

WILLIAM PENN BANCORP INC  
Form 10-Q  
May 15, 2008  
UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

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FORM 10-Q

(Mark One)

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

For the Quarterly Period Ended March 31, 2008

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 0-53172

**WILLIAM PENN BANCORP, INC.**  
(Exact name of registrant as specified in its charter)

**United States**  
(State or other jurisdiction of  
incorporation or organization)

**37-1562563**  
(I.R.S. Employer  
Identification No.)

**8150 Route 13, Levittown, Pennsylvania**  
(Address of principal executive offices)

**19057**  
(Zip Code)

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**(215) 945-1200**

(Registrant's telephone number, including area code)

**Not applicable**

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

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 is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definition of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act:

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a 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 May 14, 2008, there were 3,641,018 shares of the issuer's common stock outstanding.

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**WILLIAM PENN BANCORP, INC.**

**QUARTERLY REPORT ON FORM 10-Q**

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**PART I – FINANCIAL INFORMATION****Item 1. Financial Statements****William Penn Bank, FSB****Consolidated Balance Sheets (In Thousands)**

	<b>March 31, 2008 (Unaudited)</b>	<b>June 30, 2007</b>
<b>ASSETS</b>		
Cash and due from banks	\$ 13,373	\$ 14,229
Interest bearing time deposits	3,749	3,418
Securities available for sale	15	25
Securities held to maturity, fair value \$60,380 and \$61,049	58,959	61,637
Loans receivable, net of allowance for loan losses \$1,860 and \$1,840	185,751	180,204
Premises and equipment, net	1,846	1,937
Federal Home Loan Bank stock, at cost	3,642	3,838
Deferred income taxes	1,727	1,816
Accrued interest receivable and other assets	2,209	1,726
<b>Total Assets</b>	<b>\$ 271,271</b>	<b>\$ 268,830</b>
<b>LIABILITIES AND EQUITY</b>		
<b>Liabilities</b>		
Deposits:		
Non-interest bearing	\$ 1,242	\$ 1,755
Interest-bearing	155,735	157,185
Deposits held for Stock Purchase	9,260	—
Total Deposits	166,237	158,940
Advances from Federal Home Loan Bank	66,000	71,000
Advances from borrowers for taxes and insurance	1,985	1,947
Accrued interest payable and other liabilities	2,483	2,885
<b>Total Liabilities</b>	<b>236,705</b>	<b>234,772</b>
<b>Equity</b>	<b>34,566</b>	<b>34,058</b>
<b>Total Liabilities and Equity</b>	<b>\$ 271,271</b>	<b>\$ 268,830</b>

See accompanying notes to the unaudited consolidated financial statements.



## William Penn Bank, FSB

## Consolidated Statements of Operations (In Thousands)

	Three Months Ended		Nine Months Ended	
	March 31, 2008 (Unaudited)	2007	March 31, 2008	2007
<b>Interest Income</b>				
Loans receivable, including fees	\$ 2,920	\$ 2,837	\$ 8,913	\$ 8,568
Taxable Securities	705	707	2,383	2,152
Other	232	313	693	686
<b>Total Interest Income</b>	<b>3,857</b>	<b>3,857</b>	<b>11,989</b>	<b>11,406</b>
<b>Interest Expense</b>				
Deposits	1,462	1,572	4,783	4,584
Borrowings	808	988	2,790	2,912
<b>Total Interest Expense</b>	<b>2,270</b>	<b>2,560</b>	<b>7,573</b>	<b>7,496</b>
<b>Net Interest Income</b>	<b>1,587</b>	<b>1,297</b>	<b>4,416</b>	<b>3,910</b>
<b>Provision For Loan Losses</b>	<b>—</b>	<b>35</b>	<b>20</b>	<b>116</b>
<b>Net Interest Income after Provision for Loan Losses</b>	<b>1,587</b>	<b>1,262</b>	<b>4,396</b>	<b>3,794</b>
<b>Other Income</b>				
Service fees	32	28	97	90
Realized gains (losses) on sale of Available for Sale Securities	—	(1 )	—	6
Other	34	35	101	114
<b>Total Other Income</b>	<b>66</b>	<b>62</b>	<b>198</b>	<b>210</b>
<b>Other Expenses</b>				
Salaries and employee benefits	462	446	1,415	1,401
Termination of defined benefit pension plan	269	—	269	—
Occupancy and equipment	160	152	480	441
Prepayment Penalty on FHLB advances	—	—	1,524	—
Other	155	143	425	371
<b>Total Other Expenses</b>	<b>1,046</b>	<b>741</b>	<b>4,113</b>	<b>2,213</b>
<b>Income before Income Taxes</b>	<b>607</b>	<b>583</b>	<b>481</b>	<b>1,791</b>

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<b>Income Tax Expenses</b>	202	198	147	556
<b>Net Income</b>	\$ 405	\$ 385	\$ 334	\$ 1,235

See accompanying notes to the unaudited consolidated financial statements.

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## William Penn Bank, FSB

## Consolidated Statement of Equity (In Thousands) (Unaudited)

	Retained Earnings	Accumulated Other Comprehensive Loss	Total Equity
<b>Balance – July 1, 2006</b>	\$ 32,672	\$ —	\$ 32,672
Net income	1,235	—	1,235
<b>Balance – March 31, 2007</b>	\$ 33,907	\$ —	\$ 33,907
<b>Balance – July 1, 2007</b>	\$ 34,232	\$ (174 )	\$ 34,058
Comprehensive Income			
Net income	334	—	334
Change in unrealized loss on defined benefit pension plan, net of taxes	—	174	174
<b>Total Comprehensive Income</b>			\$ 508
Balance – March 31, 2008	\$ 34,566	\$ —	\$ 34,566

See accompanying notes to unaudited consolidated financial statements.

