

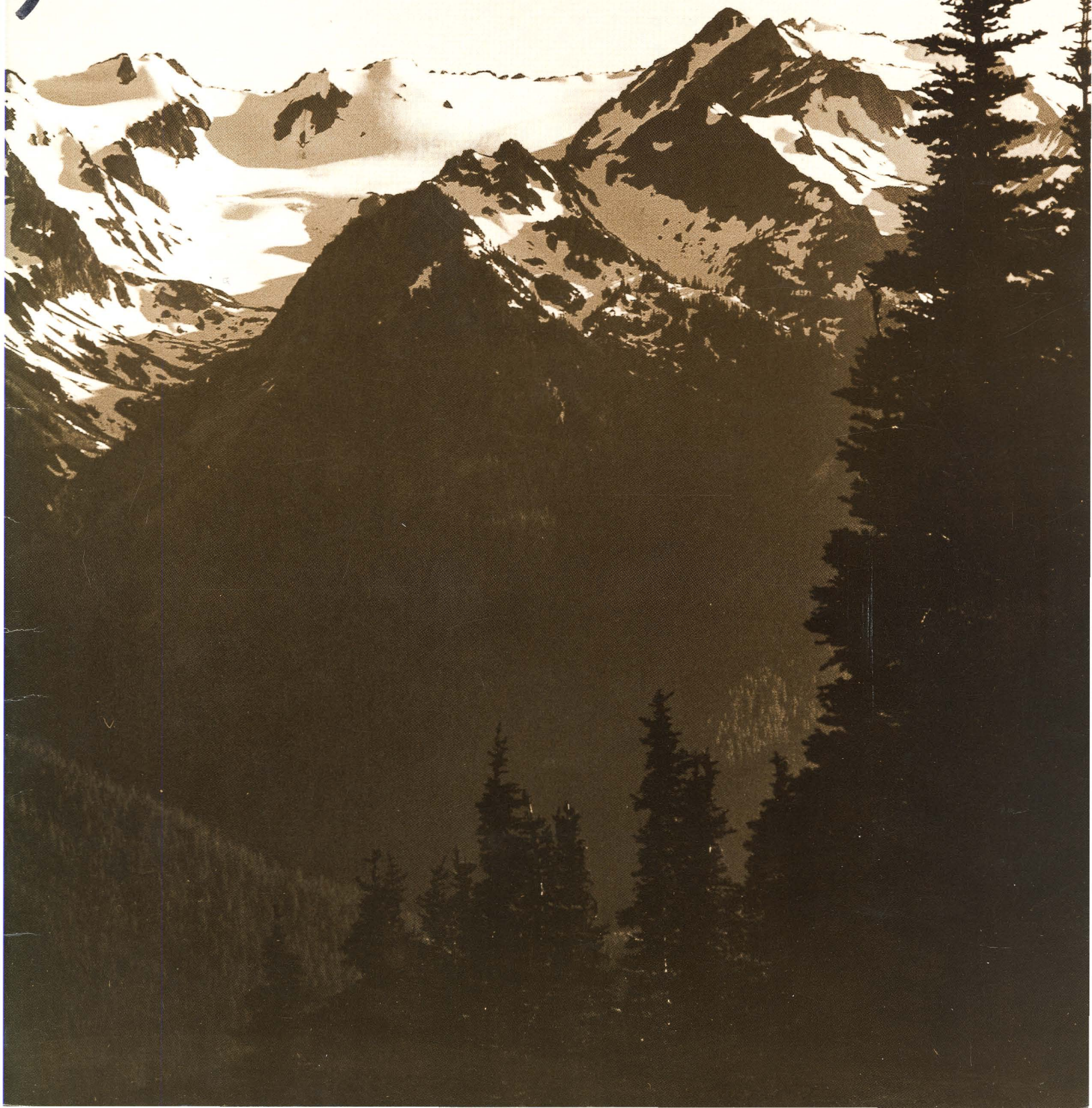
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Summit Savings Association and Subsidiaries

Annual Report 1989

Annual Report
STACK

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Financial Highlights

At June 30,		1989	1988	1987	
	Total Assets	\$109,970,398	\$98,394,287	\$82,400,611	
	Loans Receivable and Mortgage Backed Securities	79,788,307	84,543,443	68,322,825	
	Deposits	80,266,824	69,531,080	68,077,766	
	Advances from the Federal Home Loan Bank . .	9,600,000	6,600,000	7,843,750	
	Shareholders' Equity	2,915,320	4,067,216	3,642,521	
	Book Value Per Share	4.66	6.50	5.82	
	Regulatory Capital to Assets	3.42%	4.85%	5.06%	
For the Year Ended June 30:	Weighted Average Yield:	Loans and Mortgage Backed Securities	10.58%	9.50%	9.53%
		Cash and Investments	8.29	6.85	6.40
		Combined	10.33	9.28	9.22
	Weighted Average Cost of Funds:	Deposits	8.17	7.28	7.14
		Borrowings	9.93	8.48	8.96
		Combined	8.59	7.49	7.29
		Interest Rate Margin	1.74	1.79	1.93
	Net Income (Loss) ⁽¹⁾		\$ (1,151,896)	\$ 424,695	\$ (122,369)
	Earnings (Loss) per Share				
	Net Income (Loss) before Accounting Change		(1.84)	.38	(.20)
	Cumulative Effect of Accounting Change30	
	Net Income (Loss)		(1.84)	.68	(.20)
Real Estate Loans Originated		40,801,405	74,669,282	94,401,716	
Return on Average Assets . . .		(1.11)%	.47%	(.15)%	
Return on Average Shareholders' Equity		(32.99)	11.02	(3.31)	

⁽¹⁾In 1988, the Association adopted FAS 96 "Accounting for Income Taxes" effective July 1, 1987. The cumulative effect of this adoption was a federal income tax benefit of \$190,000.

