
Total shareholders' equity	118,497	69,485

Total liabilities and shareholders' equity	\$895,515	\$779,618
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See accompanying notes to consolidated financial statements (unaudited)

Bankwell Financial Group, Inc.
Consolidated Statements of Income – (Unaudited)
(Dollars in thousands, except per share amounts)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Interest and dividend income				
Interest and fees on loans	\$8,054	\$6,748	\$23,040	\$19,619
Interest and dividends on securities	569	355	1,417	1,040
Interest on cash and cash equivalents	45	18	116	39
Total interest income	8,668	7,121	24,573	20,698
Interest expense				
Interest expense on deposits	905	600	2,257	1,553
Interest on Borrowings	168	127	427	417
Total interest expense	1,073	727	2,684	1,970
Net interest income	7,595	6,394	21,889	18,728
Provision for loan losses	566	47	847	489
Net interest income after provision for loan losses	7,029	6,347	21,042	18,239
Noninterest income				
Gains and fees from sales of loans	366	972	1,008	1,737
Service charges and fees	153	100	420	297
Bank owned life insurance	135	-	305	-
Net gain on sale of available for sale securities	-	-	-	648
Gain (loss) on sale of foreclosed real estate, net	-	(16)	-	49
Other	103	27	475	141
Total noninterest income	757	1,083	2,208	2,872
Noninterest expense				
Salaries and employee benefits	2,786	2,894	9,412	8,146
Occupancy and equipment	1,066	836	3,162	2,410
Professional services	394	422	1,035	1,212
Data processing	314	280	949	787
Director fees	177	142	460	426
Merger and acquisition related expenses	145	-	408	64
Marketing	135	378	463	776
FDIC insurance	120	36	345	267
Amortization of intangibles	27	-	80	-
Foreclosed real estate	9	1	21	4
Other	357	342	1,134	950
Total noninterest expense	5,530	5,331	17,469	15,042

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Income before income tax expense	2,256	2,099	5,781	6,069
Income tax expense	765	780	1,940	2,270
Net income	\$1,491	\$1,319	\$3,841	\$3,799
Net income attributable to common shareholders	\$1,441	\$1,271	\$3,677	\$3,660
Earnings per common share - basic	\$0.22	\$0.38	\$0.72	\$1.12
Earnings per common share - diluted	0.22	0.37	0.72	1.10

See accompanying notes to consolidated financial statements (unaudited)

Bankwell Financial Group, Inc.
Consolidated Statements of Comprehensive Income – (Unaudited)
(In thousands)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Net income	\$ 1,491	\$ 1,319	\$ 3,841	\$ 3,799
Other comprehensive income (loss):				
Unrealized gains (losses) on securities:				
Unrealized holding gains (losses) on available for sale securities	(253)	(13)	180	(920)
Reclassification adjustment for (gain) loss realized in net income	-	-	-	(648)
Net change in unrealized gain (loss)	(253)	(13)	180	(1,568)
Tax effect - (expense) benefit	99	5	(70)	610
Unrealized gains (losses) on securities, net of tax	(154)	(8)	110	(958)
Unrealized gains (losses) on interest rate swap:				
Unrealized gains (losses) on interest rate swaps designated as cash flow hedge	218	-	111	-
Tax effect - (expense) benefit	(85)	-	(43)	-
Unrealized gains (losses) on interest rate swap	133	-	68	-
Total other comprehensive income (loss)	(21)	(8)	178	(958)
Comprehensive income	\$ 1,470	\$ 1,311	\$ 4,019	\$ 2,841

See accompanying notes to consolidated financial statements (unaudited)

Bankwell Financial Group, Inc.
 Consolidated Statements of Shareholders' Equity – (Unaudited)
 (In thousands, except share data)

	Preferred Stock	Common Stock	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
Balance at December 31, 2012	\$ 10,980	\$ 38,117	\$ 926	\$ 1,511	\$ 51,534
Net income	-	-	3,799	-	3,799
Other comprehensive loss, net of tax	-	-	-	(958)	(958)
Preferred stock dividends	-	-	(84)	-	(84)
Stock based compensation expense	-	205	-	-	205
Capital from exercise of stock options	-	471	-	-	471
Capital from private placement	-	13,178	-	-	13,178
Balance at September 30, 2013	\$ 10,980	\$ 51,971	\$ 4,641	\$ 553	\$ 68,145