## William Penn Bank, FSB

## Consolidated Statements of Cash Flows (In Thousands)

	<b>Nine Months Ended</b>	
	<b>March 31,</b>	
	<b>2008</b>	<b>2007</b>
	<b>(Unaudited)</b>	
<b>Cash Flows from Operating Activities</b>		
Net income	\$ 334	\$ 1,235
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Provision for loan losses	20	116
Provision for depreciation	123	136
Net accretion of securities premiums and discounts	(188 )	(145 )
Realized gains on sales of securities	—	(6 )
Increase in accrued interest receivable and other assets	(483 )	(109 )
Increase (decrease) in accrued interest payable and other liabilities	(139 )	11
<b>Net Cash Provided by (Used in) Operating Activities</b>	<b>(333 )</b>	<b>1,238</b>
<b>Cash Flows from Investing Activities</b>		
Securities available for sale:		
Purchases	(98 )	(7,342 )
Proceeds from sales of securities	108	7,887
Securities held to maturity:		
Purchases	(16,133 )	(26,415 )
Maturities, calls and principal paydowns	18,999	25,851
Net (increase) decrease in loans receivable	(5,567 )	335
Net increase in maturities of interest bearing time deposits	(331 )	(618 )
Net (increase) decrease in Federal Home Loan Bank Stock	196	(174 )
Purchases of premises and equipment	(32 )	(83 )
<b>Net Cash Used in Investing Activities</b>	<b>(2,858 )</b>	<b>(559 )</b>
<b>Cash Flows from Financing Activities</b>		
Net increase (decrease) in deposits	7,297	(1,792 )
Proceeds from advances from Federal Home Loan Bank	30,000	5,000
Repayment of advances from Federal Home Loan Bank	(35,000 )	—
Increase (decrease) in advances from borrowers for taxes and insurance	38	(22 )
<b>Net Cash Provided by Financing Activities</b>	<b>2,335</b>	<b>3,186</b>
<b>Net Increase (Decrease) in Cash and Cash Equivalents</b>	<b>(856 )</b>	<b>3,865</b>
<b>Cash and Cash Equivalents-Beginning</b>	<b>14,229</b>	<b>7,476</b>
<b>Cash and Cash Equivalents-Ending</b>	<b>\$ 13,373</b>	<b>\$ 11,341</b>
<b>Supplementary Cash Flows Information</b>		
Interest paid	\$ 7,555	\$ 7,546
Income taxes paid	\$ 240	\$ 390

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See accompanying notes to the unaudited consolidated financial statements.

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**WILLIAM PENN BANK, FSB**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**(UNAUDITED)**

**Note 1 – William Penn Bancorp, Inc.**

The registrant, William Penn Bancorp, Inc. (the “Company”) is a federally chartered corporation formed for the purpose of becoming the mid-tier holding company for William Penn Bank, FSB (the “Bank”) in connection with its mutual holding company reorganization.

On April 15, 2008, the Bank completed the reorganization and became a wholly-owned subsidiary of the Company. As part of the transaction, the Company sold 1,025,283 shares of its common stock, \$.10 par value, to the public at \$10.00 per share (including 87,384 shares purchased by the Bank’s Employee Stock Ownership Plan with funds borrowed from the Company) and issued 2,548,713 shares to William Penn, MHC. In addition, the Company contributed 67,022 shares to the William Penn Bank Community Foundation. Prior to consummation of the reorganization, the Company had no assets or liabilities. Accordingly, the Company’s financial statements consist of those of the Bank for periods prior to April 15, 2008.

**Note 2 - Nature of Operations**

William Penn Bank, FSB (the “Bank”) is a federally chartered savings bank. The Bank’s primary business consists of the taking of deposits and granting of mortgage loans to customers generally in the Bucks County, Pennsylvania area. The Bank is supervised and regulated by the Office of Thrift Supervision.

**Note 3 – Basis of Consolidated Financial Statement Presentation**

The consolidated financial statements include the accounts of the Bank and its wholly-owned subsidiary, WPSLA Investment Corporation. WPSLA Investment Corporation was incorporated under Delaware law to hold securities for the Bank. All intercompany transactions and balances have been eliminated in consolidation.

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, results of operations 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-month and nine month periods ended March 31, 2008, 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 balance sheet for June 30, 2007 was derived from the Bank’s audited consolidated financial statements as of June 30, 2007. That data, along with the interim financial information presented in the consolidated balance sheets, statements of operations, statement of changes in equity and statements of cash flows should be read in conjunction with the 2007 consolidated financial statements of William Penn Bank, FSB, including the notes thereto included in the Registration Statement of William Penn Bancorp, Inc. on Form S-1, as amended (File No. 333-148219). William Penn Bancorp, Inc. is a “smaller reporting company” as defined by Item 10 of Regulation S-K and the financial statements were prepared in accordance with instructions applicable for such companies.



**Note 4 – Comprehensive Income**

Accounting principles generally require that recognized revenue, expenses, gains and losses be included in net income. Although certain changes in assets and liabilities, such as unrealized gains and losses on available for sale securities and changes in unrecognized pension assets or liabilities, are reported as a separate component of the equity section of the balance sheet, such items, along with net income, are components of comprehensive income.