Summit Savings Association and Subsidiaries

Board of Directors



Back Row – Left to Right
William P. Newman, John D. Cadigan,
William P. Hurme, Doug T. Mergenthaler,
Paul E. Nolan

Front Row – Left to Right
James D. Huber, James F. Grabicki

Not Pictured – Norman D. Winton

Letter to Shareholders



Dear Shareholders:

On March 1, 1989, the Board of Directors appointed me President and Chief Executive Officer of Summit Savings, with the charge of returning the Association to operating profitability. I am confident that we will be successful in achieving that goal. Summit Savings is blessed with a dedicated Board, an excellent management team, and a very capable and professional staff. We are located in a prosperous and growing market which shows every sign of continued prosperity and growth.

Fiscal 1989 was a difficult year for Summit. The Association recorded a loss of \$1,151,896, or \$1.84 per share, primarily the result of additional loss provisions totaling \$1,249,485, and \$49,385 of expenses required to maintain foreclosed and other problem properties. Capital, which is currently the subject of much discussion in our industry, fell to \$2,915,320 or 2.65% of total assets, as measured by Generally Accepted Accounting Principles (GAAP), at fiscal year end. Loan production was \$40,801,405 as compared to \$74,669,282 in fiscal 1988.

We look forward to significantly improving these numbers in fiscal 1990. A prerequisite to our return to profitability lies in our ability to reduce non-earning assets, primarily real estate owned as a result of foreclosures, which are disproportionately high. As we are successful in returning these assets to an earning status, we will enjoy not only the benefit of increased interest income but also a reduction of the very high cost of carrying these problem assets. Equally critical is the addition of equity capital through a stock offering which, as of the date of this writing, has not yet been completed. We plan to raise approximately \$5,000,000 of new capital in the offering, which will satisfy new regulatory requirements and allow us to grow. An additional benefit of the capital increase is restoration of faith in the strength and stability of Summit Savings by the public.

There are numerous other challenges which must be addressed as we are working toward strengthening capital adequacy and asset quality. These include improvement of the net interest margin, increasing our loan servicing portfolio, the addition of consumer lending to our array of loan services, and further lowering of fixed overhead expenses through increased efficiency. To meet these challenges, we are taking a number of measures within a general strategy of focusing on residential real estate lending which offers acceptable levels of risk and needed liquidity.

Gary Wilson joined us in April as Senior Vice President and Chief Lending Officer. Gary's mission is to develop and implement a plan which will result in Summit Savings being a premier mortgage lender in the markets we serve. He has assembled a team which is knowledgeable and experienced in our markets and we have developed products which the customers in those markets want and need. Progress to date gives every indication that our ambitious production goals this year will be met.

I am proud to have the opportunity to work with the entire senior management group at Summit Savings. All are well qualified for their positions and dedicated to the goal of being recognized by our peers and customers as being the best at what we do.

I am also proud to be associated with our Board of Directors. Without exception, they are also committed to our success. I will take this opportunity to introduce John Cadigan as our newest member of the Board. John brings to us a wealth of experience and expertise as a successful manager, accountant and investor.

Fiscal 1990 promises to be a year of continued change for Summit Savings Association in particular and for our industry in general. I am confident we will successfully manage those changes and that, with a lot of hard work, we will be able to add significantly to the value of the shares you own in our company.

Sincerely,

A handwritten signature in orange ink that reads "James F. Grabicki". The signature is fluid and cursive, with a long horizontal stroke at the end.

James F. Grabicki

Summit Savings Association and Subsidiaries

Table of Contents

Management's Discussion and Analysis of Financial Condition and Results of Operations	5
Report of Ernst & Whinney, Independent Auditors	12
Consolidated Statements of Financial Condition	13
Consolidated Statements of Shareholders' Equity	14
Consolidated Statements of Operations	14
Consolidated Statement of Cash Flows	16
Consolidated Statements of Changes in Financial Position	17
Notes to Consolidated Financial Statements	19
Corporate Information	31



Management's Discussion and Analysis of Financial Condition and Results of Operations

Description of Business

Summit Savings is a Washington chartered stock savings and loan association, established in 1981 and located in Bellevue, Washington. The Association's primary market is the Puget Sound area. The Association has two wholly owned subsidiaries. Life insurance and annuities are sold through its subsidiary, Summit Services, Inc. In June 1988, a finance subsidiary, Summit Capital Corporation, was formed to issue collateralized mortgage obligations.