	Preferred Stock	Common Stock	Retained Earnings	Accumulated Other Comprehensive Income	Total
Balance at December 31, 2013	\$ 10,980	\$ 52,105	\$ 5,976	\$ 424	\$ 69,485
Net income	-	-	3,841	-	3,841
Other comprehensive income, net of tax	-	-	-	178	178
Preferred stock dividends	-	-	(82)	-	(82)
Stock based compensation expense	-	164	-	-	164
Capital from exercise of stock options	-	207	-	-	207
Issuance of 2,702,703 shares, net of expenses	-	44,704	-	-	44,704
Balance at September 30, 2014	\$ 10,980	\$ 97,180	\$ 9,735	\$ 602	\$ 118,497

See accompanying notes to consolidated financial statements (unaudited)

Bankwell Financial Group, Inc.
Consolidated Statements of Cash Flows – (Unaudited)
(In thousands)

	Nine Months Ended September 30,	
	2014	2013
Cash flows from operating activities		
Net income	\$3,841	\$3,799
Adjustments to reconcile net income to net cash provided by operating activities:		
Net amortization of premiums and discounts on investment securities	82	151
Provision for loan losses	847	489
Benefit for deferred taxes	(213)	(43)
Net gain on sales of available for sale securities	-	(648)
Depreciation and amortization	835	440
Increase in cash surrender value of bank-owned life insurance	(305)	-
Loans originated for sale	(22,465)	(59,580)
Proceeds from sales of loans	23,572	61,316
Net gain on sales of loans	(1,008)	(1,737)
Equity-based compensation	164	205
Net accretion of purchase accounting adjustments	(352)	-
Gain on sale of foreclosed real estate	-	(49)
Net change in:		
Deferred loan fees	583	297
Accrued interest receivable	(311)	(55)
Other assets	(3,524)	(71)
Accrued expenses and other liabilities	167	(1,390)
Net cash provided by operating activities	1,913	3,124
Cash flows from investing activities		
Proceeds from principal repayments on available for sale securities	3,307	638
Proceeds from principal repayments on held to maturity securities	2,308	145
Net proceeds from sales and calls of available for sale securities	1,620	10,194
Purchases of held to maturity securities	-	(7,700)
Purchase of available for sale securities	(43,763)	-
Purchase of bank-owned life insurance	(12,500)	-
Net increase in loans	(109,323)	(54,334)
Purchases of premises and equipment	(1,562)	(450)
Purchase of Federal Home Loan Bank stock	-	(134)
Proceeds from sale of foreclosed real estate	-	1,011
Net cash used by investing activities	(159,913)	(50,630)

See accompanying notes to consolidated financial statements (unaudited)

Consolidated Statements of Cash Flows- (Continued)
(In thousands)

	Nine Months Ended September 30,	
	2014	2013
Cash flows from financing activities		
Net change in time certificates of deposit	\$38,569	\$68,400
Net change in other deposits	(4,845)	13,643
Net proceeds (repayments) from short term FHLB advances	40,000	(13,000)
Net proceeds (repayments) from long term FHLB advances	(7,000)	(13,000)
Proceeds from issuance of common stock	44,704	13,178
Proceeds from exercise of options	207	471
Dividends paid on preferred stock	(82)	(84)
Net cash provided by financing activities	111,553	69,608
Net increase (decrease) in cash and cash equivalents	(46,447)	22,102
Cash and cash equivalents:		
Beginning of year	82,013	28,927
End of period	\$35,566	\$51,029
Supplemental disclosures of cash flows information:		
Cash paid for:		
Interest	\$2,742	\$1,872
Income taxes	450	2,042
Noncash investing and financing activities	-	-

See accompanying notes to consolidated financial statements (unaudited)

Bankwell Financial Group, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

1. Nature of Operations and Summary of Significant Accounting Policies

Bankwell Financial Group, Inc. (the “Company” or “Bankwell”) is a bank holding company headquartered in New Canaan, Connecticut. The Company offers a broad range of financial services through its banking subsidiary, Bankwell Bank, (the “Bank”). The Bank was originally chartered as two separate banks, The Bank of New Canaan (“BNC”) and The Bank of Fairfield (“TBF”). In September 2013, BNC and TBF were merged and rebranded as “Bankwell Bank.” In November 2013, the Bank acquired The Wilton Bank (“Wilton”), which added one branch and approximately \$25.1 million in loans and \$64.2 million in deposits. See Note 12, Mergers and Acquisitions, for further information on the acquisition.