The components of other comprehensive income (loss) and related tax effects are as follows (in thousands):

	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>March 31,</b>		<b>March 31,</b>	
	<b>2008</b>	<b>2007</b>	<b>2008</b>	<b>2007</b>
	<b>(Unaudited)</b>			
Unrealized holding gains (losses) on available for sale securities	\$ —	\$ —	\$ —	\$ 6
Reclassification adjustment for (gains) included in net income	—	—	—	(6 )
Reclassification adjustment expense for termination of defined benefit pension plan	263	—	263	—
	263	—	263	—
<b>Net Unrealized Losses</b>				
Income tax effect	89	—	89	—
<b>Net of Tax Amount</b>	<b>\$ 174</b>	<b>\$ —</b>	<b>\$ 174</b>	<b>\$ —</b>

**Note 5 – Advances from Federal Home Loan Bank**

In December 2007, the Bank refinanced \$25,000,000 of advances from the Federal Home Loan Bank, which had a weighted average interest rate of 5.87%. The refinancing was funded with new advances totaling \$30,000,000, which have a weighted average interest rate of 3.84%. The transaction resulted in a prepayment penalty of approximately \$1.5 million which is reflected in other expenses in the nine month period ending March 31, 2008.

**Note 6 – Employee Pension Plan**

The Bank terminated its defined benefit Pension Plan effective January 20, 2008. All obligations to plan participants were paid in full on March 31, 2008 through lump sum distributions. Pension expense related to the termination of \$269,000 was included in salaries and employee benefit expenses for the quarter ended March 31, 2008. In addition, the FASB Statement (“SFAS”) No. 158 accounting adjustment related to the pension plan was reversed which resulted in a decrease in other liabilities of \$260,000 and an increase to comprehensive income of \$174,000, net of an \$89,000 deferred tax adjustment.

**Note 7 – Recent Accounting Pronouncements**

In September 2006, the FASB issued SFAS No. 157, “Fair Value Measurements,” which defines fair value, establishes a framework for measuring fair value under GAAP, and expands disclosures about fair

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value measurements. FASB Statement No. 157 applies to other accounting pronouncements that require or permit fair value measurements. The new guidance is effective for financial statements issued for fiscal years beginning after November 15, 2007, and for interim periods within those fiscal years. The Bank is evaluating the impact, if any, of the adoption of SFAS No. 157 on its consolidated financial position and results of operations.

In February 2008, the FASB issued proposed FASB Staff Position (FSP) 157-2, "Effective Date of FASB Statement No. 157," that permits a one-year deferral in applying the measurement of Statement No. 157 to non-financial assets and non-financial liabilities (non-financial items) that are not recognized or disclosed at fair value in an entity's financial statements on a recurring basis (at least annually). Therefore, if the change in fair value of a non-financial item is not required to be recognized or disclosed in the financial statements on an annual basis or more frequently, the effective date of application of Statement 157 to that item is deferred until fiscal years beginning after November 15, 2008 and interim periods within those fiscal years. The Bank is currently evaluating the impact, if any, that the adoption of FSP 157-2 will have on the Bank's operating income or net earnings.

In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities - Including an Amendment of FASB Statement No. 115." SFAS No. 159 permits entities to choose to measure many financial instruments and certain other items at fair value. Unrealized gains and losses on items for which the fair value option has been elected will be recognized in earnings at each subsequent reporting date. SFAS No. 159 is effective for the Bank July 1, 2008. The Bank is evaluating the impact that the adoption of SFAS No. 159 will have on its consolidated financial statements.

FASB statement No. 141(R) "Business Combinations" was issued in December of 2007. This Statement establishes principles and requirements for how the acquirer of a business recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, and any noncontrolling interest in the acquiree. The Statement also provides guidance for recognizing and measuring the goodwill acquired in the business combination and determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of the business combination. The guidance will become effective as of the beginning of a company's fiscal year beginning after December 15, 2008. This new pronouncement will impact the Bank's accounting for business combinations beginning July 1, 2009.

Staff Accounting Bulletin No. 109 (SAB 109), "Written Loan Commitments Recorded at Fair Value Through Earnings" expresses the views of the staff regarding written loan commitments that are accounted for at fair value through earnings under generally accepted accounting principles. To make the staff's views consistent with current authoritative accounting guidance, the SAB revises and rescinds portions of SAB No. 105 "Application of Accounting Principles to Loan Commitments." Specifically, the SAB revises the SEC staff's views on incorporating expected net future cash flows related to loan servicing activities in the fair value measurement of a written loan commitment. The SAB retains the staff's views on incorporating expected net future cash flows related to internally-developed intangible assets in the fair value measurement of a written loan commitment. The staff expects registrants to apply the views in Question 1 of SAB 109 on a prospective basis to derivative loan commitments issued or modified in fiscal quarters beginning after December 15, 2007. The adoption of SAB 109 did not have a material impact on the consolidated financial statements.

In March 2008, the FASB issued Statement No. 161, "Disclosures about Derivative Instruments and Hedging Activities – an amendment of FASB Statement No. 133" (Statement 161). Statement 161 requires entities that utilize derivative instruments to provide qualitative disclosures about their objectives and strategies for using such instruments, as well as any details of credit-risk-related contingent features





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contained within derivatives. Statement 161 also requires entities to disclose additional information about the amounts and location of derivatives located within the financial statements, how the provisions of SFAS 133 has been applied, and the impact that hedges have on an entity's financial position, financial performance, and cash flows. Statement 161 is effective for fiscal years and interim periods beginning after November 15, 2008 with early application encouraged. The Bank is currently evaluating the potential impact the new pronouncement will have on its consolidated financial statements.