In December 1988, former President Dale Harrison resigned and in March 1989, James F. Grabicki was appointed by the Board of Directors as President and Chief Executive Officer of the Association. Under the new management, the Association is increasing capital through the issuance of stock, attempting to decrease non-performing loans and real estate owned, and refocusing the business of the Association toward residential lending and retail deposits. In addition, management is reviewing pricing and operations in order to enhance income and control costs. Asset and liability management policy is being updated to integrate new regulatory pronouncements and to monitor and manage asset quality, asset credit and interest rate risk.

Financial Condition

Assets

Total assets of the Association increased to \$110.0 million at June 30, 1989 compared to \$98.4 million at June 30, 1988, primarily as a result of a \$15.8 million increase in cash, interest-bearing deposits and investment securities. This increase was partially offset by a \$4.8 million decrease in mortgage backed securities and loans receivable.

The increase in cash and investments will provide funds for the anticipated increase in loan production in fiscal 1990 and provide adequate liquidity. The funds are currently invested in U.S. Treasury and Agency Securities, bankers' acceptances, certificates of deposit and corporate notes and bonds.

Real estate owned increased \$718,000 due to transfers from loans receivable and capitalized improvements totaling \$2.1 million, offset by real estate sold of \$580,000 and an increase of \$846,000 in the allowance for estimated losses on real estate owned. The allowance for estimated losses was increased from \$174,000 to \$1.1 million by a provision for losses on real estate owned of \$927,000, reduced by losses on real estate owned of \$81,000.

The \$4.8 million decrease in loans receivable and mortgage backed securities is attributable primarily to new loan production and construction loan disbursements of \$53.0 million, offset by principal repayments of \$37.1 million, loans sold of \$17.9 million and loans transferred to real estate owned of \$2.1 million. The allowance for loan losses was decreased from \$752,000 to \$375,000 due to losses of \$700,000 being charged off, offset by an additional provision for losses on loans of \$323,000.

Management's Discussion and Analysis of Financial Condition and Results of Operations

Financial Condition (continued)	Liabilities and Retained Earnings	<p>————— Total liabilities increased \$12.7 million from \$94.3 million at June 30, 1988 to \$107.0 million at June 30, 1989. The increase was due primarily to increases of \$10.7 million in deposits and \$3.0 million in advances from the Federal Home Loan Bank. Retained earnings decreased \$1.2 million, which reflected the net loss for fiscal 1989.</p>
Results of Operations	General	<p>————— The Association recorded a net loss of \$1.2 million for the year ended June 30, 1989 compared to net income of \$425,000 for the year ended June 30, 1988, and a net loss of \$122,000 for the year ended June 30, 1987. Net losses in fiscal 1989 and 1987 resulted primarily from additions to the provisions for losses on loans and real estate owned of \$1.2 million in fiscal 1989 and \$1.1 million in fiscal 1987. The operating results for fiscal 1988 were favorably affected by a gain of \$398,000 on the sale of a parcel of real estate acquired in exchange for a loan receivable which offset additions to the provisions for losses on loans and real estate owned of \$230,000 and by a change in the method of accounting for income taxes. See Note J of the Notes to the Consolidated Financial Statements.</p>
	Interest Income and Expense	<p>————— Interest income from mortgage backed securities and loans receivable increased \$1.7 million, or 21.5%, in fiscal 1989 compared to fiscal 1988, and \$883,000, or 12.8%, in fiscal 1988 compared to fiscal 1987. The increase in 1989 was due to an increase of \$7.5 million, or 9.2%, in average balances and an increase from 9.5% to 10.6% in average interest yield in fiscal 1989 compared to fiscal 1988. The increase in yield reflects generally rising interest rates and an increase in higher yielding construction lending during the period. The increase in fiscal 1988 was due to an increase of \$9.5 million, or 13.2%, in average balances, while the average interest yield was 9.5% during both fiscal 1988 and 1987.</p> <p>————— Interest income from cash, interest-bearing deposits and investment securities increased \$371,000, or 72.3%, in fiscal 1989 compared to fiscal 1988, and \$5,000, or 1.0%, in fiscal 1988 compared to fiscal 1987. The increase in fiscal 1989 was due to an increase of \$3.2 million, or 42.4%, in average balances during fiscal 1989 and an increase from 6.9% to 8.3% in average interest rates earned in fiscal 1989 compared to fiscal 1988. The slight increase in fiscal 1988 was due to relatively stable average balances and interest yields in fiscal 1988 and 1987. Yields on cash, interest-bearing deposits and investment securities are calculated on average balances which include non-interest earning cash, consistent with the Federal Home Loan Bank method of calculating yields.</p>

Management's Discussion and Analysis of Financial Condition and Results of Operations



Results of Operations

Interest Income and Expense (continued)

Deposit interest expense increased \$919,000, or 17.5%, in fiscal 1989 compared to fiscal 1988 and \$71,000, or 1.4%, in fiscal 1988 compared to fiscal 1987 because of the reliance on short-term deposits which are interest rate sensitive. The increase in fiscal 1989 was due to a \$3.4 million, or 4.7%, increase in average balances during fiscal 1989 and an increase in average interest rates paid from 7.3% in fiscal 1988 to 8.2% in fiscal 1989. In fiscal 1988 average balances decreased \$493,000, or .7%, over fiscal 1987 and average interest rates paid increased from 7.1% in fiscal 1987 to 7.3% in fiscal 1988.