The Bank is a Connecticut state chartered commercial bank, founded in 2002, whose deposits are insured under the Deposit Insurance Fund administered by the Federal Deposit Insurance Corporation (“FDIC”). The Bank provides a full range of banking services to commercial and consumer customers, primarily concentrated in the Fairfield County region of Connecticut, with branch locations in New Canaan, Stamford, Fairfield and Wilton Connecticut. The Company has received approval from its regulators to establish a branch location in Norwalk, Connecticut, which is expected to open in the first quarter of 2015. In addition, The Company acquired Quinnipiac Bank and Trust Company on October 1, 2014. The acquisition expanded the Company’s branch locations to New Haven County, Connecticut, adding a branch in Hamden Connecticut and North Haven, Connecticut. See note 13, *Subsequent Events* for further information about the merger with Quinnipiac Bank and Trust Company.

Principles of consolidation

The consolidated interim financial statements include the accounts of the Company and the Bank. All significant intercompany accounts and transactions have been eliminated in consolidation.

Use of estimates

The accounting and reporting policies of the Company conform to accounting principles generally accepted in the United States of America (“GAAP”) and general practices within the banking industry. In preparing the interim consolidated financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosures of contingent assets and liabilities as of the date of the balance sheet and revenue and expenses for the period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to deferred taxes, the fair values of financial instruments and the determination of the allowance for loan losses.

Basis of consolidated financial statement presentation

The unaudited consolidated financial statements presented herein have been prepared pursuant to the rules of the Securities and Exchange Commission (“SEC”) for quarterly reports on Form 10-Q and Rule 10-1 of Regulation S-X and do not include all of the information and note disclosures required by GAAP. In the opinion of management, all adjustments (consisting of normal recurring adjustments) and disclosures considered necessary for the fair presentation of the accompanying unaudited interim consolidated financial statements have been included. Interim results are not necessarily reflective of the results that may be expected for the year ending December 31, 2014. The accompanying unaudited interim consolidated financial statements should be read in conjunction with the audited

consolidated financial statements and notes thereto included in the Registration Statement on Form S-1 for the year ended December 31, 2013.

Significant concentrations of credit risk

Most of the Company's activities are with customers located within Fairfield County and the surrounding region of Connecticut, and declines in property values in these areas could significantly impact the Company. The Company has significant concentrations in commercial real estate loans. Management does not believe they present any special risk. The Company does not have any significant concentrations in any one industry or customer.

Bankwell Financial Group, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

Derivative Instruments

The Company enters into interest rate swap agreements as part of the Company's interest rate risk management strategy. Management applies the hedge accounting provisions of Accounting Standards Codification ("ASC") Topic 815, and formally documents at inception all relationships between hedging instruments and hedged items, as well as its risk management objectives and strategies for undertaking the various hedges. Additionally, the Company uses dollar offset or regression analysis at the hedge's inception and for each reporting period thereafter, to assess whether the derivative used in its hedging transaction is expected to be and has been highly effective in offsetting changes in the fair value or cash flows of the hedged item. The Company discontinues hedge accounting when it is determined that a derivative is not expected to be or has ceased to be highly effective as a hedge, and then reflects changes in fair value of the derivative in earnings after termination of the hedge relationship.

The Company has characterized all of its interest rate swaps that qualify under Topic 815 hedge accounting as cash flow hedges. Cash flow hedges are used to minimize the variability in cash flows of assets or liabilities, or forecasted transactions caused by interest rate fluctuations, and are recorded at fair value in other assets within the consolidated balance sheet. Changes in the fair value of these cash flow hedges are initially recorded in accumulated other comprehensive income and subsequently reclassified into earnings when the forecasted transaction affects earnings. Any hedge ineffectiveness assessed as part of the Company's quarterly analysis is recorded directly to earnings.

Reclassification

Certain prior period amounts have been reclassified to conform to the 2014 financial statement presentation. These reclassifications only changed the reporting categories and did not affect the results of operations or consolidated financial position.

Recent accounting pronouncements

The following section includes changes in accounting principles and potential effects of new accounting guidance and pronouncements.

ASU No. 2013-11-Income Taxes (Topic 740) - Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists (a consensus of the FASB Emerging Issues Task Force).