In February 2008, the FASB issued a FASB Staff Position (FSP) FAS 140-3, "Accounting for Transfers of Financial Assets and Repurchase Financing Transaction." This FSP addresses the issue of whether or not these transactions should be viewed as two separate transactions or as one "linked" transaction. The FSP includes a "rebuttable presumption" that presumes linkage of the two transactions unless the presumption can be overcome by meeting certain criteria. The FSP will be effective for fiscal years beginning after November 15, 2008 and will apply only to original transfers made after that date; early adoption will not be allowed. The Bank is currently evaluating the potential impact the new pronouncement will have on its consolidated financial statements.

### ITEM 2 -MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Throughout this Form 10-Q, the terms "we", "us" or "our" refer to William Penn Bancorp, Inc. or William Penn Bank, FSB, or both, as the context indicates. We also refer to William Penn Bank, FSB as "the Bank" and to William Penn Bancorp, Inc. as "the Registrant" or "the Company."

#### Forward-Looking Statements

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

- statements of our goals, intentions and expectations;
- statements regarding our business plans, prospects, growth and operating strategies;
- statements regarding the quality of our loan and investment portfolios; and
- estimates of our risks and future costs and benefits.

These forward-looking statements are subject to significant risks and uncertainties. Actual results may differ materially from those contemplated by the forward-looking statements due to, among others, the following factors:

- general economic conditions, either nationally or in our market area, that are worse than expected;

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- changes in the interest rate environment that reduce our interest margins or reduce the fair value of financial instruments;
- our ability to enter into new markets and/or expand product offerings successfully and take advantage of growth opportunities;
- increased competitive pressures among financial services companies;

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- changes in consumer spending, borrowing and savings habits;
- legislative or regulatory changes that adversely affect our business;
- adverse changes in the securities markets;
- our ability to successfully manage our growth; and
- changes in accounting policies and practices, as may be adopted by the bank regulatory agencies, the Financial Accounting Standards Board or the Public Company Accounting Oversight Board.

Any of the forward-looking statements that we make in this Form 10-Q and in other public statements we make may turn out to be wrong because of inaccurate assumptions we might make, because of the factors illustrated above or because of other factors that we cannot foresee. Consequently, no forward-looking statement can be guaranteed.

### Overview

This discussion and analysis reflects William Penn Bank's consolidated financial statements and other relevant statistical data and is intended to enhance your understanding of our financial condition and results of operations. You should read the information in this section in conjunction with William Penn Bank's unaudited consolidated financial statements and accompanying notes thereto included in this Form 10-Q.

Our primary business is attracting retail deposits from the general public and using those deposits, together with funds generated from operations, principal repayments on securities and loans, and borrowed funds, for our lending and investing activities. Our results of operations depend mainly on our net interest income, which is the difference between the interest income earned on our loan and investment portfolios and interest expense paid on our deposits and borrowed funds. Net interest income is a function of the average balances of loans and investments versus deposits and borrowed funds outstanding in any one period and the yields earned on those loans and investments and the cost of those deposits and borrowed funds.

### Anticipated Loss for the Fiscal Year Ending June 30, 2008

We incurred a prepayment penalty during the quarter ended December 31, 2007 of \$1.5 million in connection with the refinancing of our Federal Home Loan Bank borrowings. The after-tax expense related to the penalty is approximately \$1.0 million. We also had an additional expense of \$269,000 in the quarter ending March 31, 2008 in connection with the termination of our defined benefit pension plan effective on January 20, 2008. We will also have a significant expense related to the establishment of a charitable foundation in connection with the initial public offering of William Penn Bancorp, Inc. In April 2008, we contributed to the foundation approximately 2% of the total outstanding shares of William Penn Bancorp common stock and \$150,000 in cash. This contribution of shares and cash will have an adverse effect on our net income in the fourth quarter and for the year. The after-tax expense of the contribution will reduce net income in our 2008 fiscal year by approximately \$636,000.

The combination of these expenses (the prepayment penalty on FHLB advances, the cost of terminating the Pension Plan and the expense of the contribution to the charitable foundation) is expected to result in our incurring a net loss for the fiscal year ending June 30, 2008.

### **Anticipated Increase in Operating Expenses**

Our results of operations are significantly affected by other expenses, which include salaries and benefits expense, occupancy and equipment expense and other general and administrative expenses such as data processing, professional fees and marketing/advertising costs.

After the stock offering, additional annual employee compensation and benefit expenses stemming from the shares granted to employees, officers and directors under new benefit plans will increase this category of expense. We will recognize expense for our employee stock ownership plan when shares are committed to be released to participants' accounts and will recognize expenses for restricted stock awards over the vesting period of awards made to recipients. In addition, we will be required to recognize compensation expense related to stock options outstanding based upon the fair value of such awards at the date of grant over the period that such awards are earned. Our decision to terminate the defined benefit pension plan as of January 2008 was made in order to mitigate benefit costs in anticipation of these stock related compensation expenses.

We also expect that noninterest expense will be higher going forward as a result of the accounting, legal and various other additional noninterest expenses associated with operating as a public company, particularly as a result of the requirements of the Sarbanes-Oxley Act of 2002. We will have public company expenses that we have not had previously such as periodic reporting, annual meetings, retention of a transfer agent and professional fees.

Furthermore, noninterest expense in the future will be impacted by our plan to expand our branch network; we currently intend to open some new offices over approximately the next five years. We also expect higher compensation and benefits expenses going forward as the result of our plans to expand the size of our lending department plus hire additional branch personnel and management staff.