Interest on borrowings increased \$1.1 million, or 84.9%, in fiscal 1989 compared to fiscal 1988 and \$649,000, or 107.7%, in fiscal 1988 compared to fiscal 1987. The 1989 increase was due to an increase in average borrowings of \$8.6 million, or 58.2%, and an increase in average interest rates paid from 8.5% in 1988 to 9.9% in 1989. The increase in fiscal 1988 over fiscal 1987 was due to an \$8.0 million, or 119.6%, increase in average borrowings, offset by a decrease in average interest rates from 9.0% in fiscal 1987 to 8.5% in fiscal 1988.

During the three years ended June 30, 1989, there was a change in the liability structure of the Association. Certificates of deposit were 90.1%, 82.9% and 74.7% of total deposits at June 30, 1989, 1988 and 1987, respectively. In order to reduce its regulatory net worth requirement and to fund asset growth, in June 1988 the Association used its mortgage backed securities as collateral for the issuance of a collateralized mortgage obligation. As a result of these changes, the Association has experienced an increase in interest expense in addition to that caused by gradually rising interest rates during the period.

Net interest income before provision for loan losses increased \$56,000, or 3.2%, in fiscal 1989 compared to fiscal 1988 and \$169,000, or 10.5%, in fiscal 1988 compared to fiscal 1987. The rate of increase has been affected by the ratio of average interest-earning assets to average interest-bearing liabilities, which was 98.5%, 99.9% and 93.4% in fiscal 1989, 1988 and 1987, respectively. The interest rate margin (the difference between the yields received on the Association's interest-bearing deposits, investments, mortgage backed securities and loans, including nonaccruing loans, and the rates paid for the Association's deposits and borrowings) was 1.74%, 1.79% and 1.93% in fiscal years 1989, 1988 and 1987, respectively. The decline in interest rate margin had a negative effect on net interest income. The net yield on interest-earning assets (net interest income to average interest-earning assets) for the years ended June 30, 1989, 1988 and 1987 was 1.87%, 2.03% and 2.18%, respectively.

Management's Discussion and Analysis of Financial Condition and Results of Operations

Results of Operations

Provision for Losses on Loans and Real Estate Owned

The Association continues to be adversely affected by non-earning mortgage loans and real estate owned. One measure of the quality of the loan portfolio is the amount of real estate owned and loans over 90 days delinquent (net of loss allowances). The following table illustrates this information:

At June 30 (in millions)			
	1989	1988	1987
Real estate owned	\$3.0	\$2.3	\$3.7
Non-earning loans8	1.8	2.1
Total	\$3.8	\$4.1	\$5.8
Percent of real estate owned and loans receivable .	5.8%	5.9%	10.1%

Another measure of the quality of the Association's assets is the amount of problem assets classified in accordance with Federal Home Loan Bank guidelines:

At June 30 (in millions)			
	1989	1988	1987
Classified assets	\$5.0	\$8.2	\$8.8
Percent of total assets	4.6%	8.4%	10.6%

The Association evaluates allowances for losses on loans and real estate owned on an ongoing basis. Economic conditions, portfolio mix and growth, historical loss experience and an in-depth review of selected individual loans determine the amount of the loss provisions.

The provision for losses on loans was \$323,000, \$134,000 and \$995,000 for the years ended June 30, 1989, 1988 and 1987, respectively, while loans charged off during the same periods were \$700,000, \$26,000 and \$754,000, respectively. In 1989, after an extensive review of the loan portfolio, the nonspecified loan loss allowance was increased for possible future losses. The unusually large provision in fiscal 1987 resulted primarily from anticipated losses on an improved multi-family parcel of real estate and on a renovated office building. The nonspecified allowance at June 30, 1989, net of chargeoffs, was \$330,000 compared to \$185,000 at June 30, 1988 and \$100,000 at June 30, 1987, while total allowances for loan losses on the same dates totaled \$374,000, \$752,000 and \$643,000, respectively.

Management's Discussion and Analysis of Financial Condition and Results of Operations



Results of Operations

Provision for Losses on Loans and Real Estate Owned (continued)

— The provision for estimated losses on real estate owned was \$927,000, \$96,000 and \$70,000 for fiscal years 1989, 1988 and 1987, respectively. This provision is included in "Net cost of (income from) operations of real estate owned." Since anticipated losses are expensed in the loan loss provision at the date real estate is acquired by the Association, any additions to the provision for estimated losses on real estate owned represent changes in net realizable value occurring thereafter. The unusually large provision in fiscal 1989 reflects the effects of the rezoning of an improved multi-family parcel of land and operating losses anticipated on an alcoholic treatment center acquired by foreclosure. The allowance for estimated losses on real estate owned at June 30, 1989, 1988 and 1987 was \$1.1 million, \$174,000 and \$85,000, respectively.

Other Income and Expense

— Mortgage loan originations were \$40.8 million, \$74.7 million and \$94.4 million for fiscal years 1989, 1988 and 1987, respectively. The declines in 1989 and 1988 were due in part to the unavailability of funds caused by decreased loan sales and to generally increasing interest rates which affected production and decreased refinancings. Loan sales decreased from \$60.9 million in fiscal 1987 to \$32.3 million in fiscal 1988 and to \$18.0 million in fiscal 1989. As a result of declining production and sales, corresponding decreases occurred in loan fees and gain on sale of loans.