As a result of applying this ASU, an unrecognized tax benefit should be presented as a reduction of a deferred tax asset for a net operating loss ("NOL") or other tax credit carryforward when settlement in this manner is available under the tax law. The assessment of whether settlement is available under the tax law would be based on facts and circumstances as of the balance sheet reporting date and would not consider future events (e.g., upcoming expiration of related NOL carryforwards). This classification should not affect an entity's analysis of the realization of its deferred tax assets. Gross presentation in the roll forward of unrecognized tax positions in the notes to the financial statements will still be required. For the Company, the update was effective prospectively for annual reporting periods beginning on or after January 1, 2014, and interim periods within those annual periods. Retrospective application is permitted. Adoption of this ASU did not have a material impact on the Company's consolidated financial statements.

Bankwell Financial Group, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

ASU No. 2014-04 - Troubled Debt Restructuring by Creditors (Subtopic 310-40) - Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure (a consensus of the FASB Emerging Issues Task Force).

The amendments in this update apply to all creditors who obtain physical possession (resulting from an in substance repossession or foreclosure) of residential real estate property collateralizing a consumer mortgage loan in satisfaction of a receivable. The objective of the amendments in this update is to reduce diversity by clarifying when an in substance repossession or foreclosure occurs, that is, when a creditor should be considered to have received physical possession of residential real estate property collateralizing a consumer mortgage loan such that the loan receivable should be derecognized and the real estate property recognized. Additionally, the amendments require interim and annual disclosure of both (1) the amount of foreclosed residential real estate property held by the creditor and (2) the recorded investment in consumer mortgage loans collateralized by residential real estate property that are in the process of foreclosure according to requirements of the applicable jurisdiction. The amendments in this update are effective for the Company for annual reporting periods beginning on or after January 1, 2015, and interim periods within those annual periods. Adoption of this ASU is not expected to have a material impact on the Company's consolidated financial statements.

ASU No. 2014-09 - Revenue from Contracts with Customers (Topic 660).

This update requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. The ASU will replace most existing revenue recognition guidance in U.S. GAAP when it becomes effective. The new standard is effective for the Company on January 1, 2017. Early application is not permitted. The standard permits the use of either the retrospective or cumulative effect transition method. The Company is evaluating the effect that ASU 2014-09 will have on its consolidated financial statements and related disclosures. The Company has not yet selected a transition method nor has it determined the effect of the standard on its ongoing financial reporting.

ASU No. 2014-12 - Compensation-Stock Compensation (Topic 718) - Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period a consensus of the FASB Emerging Issues Task Force.

The amendments in this update require that a performance target that affects vesting and that could be achieved after the requisite service period be treated as a performance condition. As such, the performance target should not be reflected in estimating the grant-date fair value of the award. Compensation cost should be recognized in the period in which it becomes probable that the performance target will be achieved and should represent the compensation cost attributable to the period(s) for which the requisite service has already been rendered. If the performance target becomes probable of being achieved before the end of the requisite service period, the remaining unrecognized compensation cost should be recognized prospectively over the remaining requisite service period. The amendments in this update are effective for the Company for annual periods and interim periods beginning on or after January 1, 2016. Earlier adoption is permitted. Adoption of this ASU is not expected to have a material impact on the Company's consolidated financial statements.

Bankwell Financial Group, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

ASU No. 2014-14 - Receivables - Troubled Debt Restructurings by Creditors (Subtopic 310-40) - Classification of Certain Government-Guaranteed Mortgage Loans upon Foreclosure a Consensus of the FASB Emerging Issues Task Force.

The objective of this update is to reduce the diversity in classification of government-guaranteed mortgage loans, including FHA or VA guaranteed loans, upon foreclosure. The amendments in this update are effective for the Company for annual periods and interim periods beginning on or after January 1, 2016. Earlier adoption is permitted. Adoption of this ASU is not expected to have a material impact on the Company's consolidated financial statements.

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Bankwell Financial Group, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

2. Investment Securities

The amortized cost, gross unrealized gains and losses and fair values of available for sale and held to maturity securities at September 30, 2014 were as follows:

	Amortized Cost (In thousands)	Gains	September 30, 2014 Gross Unrealized Losses	Fair Value
Available for sale securities:				
U.S. Government and agency obligations				
Due from one through five years	\$ 4,994	\$ 5	\$ (59)	\$ 4,940
Due from five through ten years	20,995	15	(174)	20,836
Due after ten years	7,961	2	(4)	7,959
	33,950	22		