### **Critical Accounting Policies**

Our accounting policies are integral to understanding the results reported and our significant policies are described in Note 2 to our consolidated financial statements included in the Registration Statement of William Penn Bancorp, Inc. on Form S-1, as amended (File No. 333-148219). In preparing the consolidated financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the dates of the consolidated statements of financial condition and revenues and expenses for the periods then ended. Actual results could differ significantly from those estimates. Material estimates that are particularly susceptible to significant change relate to the determination of the allowance for loan losses, the valuation allowance for deferred tax assets and other-than-temporary impairment of securities.

***Allowance for Loan Losses.*** The allowance for loan losses is maintained by management at a level which represents their evaluation of known and inherent losses in the loan portfolio at the consolidated balance sheet date that are both probable and reasonable to estimate. Management's periodic evaluation of the adequacy of the allowance is based on the Bank's past loan loss experience, known and inherent losses in the portfolio, adverse situations that may affect the borrower's ability to repay, the estimated value of any underlying collateral, composition of the loan portfolio, current economic conditions, and other relevant factors. This evaluation is inherently subjective as it requires material estimates that may be susceptible to significant change, including the amounts and timing of future cash flows expected to be received on impaired loans.

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The allowance consists of specific and general components. The specific component relates to loans that are classified as doubtful, substandard, or special mention. For such loans that are also

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classified as impaired, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan. The general component covers nonclassified loans and is based on historical loss experience adjusted for qualitative factors.

Although specific and general loan loss allowances are established in accordance with management's best estimate, actual losses are dependent upon future events and, as such, further provisions for loan losses may be necessary. For example, our evaluation of the allowance includes consideration of current economic conditions, and a change in economic conditions could reduce the ability of our borrowers to make timely repayments of their loans. This could result in increased delinquencies and increased non-performing loans, and thus a need to make increased provisions to the allowance for loan losses, which would require us to record a charge against income during the period the provision is made, resulting in a reduction of our earnings. A change in economic conditions could also adversely affect the value of the properties collateralizing our real estate loans, resulting in increased charge-offs against the allowance and reduced recoveries of loans previously charged-off, and thus a need to make increased provisions to the allowance for loan losses. Furthermore, a change in the composition of our loan portfolio or growth of our loan portfolio could result in the need for additional provisions.

**Other-than-Temporary Investment Security Impairment.** Securities are evaluated periodically to determine whether a decline in their value is other-than-temporary. Management utilizes criteria such as the magnitude and duration of the decline, in addition to the reasons underlying the decline, to determine whether the loss in value is other-than-temporary. The term "other-than-temporary" is not intended to indicate that the decline is permanent, but indicates that the prospect for a near-term recovery of value is not necessarily favorable, or that there is a lack of evidence to support a realizable value equal to or greater than the carrying value of the investment. Once a decline in value is determined to be other-than-temporary, the value of the security is reduced and a corresponding charge to earnings is recognized.

### **Comparison of Financial Condition at March 31, 2008 and June 30, 2007**

Our total assets were \$271.3 million at March 31, 2008, representing a slight increase over \$268.8 million at June 30, 2007, primarily due to a \$5.4 million increase in loans receivable, net to \$185.8 million at March 31, 2008 from \$180.2 million at June 30, 2007. The increase in loans was offset by a \$2.7 million or 4.3% decrease in securities held to maturity to \$59.0 million from \$61.6 million. There was a \$7.3 million increase in deposits to \$166.2 million from \$158.9 million primarily due to \$9.3 million in subscription funds held in escrow pending completion of the Company's stock offering. FHLB borrowings declined to \$66.0 million from \$71.0 million at June 30, 2007 due to the repayment of \$35.0 million in advances, partially offset by \$30.0 million in new advances.

Equity grew by \$508,000 to \$34.6 million at March 31, 2008, from \$34.1 million at June 30, 2007. The increase was the result of the Bank's net income for the period and a \$174,000 adjustment for termination of the defined benefit pension plan, net of deferred income tax benefit of \$89,000.

### **Comparison of Operating Results for the Three and Nine Months Ended March 31, 2008 and 2007**

**General.** Net income for the three months ended March 31, 2008 was \$405,000 compared to net income of \$385,000 for the three months ended March 31, 2007. The increase in net income for the 2008 period was due to higher net interest income which offset an increase in other expenses. For the nine months ended March 31, 2008, net income declined to \$334,000 from \$1.2 million in the prior year primarily due to the FHLB refinancing prepayment penalty.





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**Interest Income.** Total interest income was \$3.9 million for both the three months ended March 31, 2008, and the three months ended March 31, 2007. Interest income on loans receivable was \$2.9 million for the three months ended March 31, 2008 compared to \$2.8 million for the same period in 2007. Interest income on securities and other interest-earning assets declined by \$76,000 to total \$937,000 compared to \$1.0 million in the prior year period.

For the nine months ended March 31, 2008, total interest income increased \$583,000 to \$12.0 million, from \$11.4 million for the nine months ended March 31, 2007. Interest income on loans receivable was \$345,000 higher, at \$8.9 million, for the nine months ended March 31, 2008 compared to \$8.6 million for the same period in 2007. Interest income on securities and other interest-earning assets improved by \$238,000 to total \$3.1 million compared to \$2.8 million in the prior year period.

**Interest Expense.** Total interest expense decreased \$290,000 to \$2.3 million for the three months ended March 31, 2008 as compared to \$2.6 million for the same period in 2007. The decrease resulted primarily from a decrease in deposit expense to \$1.5 million from \$1.6 million in the prior year period. Expense on borrowings was \$808,000 compared to \$988,000 reflecting the repayment of higher rate advances and the maturity of an additional \$5.0 million in advances.