— Loan fee income decreased \$1.0 million from fiscal 1988 to fiscal 1989 and \$127,000 from fiscal 1987 to fiscal 1988. Loan fees in fiscal 1989 decreased \$554,000 as a result of implementing a new accounting standard for loan fees. (See Note A – Interest on Loans and Loan Fees.) Loan fees also decreased \$491,000 as a result of a 45.4% decrease in loan originations and changes in the amount of loan fees charged. Loan fees in fiscal 1988 decreased only 9.9% despite a 20.9% decrease in loan production because of a shift in the types of loans originated. In fiscal 1988, 42.2% of the loans originated were multi-family, commercial and land projects, commanding higher loan fees, compared to 23.8% of these types of loans originated in 1987.

— Gain on sale of loans decreased \$66,000 from fiscal 1988 to fiscal 1989 and \$985,000 from fiscal 1987 to fiscal 1988. The 32.8% decrease in fiscal 1989 resulted primarily from a 44.3% decrease in loan sales compared to fiscal 1988, offset by \$96,000 of additional income related to the implementation of the new accounting standard. The 83.1% decrease in fiscal 1988 was partially the result of a 47.0% decrease in loan sales compared to fiscal 1987. In addition, through April 1987 lower interest rates and the Association's ability to convert loan production into mortgage backed securities significantly increased gain on sale in fiscal 1987.

— Other income has declined each year during the three years ended June 30, 1989. Declining loan originations caused decreases in miscellaneous fees charged in closing loans, and declining sales of insurance and annuity products caused a decline in fees received on these sales.

Management's Discussion and Analysis of Financial Condition and Results of Operations

Results of Operations

Other Income and Expense (continued)

————— The primary factor in the \$793,000 increase in other expense for fiscal 1989 over fiscal 1988 and the \$799,000 decrease in fiscal 1988 over fiscal 1987 is the net cost of, or income from, the operation of real estate owned. As previously discussed, the provision for estimated losses on real estate owned was \$927,000, \$96,000 and \$70,000 during the three years ended June 30, 1989, 1988 and 1987, respectively. In addition, expense to operate and maintain these properties was \$49,000, \$54,000 and \$106,000 in fiscal 1989, 1988 and 1987, respectively. In fiscal 1988 a gain of \$398,000 was recorded from the sale of a parcel of land acquired in exchange for a loan receivable, and in fiscal 1987 \$33,000 was recorded as gain on sale of real estate owned.

————— Another major factor affecting other expense was a decline in compensation and employee benefits of \$455,000 in fiscal 1989 and \$285,000 in fiscal 1988. The implementation of the new accounting standard accounted for \$317,000 of the decrease. The remaining decrease resulted from a decline in commissions paid on loan originations and fewer employees.

Federal Income Taxes

————— In the year ended June 30, 1988, the Association implemented a new accounting standard and recorded an extraordinary income tax credit of \$190,000. See Note J - Income Taxes.

Liquidity and Capital Resources

————— The Association is required by regulations to maintain in cash and liquid assets a monthly average of 5% of net withdrawable accounts plus borrowings payable on demand or within one year. The Association's liquidity ratio for the month of June 1989 was 21.6% compared to 5.1% for the month of June 1988. The increased liquidity ratio in June 1989 reflects management's desire to lessen liquidity risk and to provide funds for anticipated increases in loan production.

————— The principal sources of funds are principal and interest payments on mortgage loans and mortgage backed securities, sale of loans in the secondary market, deposit accounts, and Federal Home Loan Bank advances.

————— The repayment of principal on construction loans has been an important source of funds. During fiscal 1989 principal repayments on loans and mortgage backed securities were \$40.1 million, compared to \$24.7 million in fiscal 1988.

————— The ability of the Association to meet its liquidity needs is also dependent on the ability of the Association to sell loans in the secondary mortgage market. Most of the Association's loans are underwritten, documented and priced for sale in the secondary market. Loan sales in fiscal 1989 and 1988 were \$17.9 million and \$28.1 million, respectively.

————— In fiscal 1989 deposits were a significant source of funds, contributing \$4.6 million in cash, net of \$6.2 million in interest credited. Federal Home Loan Bank advances also provided a net increase of \$3.0 million in liquidity in fiscal 1989.



Management's Discussion and Analysis of Financial Condition and Results of Operations

Liquidity and Capital Resources (continued)

At June 30, 1989, the Association had \$3,765,749 in regulatory capital which exceeded its regulatory capital requirement of \$2,780,757 by \$984,992. On August 9, 1989, President Bush signed into law the "Financial Institutions Reform, Recovery and Enforcement Act of 1989" which, among other things, requires the new Office of Thrift Supervision to issue risk-based capital requirements which are comparable to those of national banks. In the interim, savings institutions will be required to maintain core capital of at least 3% of total assets with tangible capital of at least 1.5% required.

In anticipation of a stock offering in mid 1989, the Association has filed an offering circular for approval by the Office of Thrift Supervision. It is expected that the offering, when completed, will increase capital and liquidity by approximately \$5,000,000. Upon successful completion of this offering, the Association is expected to be in statutory compliance with new capital requirements.

Asset and Liability Management

The objective of the Association's asset and liability management program is to achieve predictable and adequate earnings and equity, with the primary focus on interest income and market value.