For the nine months ended March 31, 2008, total interest expense increased \$77,000 to \$7.6 million as compared to \$7.5 million for the same period in 2007. The increase resulted primarily from a \$199,000 increase in deposit expense to \$4.8 million from \$4.6 million. Expense on borrowings was \$2.8 million compared to \$2.9 million in the prior year.

It has been the Bank's practice consistently to offer deposit rates toward the high end of current market ranges. The Bank expects to have lower borrowing expense going forward as a result of the refinancing of certain of the Bank's FHLB advances during the quarter ending December 31, 2007, as discussed above.

**Net Interest Income.** For the three months ended March 31, 2008, the Bank's interest rate spread and net interest margin were 1.88% and 2.41%, respectively, compared to 1.37% and 1.99%, respectively, for the three months ended March 31, 2007. The interest rate spread and net interest margin for the nine months ended March 31, 2008 were 1.64% and 2.23%, respectively, as compared to 1.42% and 2.03%, respectively, for the nine months ended March 31, 2007. The improvement in spread and margin for the three months ended March 31, 2008 was attributable to a decline of 56 basis points in the average cost of interest-bearing liabilities which offset a 5 basis point decline in yields on interest-earning assets. For the nine months ended March 31, 2008, our spread and margin benefited from both a 14 basis point gain in yield on interest-earning assets and an 8 basis point decline in the average cost of interest-bearing liabilities. Average interest-earning assets rose to \$263.5 million and \$263.9 million, respectively, for the three and nine months ended March 31, 2008 as compared to \$260.9 million and \$257.0 million, respectively, for the comparable 2007 periods. Average interest-bearing liabilities were \$228.4 million for both the three and nine months ended March 31, 2008 compared to \$225.6 million and \$222.3 million, respectively, for the comparable 2007 periods.

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The following table sets forth certain information with respect to the Bank's interest-earning assets and interest-bearing liabilities for the three and nine months ended March 31, 2008 and 2007. The average yields and costs are derived by dividing income or expense by the average balance of assets or liabilities, respectively, for the periods presented. Average balances are derived from month end balances. Management does not believe that the use of month end balances rather than daily balances has caused any material differences in the information presented.

	For the Three Months Ended March 31,						For the Nine Months Ended March 31,					
	2008			2007			2008			2007		
	Average Balance	Average Yield/ Interest Cost	Average Yield/ Cost	Average Balance	Interest (1)	Average Yield/ Cost	Average Balance	Interest (1)	Average Yield/ Cost	Average Balance	Interest (1)	Average Yield/ Cost
(Dollars in thousands)												
<b>Interest-earning assets:</b>												
Net loans receivable (3)	\$186,119	\$2,920	6.28%	\$181,094	\$2,837	6.27%	\$183,777	\$8,913	6.47%	\$180,970	\$8,568	6.31%
Securities (2)	57,521	705	4.90%	60,012	707	4.71%	60,310	2,383	5.27%	60,605	2,152	4.73%
Other interest-earning assets	19,830	232	4.68%	19,776	313	6.33%	19,853	693	4.65%	19,435	686	5.93%
Total interest-earning assets	263,470	3,857	5.86%	260,882	3,857	5.91%	263,940	11,989	6.05%	261,010	11,406	5.92%
Non-interest earning assets	5,115			4,110			4,695			3,857		
Total Assets	\$268,585			\$264,992			\$268,635			\$260,867		
<b>Interest-bearing liabilities:</b>												
NOW accounts	\$12,585	43	1.37%	\$12,846	47	1.46%	\$12,545	136	1.45%	\$12,188	142	1.44%
Money Market Accounts	37,960	303	3.19%	35,281	371	4.21%	38,090	1,099	3.85%	37,021	1,036	4.06%
Savings and Club accounts	15,288	72	1.88%	13,667	99	2.90%	14,162	273	2.57%	13,652	280	2.73%
Certificates of deposit	94,054	1,044	4.44%	92,768	1,055	4.55%	93,625	3,275	4.66%	94,457	3,126	4.46%
Total Deposits	159,887	1,462	3.66%	154,562	1,572	4.07%	158,422	4,783	4.05%	154,318	4,584	3.96%
Federal Home Loan Bank Advances	68,500	808	4.72%	71,000	988	5.57%	70,000	2,790	5.36%	71,000	2,912	5.71%
Total interest-bearing liabilities	228,387	2,270	3.98%	225,562	2,560	4.54%	228,422	7,573	4.22%	227,318	7,496	4.50%
Non-interest-bearing deposits	1,603			1,618			1,595			1,431		
Non-interest-bearing liabilities	4,377			4,089			4,314			3,871		
Total Liabilities	234,367			231,269			234,331			227,620		
Equity	34,218			33,723			34,304			33,247		
Total Liabilities and Equity	\$268,585			\$264,992			\$268,635			\$260,867		
Net interest income		\$1,587			\$1,297			\$4,416			\$3,910	
Interest rate spread			1.88%			1.37%			1.64%			1.42%
Net interest margin			2.41%			1.99%			2.23%			2.03%
Ratio of average interest-earning assets to average interest-bearing liabilities	115.36	%		115.66	%		115.55	%		115.60	%	

(1) Includes loan fee income.

(2) Average rates on securities are calculated on average costs.

(3) Loans outstanding include non-accrual loans.