Interest rate risk, as measured by calculating the dollar difference between liabilities and assets repricing or maturing over a given time period, is minimal at June 30, 1989. However, interest spread and net yield have decreased over the past three years as a result of a disproportionate increase in non-accruing loans and an increasing reliance on interest sensitive certificates of deposit. Efforts are currently being directed to decrease non-accruing loans and to restructure the deposit mix.

Liquidity risk has also been reduced as evidenced by the ratio of liquid assets to total assets. Increased liquidity was accomplished through Federal Home Loan Bank borrowings, mortgage loan sales and mortgage backed security principal repayments during a period of relatively low loan production.

Credit risk is currently being addressed by the Association through a new emphasis on residential lending. This policy is intended to reduce the concentration of large income property loans, the relatively high ratio of construction loans to total loans, and the concentration of the large number of loans to relatively few borrowers.

Report of Ernst & Whinney, Independent Auditors

**Ernst &
Whinney**

999 Third Avenue
Suite 3300
Seattle, Washington 98104

Board of Directors and Shareholders
Summit Savings Association
Bellevue, Washington

We have audited the accompanying consolidated statements of financial condition of Summit Savings Association and subsidiaries as of June 30, 1989 and 1988, and the related consolidated statements of operations and shareholders' equity for each of the three years in the period ended June 30, 1989, the consolidated statement of cash flows for the year ended June 30, 1989, and the consolidated statement of changes in financial position for the years ended June 30, 1988 and 1987. These financial statements are the responsibility of the Association's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Summit Savings Association and subsidiaries at June 30, 1989 and 1988, and the consolidated results of their operations for each of the three years in the period ended June 30, 1989, their cash flows for the year ended June 30, 1989 and changes in their financial position for the years ended June 30, 1988 and 1987, in conformity with generally accepted accounting principles.

As discussed in Note J to the financial statements, effective July 1, 1987, the Association changed its method of accounting for income taxes. As discussed in Note A to the financial statements, in fiscal 1989, the Association prospectively adopted Financial Accounting Standards Board Statement No. 91, "Accounting for Nonrefundable Fees and Costs Associated with Originating or Acquiring Loans and Initial Direct Costs of Leases" and also prospectively adopted Statement No. 95, "Statement of Cash Flows."

Ernst & Whinney

Seattle, Washington
August 4, 1989

Consolidated Statements of Financial Condition



		June 30	
		1989	1988
Assets	Cash	\$ 2,984,105	\$ 1,380,140
	Interest-bearing deposits	8,992,576	2,213,373
	Investment securities (market value of \$8,067,413 in 1989 and \$3,483,177 in 1988) - Notes B, F and I	8,206,777	3,742,352
	Investment securities held for sale (market value of \$2,990,188) - Note B	2,960,983	
	Federal Home Loan Bank stock - Note G	1,071,000	945,000
	Mortgage backed securities (market value of \$15,811,514 in 1989 and \$16,196,195 in 1988) - Note H	17,035,586	17,908,280
	Mortgage loans receivable held for sale (market value of \$1,137,602)	1,130,081	
	Loans receivable, net - Notes C and G	61,622,640	66,635,163
	Accrued loan interest receivable	813,482	834,876
	Accrued investment interest receivable	167,532	75,797
	Real estate owned, net - Note D	2,982,056	2,263,602
	Leasehold improvements, and furniture and equipment - Note E	214,234	302,233
	Deferred premium on loan sales	1,189,989	1,587,032
	Other assets	599,357	506,439
		<u>\$109,970,398</u>	<u>\$98,394,287</u>
Liabilities	Deposits - Note F	\$ 80,266,824	\$69,531,080
	Advances from Federal Home Loan Bank - Note G	9,600,000	6,600,000
	Short-term borrowings - Note I	409,441	269,813
	Collateralized mortgage obligations - Note H	14,047,822	14,685,901
	Convertible subordinated debentures - Note I	520,509	520,509
	Accrued interest payable	620,295	604,565
	Advances from borrowers for taxes and insurance	319,331	474,897
	Principal and interest payable on sold loans	845,395	699,020
	Accounts payable and accrued expenses	398,961	427,286
	Federal income taxes - Note J	26,500	514,000
		<u>107,055,078</u>	<u>94,327,071</u>
	Commitments - Notes C and L		
Shareholders' Equity - Notes J, K, M and N	Preferred stock, par value \$.01 per share - authorized 500,000 shares, no shares issued or outstanding.		
	Common stock, par value \$.01 per share - authorized 3,500,000 shares, issued and outstanding 625,974 shares	6,260	6,260
	Additional paid-in capital	2,939,357	2,939,357
	Retained earnings (deficit) - substantially restricted	(30,297)	1,121,599
		<u>2,915,320</u>	<u>4,067,216</u>
		<u>\$109,970,398</u>	<u>\$98,394,287</u>

See notes to consolidated financial statements.