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**Provision for Loan Losses.** We charge to operations provisions for loan losses at a level required to reflect credit losses in the loan portfolio that are both probable and reasonable to estimate. Management, in determining the allowance for loan losses, considers the losses inherent in the loan portfolio and changes in the nature and volume of our loan activities, along with general economic and real estate market conditions. We utilize a two-tier approach: (1) identification of impaired loans and establishment of specific loss allowances on such loans; and (2) establishment of general valuation allowances on the remainder of our loan portfolio. We establish a specific loan loss allowance for an impaired loan based on delinquency status, size of loan, type of collateral and/or appraisal of the underlying collateral and financial condition of the borrower. We base general loan loss allowances upon a combination of factors including, but not limited to, actual loan loss experience, composition of the loan portfolio, current economic conditions and management's judgment.

There was no provision for loan losses made during the three months ended March 31, 2008 compared to \$35,000 in the three months ended March 31, 2007. For the nine months ended March 31, 2008 the provision totaled \$20,000 compared to \$116,000 for the prior year period. Non-performing loans were 1.25% of total loans at March 31, 2008, as compared to 1.13% of total loans at June 30, 2007. The increase in non-performing loans between June 30, 2007 and March 31, 2008 is attributable to the balance of four loans which became non-performing between those dates. Management believes that the allowance for loan and lease losses is sufficient given the status of the loan portfolio at this time.

**Noninterest Income.** Noninterest income was \$66,000 for the three months ended March 31, 2008 compared to \$62,000 for same period in 2007. The increase was due to a \$4,000 increase in service fees and the loss of \$1,000 on securities sales during the prior year.

For the nine months ended March 31, 2008, noninterest income was \$198,000 compared to \$210,000 for same period in 2007 caused by a \$13,000 decline in other income. Other noninterest income was \$101,000 and \$114,000 for the nine months ended March 31, 2008 and 2007, respectively.

Traditionally, noninterest income has not been a significant area of our operations as we have not in the past focused on fee generation. We hold the bulk of our securities portfolio as held to maturity so gains or losses on the sales of securities is not expected to be a large item in noninterest income. We currently have no plans to seek fee income generation through the offering of complementary services or acquisition of fee producing subsidiaries such as title insurance or third-party securities sales. We do not at present hold any bank owned life insurance.

**Noninterest Expense.** Noninterest expense was significantly impacted during the three months ended March 31, 2008 by \$269,000 in expenses included in salaries and employee benefits expense relating to the termination of the defined benefit pension plan. Noninterest expense for the three months ended March 31, 2008 was \$1.0 million compared to \$741,000 for the same period in 2007. Without the termination expense, noninterest expense would have been approximately \$777,000 for the 2008 period. All components of noninterest expense were higher in the 2007 period.

For the nine months ended March 31, 2008, noninterest expense was \$4.1 million compared to \$2.2 million for the same period in 2007. The 2008 period was significantly impacted by the \$1.5 million prepayment penalty for refinancing FHLB advances and the expense related to the defined benefit plan termination discussed above. Without the penalty, noninterest expense would have been \$2.6 million for the 2008 period. Salaries and employee benefits expense increased by \$283,000 for the 2008 period primarily due to the expense resulting from the termination of the pension plan. Occupancy and equipment expense and other noninterest expense rose by \$39,000 and \$54,000, respectively. The increase in occupancy and equipment was due to landscaping tree removal and paving repairs. Other



noninterest expenses increased primarily due to write-offs related to the Bank's investment in a low-income housing project.

**Provision for Income Taxes.** For the three and nine months ended March 31, 2008 income tax expense was \$202,000 and \$147,000, respectively, as compared to income tax expense of \$198,000 and \$556,000, respectively, for the same periods in 2007. The Bank's effective tax rates for the three and nine months ended March 31, 2008 were 33.3% and 30.6%, respectively, compared to 34.0% and 31.0%, respectively, for the three and nine months ended March 31, 2007.

### **Liquidity, Commitments and Capital Resources**

The Bank must be capable of meeting its customer obligations at all times. Potential liquidity demands include funding loan commitments, cash withdrawals from deposit accounts and other funding needs as they present themselves. Accordingly, liquidity is measured by our ability to have sufficient cash reserves on hand, at a reasonable cost and/or with minimum losses.

The Asset and Liability Management Committee and the Board of Directors sets limits and controls to guide senior management's managing of our overall liquidity position and risk. The Board of Directors and its Committee, along with senior management, are responsible for ensuring that our liquidity needs are being met on both a daily and long term basis.

Our approach to managing day-to-day liquidity is measured through our daily calculation of investable funds and/or borrowing needs to ensure adequate liquidity. In addition, we constantly evaluate our short-term and long-term liquidity risk and strategy based on current market conditions, outside investment and/or borrowing opportunities, short and long-term economic trends, and anticipated short and long-term liquidity requirements. The Bank's loan and deposit rates may be adjusted as another means of managing short and long-term liquidity needs. We do not at present participate in derivatives or other types of hedging instruments to meet liquidity demands.

At March 31, 2008, the total approved loan origination commitments outstanding amounted to \$6.3 million. At that date, construction loans in process were \$8.5 million. Certificates of deposit scheduled to mature in one year or less at March 31, 2008, totaled \$60.9 million. Based on the competitive rates and on historical experience, management believes that a significant portion of maturing deposits will remain with the Bank. At March 31, 2008, we had an unused borrowing capacity of \$123.8 million from the Federal Home Loan Bank of Pittsburgh which we may use as a funding source to meet commitments and for liquidity purposes.