Summit Savings Association and Subsidiaries

Consolidated Statements of Shareholders' Equity

	Number of Shares Outstanding	Common Stock	Additional Paid-in Capital	Retained Earnings (Deficit)	Total
Balance at July 1, 1986	623,362	\$6,234	\$2,928,930	\$ 819,273	\$3,754,437
Stock options exercised	2,612	26	10,427		10,453
Net loss				(122,369)	(122,369)
Balance at June 30, 1987	625,974	6,260	2,939,357	696,904	3,642,521
Net income				424,695	424,695
Balance at June 30, 1988	625,974	6,260	2,939,357	1,121,599	4,067,216
Net loss				(1,151,896)	(1,151,896)
Balance at June 30, 1989 – Notes J and K	625,974	\$6,260	\$2,939,357	\$ (30,297)	\$2,915,320

See notes to consolidated financial statements.

Consolidated Statements of Operations

		Year Ended June 30		
		1989	1988	1987
Interest Income	Interest and fees on loans – Note A	\$ 8,035,867	\$6,521,517	\$6,666,012
	Interest on mortgage backed securities	1,392,661	1,238,745	210,608
	Interest on deposits with banks	234,305	270,742	199,977
	Interest and dividends on investment securities (taxable)	523,060	152,131	249,192
	Dividends on Federal Home Loan Bank stock	126,157	90,044	58,740
	Total Interest Income	10,312,050	8,273,179	7,384,529
Interest Expense	Interest on deposits:			
	Checking	511,513	727,655	1,067,745
	Statement savings	21,549	22,694	17,677
	Certificates of deposit	5,631,171	4,494,453	4,088,593
		6,164,233	5,244,802	5,174,015
	Interest on borrowings:			
	Advances from Federal Home Loan Bank	750,088	882,456	531,368
	Short-term borrowings	11,191	193,939	70,551
	Collateralized mortgage obligations	1,502,573	124,696	
	Convertible subordinated debentures	51,147	50,619	733
		2,314,999	1,251,710	602,652
	Total Interest Expense	8,479,232	6,496,512	5,776,667
	Net Interest Income	1,832,818	1,776,667	1,607,862
	Provision for loan losses	322,774	134,072	995,087
	Net Interest Income After Provision For Loan Losses	1,510,044	1,642,595	612,775



Consolidated Statements of Operations (continued)

Other Income	Loan fees – Note A	\$ 119,103	\$1,164,321	\$1,291,686
	Loan servicing income	280,185	236,684	265,015
	Gain on sale of loans – Note A	134,785	200,445	1,185,624
	Investment securities losses		(58,994)	(63,181)
	Other	129,604	189,027	295,229
		<u>663,677</u>	<u>1,731,483</u>	<u>2,974,373</u>
<hr/>				
Other Expense	Compensation and benefits – Note A	1,307,189	1,762,619	2,047,690
	Advertising	76,808	91,951	52,877
	Depreciation and amortization	121,381	175,429	185,275
	Data processing	136,911	143,140	128,168
	Occupancy	477,350	464,937	367,411
	Professional services	199,311	147,293	228,192
	Insurance	183,540	166,747	181,185
	Net cost of (income from) operations of real estate owned (including gains on sale of \$426,811 and \$32,940 in 1988 and 1987, respectively) – Note D	976,096	(276,420)	143,663
	Other	324,113	333,687	474,056
		<u>3,802,699</u>	<u>3,009,383</u>	<u>3,808,517</u>
	<hr/>			
	Income (Loss) Before Income Taxes and Accounting Change	(1,628,978)	364,695	(221,369)
	Provision (benefit) for deferred federal income taxes - Note J	(477,082)	130,000	(99,000)
	Income (Loss) Before Accounting Change	(1,151,896)	234,695	(122,369)
	Cumulative effect of benefit of change in accounting for income taxes - Note J .		190,000	
	Net Income (Loss)	<u>\$(1,151,896)</u>	<u>\$ 424,695</u>	<u>\$(122,369)</u>
	Earnings (loss) per share:			
	Net Income (Loss) Before Accounting Change	\$ (1.84)	\$.38	\$ (.20)
	Cumulative effect of accounting change		.30	
	Net Income (Loss)	<u>\$ (1.84)</u>	<u>\$.68</u>	<u>\$ (.20)</u>

See notes to consolidated financial statements.