### **Regulatory Capital Compliance**

Consistent with its goals to operate a sound and profitable financial organization, the Bank actively seeks to maintain its status as a well-capitalized institution in accordance with regulatory standards. As of March 31, 2008, the Bank exceeded all applicable regulatory capital requirements and was well capitalized. As of March 31, 2008, our regulatory capital amounts and ratios were as follows:





	<b>Actual Amount (Dollars in thousands)</b>	<b>Ratio</b>
Total risk-based capital	\$ 36,035	24.30%
Core Capital (to risk-weighted assets)	\$ 34,566	23.30%
Core Capital (adjusted total assets)	\$ 34,566	12.75%
Tangible Capital (to adjusted total assets)	\$ 34,566	12.75%

### **Off-Balance Sheet Arrangements**

We are a party to financial instruments with off-balance-sheet risk in the normal course of our business of investing in loans and securities as well as in the normal course of maintaining and improving William Penn Bank's facilities. These financial instruments include significant purchase commitments, such as commitments related to capital expenditure plans and commitments to purchase investment securities or mortgage-backed securities, and commitments to extend credit to meet the financing needs of our customers. At March 31, 2008, we had no significant off-balance sheet commitments other than commitments to extend credit.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Our exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit is represented by the contractual amount of those instruments. We use the same credit policies in making commitments and conditional obligations as we do for on-balance-sheet instruments. Since a number of commitments typically expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements.

### **Impact of Inflation and Changing Prices**

The financial statements, accompanying notes, and related financial data of William Penn Bank, FSB presented herein have been prepared in accordance with generally accepted accounting principles in the United States, which require the measurement of financial position and operating results in terms of historical dollars without considering the changes in purchasing power of money over time due to inflation. The primary impact of inflation is reflected in the increased cost of operations. Most of our assets and liabilities are monetary in nature, therefore, interest rates generally have a more significant impact on our performance than do general levels of inflation.

### **ITEM 3 – QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

As a "smaller reporting company" as defined by Item 10 of Regulation S-K, the Company is not required to provide the information required by this item.



**ITEM 4T – CONTROLS AND PROCEDURES**

An evaluation was performed under the supervision, and with the participation of management, including the principal executive and financial officer, of the effectiveness of the design and operation of the disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) promulgated under the Securities Exchange Act of 1934, as amended) as of March 31, 2008. Based on such evaluation, the principal executive and financial officer has concluded that the disclosure controls and procedures are effective as of March 31, 2008.

No change in the internal controls over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) promulgated under the Securities Exchange Act of 1934, as amended) occurred during the most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the internal control over financial reporting.

**PART II – OTHER INFORMATION**

**ITEM 1 – LEGAL PROCEEDINGS**

There were no material pending legal proceedings at March 31, 2008 to which the Company or its subsidiaries is a party other than ordinary routine litigation incidental to their respective businesses.

**ITEM 1A – RISK FACTORS**

As a “smaller reporting company” as defined by Item 10 of Regulation S-K, the Company is not required to provide the information required by this item.

**ITEM 2 – UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

(a) On April 15, 2008, the Registrant issued 2,548,713 shares of its common stock to William Penn, MHC in exchange for all of the outstanding shares of capital stock of William Penn Bank, FSB in a transaction that was exempt from registration under Section 4(2) of the Securities Act of 1933.

(b) On February 11, 2008, the Securities and Exchange Commission declared the registrant’s Registration Statement on Form S-1 (Commission File No. 333-148219) effective. The Registration Statement covered the sale by the registrant of up to 1,586,655 shares of its common stock, \$.10 par value, in connection with the mutual holding company reorganization of William Penn Bank, FSB (the “Bank”). The subscription offering was commenced on February 21, 2008 and terminated on March 17, 2008. The Reorganization was approved by the Bank’s members at a special meeting held on March 25, 2008. The Reorganization was completed on April 15, 2008 with 1,025,283 shares sold to the public (including 87,384 shares purchased by the Bank’s Employee Stock Ownership Plan with funds borrowed from the registrant) at \$10.00 per

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share for aggregate gross proceeds of \$10,252,830. In addition, the registrant contributed 67,022 shares to the William Penn Bank Community Foundation. As of the date hereof, the registrant has incurred approximately \$607,000 in expenses in the offering (including approximately \$200,000 in fees and reimbursable expenses paid to Keefe, Bruyette & Woods, Inc. for its services as marketing agent) for estimated net proceeds of approximately \$9.6 million. The registrant used approximately 50% of the net proceeds to acquire all of the shares of capital stock to be issued by the Bank in connection with the Reorganization and used \$873,840 to fund a loan to its Employee Stock Ownership Plan. The registrant retained the remainder of the net proceeds for ongoing expenses. All payments of proceeds or expenses were made to persons other than directors, officers, general partners of

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the registrant or their associates, persons owning 10% or more of any class of securities of the registrant or affiliates of the registrant.

(c) Not applicable.

### ITEM 3 – DEFAULTS UPON SENIOR SECURITIES

None

### ITEM 4 – SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None

### ITEM 5 – OTHER INFORMATION

None

### ITEM 6 – EXHIBITS

- 3(i) Charter of William Penn Bancorp, Inc. \*
- 3(ii) Bylaws of William Penn Bancorp, Inc. \*
- 4.1 Specimen Stock Certificate of William Penn Bancorp, Inc. \*
- 10.1 Directors Consultation and Retirement Plan \*
- 10.2 Deferred Compensation Plan for Directors \*
- 10.3 Restated Deferred Compensation Plan \*
- 31 Rule 13a-14(a)/15d-14(a) Certification
- 32 Section 1350 Certification

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\* Incorporated by reference from the Registrant's Registration Statement on Form S-1 (File No. 333-148219)

**SIGNATURES**

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

**WILLIAM PENN BANCORP, INC.**

(Registrant)

/s/ Charles Corcoran  
Charles Corcoran, President

(Duly authorized officer and principal  
financial officer)

Date: May 15, 2008