Summit Savings Association and Subsidiaries

Consolidated Statement of Cash Flows

		Year Ended June 30, 1989
Operating Activities	Net Loss	\$(1,151,896)
	Adjustments to reconcile net loss to net cash used by operating activities:	
	Discount accretion on investment securities	(158,747)
	Gains deferred on loans sold	(11,319)
	Deferred loan fee accretion	(291,900)
	Increase in accrued interest receivable	(70,341)
	Provisions for losses on loans and real estate owned	1,249,485
	Provision for depreciation	121,381
	Gain on sale of leasehold improvements abandoned	(1,545)
	Federal Home Loan Bank stock dividend	(126,000)
	Amortization of deferred premium on loan sales	408,362
	Net increase in other assets	(92,918)
	Increase in accrued interest payable	15,730
	Decrease in advances from borrowers for taxes and insurance	(155,566)
	Increase in principal and interest payable on loans sold	146,375
	Net decrease in accounts payable and accrued expenses	(28,325)
	Decrease in federal income taxes	(10,418)
	Benefit for deferred federal income taxes	(477,082)
	Net Cash Used by Operating Activities	(634,724)
Investing Activities	Proceeds from investment securities maturing	11,701,000
	Purchases of investment securities	(18,967,661)
	Proceeds from sale of loans receivable	17,935,649
	Principal collected on mortgage backed securities	872,694
	Principal collected on loans receivable and transfers to real estate owned	39,185,752
	Loans originated, net of changes in loans in process	(53,008,063)
	Loans purchased	(261,770)
	Proceeds from sale of real estate owned	513,817
	Additions to real estate owned	(2,158,982)
	Additions to leasehold improvements, furniture and equipment	(39,730)
	Proceeds from sale of leasehold improvements, furniture and equipment	7,893
	Net Cash Used by Investing Activities	(4,219,401)
Financing Activities	Net decrease in checking and statement savings	(3,941,142)
	Proceeds from sales of certificates of deposit	48,331,985
	Payments for maturing certificates of deposit	(33,655,099)
	Proceeds from advances from Federal Home Loan Bank	15,000,000
	Repayment of advances from Federal Home Loan Bank	(12,000,000)
	Net increase in short-term borrowings	139,628
	Decrease in collateralized mortgage obligations	(638,079)
	Net Cash Provided by Financing Activities	13,237,293
	Increase in Cash and Cash Equivalents	8,383,168
	Cash and cash equivalents at beginning of year	3,593,513
	Cash and Cash Equivalents at June 30, 1989	<u>\$11,976,681</u>
	Supplemental Cash Flow Information:	
	Cash paid during the year:	
	Interest on deposits and other borrowings (advances from Federal Home Loan Bank, short-term borrowings, collateralized mortgage obligations, and convertible subordinated debentures)	\$ 8,463,502
	Federal income taxes	\$ 10,418

See notes to consolidated financial statements.

Consolidated Statements of Changes in Financial Position



		Year Ended June 30	
		1988	1987
Source of Funds	From operations:		
	Income (loss) before accounting change	\$ 234,695	\$ (122,369)
	Add (deduct) items recognized in net income which did not affect funds:		
	Interest credited to deposits	5,249,181	5,179,460
	Provision for depreciation	143,892	142,404
	Amortization of organization costs	32,153	42,871
	Deferred loan fee accretion	(173,375)	(208,673)
	Amortization of deferred premium on loan sales	448,466	343,913
	Premium amortization (discount accretion) on investment securities	1,669	(88,614)
	(Increase) decrease in accrued interest receivable	(231,174)	69,453
	Federal Home Loan Bank stock dividend	(89,900)	(58,600)
	Increase (decrease) in accrued interest payable	511,134	(117,571)
	Gains on real estate sold		(35,650)
	Gains on loans and mortgage backed securities sold	(67,730)	(1,818,770)
	Loss on leasehold improvements, furniture and equipment abandoned or sold	22,116	45,192
	Provision for losses on loans and real estate	230,479	1,065,349
	Increase in deferred federal income tax	(60,000)	(99,000)
	Write-down of securities due to permanent impairment of value		98,384
		<u>6,016,911</u>	<u>4,560,148</u>
	Funds Provided From Operations Before Accounting Change	6,251,606	4,437,779
	Cumulative effect of accounting change	190,000	
	Funds Provided From Operations	6,441,606	4,437,779
	Investment securities matured and sold	6,394,348	2,107,985
	Loan and mortgage backed security principal reductions and transfers to real estate owned	24,657,035	45,857,977
	Loans and mortgage backed securities sold	28,132,233	52,020,724
	Proceeds from sale of real estate owned	4,307,056	2,709,429
	Proceeds from sale of convertible subordinated debentures	95,634	424,875
	Proceeds from collateralized mortgage obligations	14,685,901	
	Decrease in other assets		222,718
	Proceeds from advances from Federal Home Loan Bank	26,600,000	34,843,750

Summit Savings Association and Subsidiaries

Consolidated Statements of Changes in Financial Position (continued)

		Year Ended June 30	
		1988	1987
Source of Funds (continued)	Proceeds from reverse repurchase agreements	\$ 40,069,973	
	Proceeds from short-term bank borrowings	8,000,000	\$ 5,000,000
	Increase in advances from borrowers for taxes and insurance	41,307	314,874
	Increase in principal and interest payable on loans sold	182,074	198,379
	Increase in accounts payable and accrued expenses		13,661
	Proceeds from exercise of stock options		10,453
		<u>\$159,607,167</u>	<u>\$148,162,604</u>
Application of Funds	Increase in cash and interest bearing deposits	\$ 2,375,115	\$ 181,730
	Purchase of investment securities	4,973,125	3,945,641
	Loans originated, net of changes in loans in process	67,360,837	93,332,212
	Loans purchased	1,609,746	
	Additions to real estate owned	2,924,270	4,228,961
	Additions to leasehold improvements, furniture and equipment	17,350	309,885
	Purchase of Federal Home Loan Bank stock	288,800	46,300
	Increase in other assets	251,701	
	Decrease in deposits before interest credited	3,795,867	4,447,836
	Repayment of Federal Home Loan Bank advances	27,843,750	35,000,000
	Decrease in other short-term borrowings	36,494	1,670,039
	Repayment of reverse repurchase agreements	40,069,973	
	Repayment of short-term bank borrowings	8,000,000	5,000,000
	Decrease in accounts payable and accrued expenses	60,139	
		<u>\$159,607,167</u>	<u>\$148,162,604</u>

See notes to consolidated financial statements.

**Note A -
Summary of
Significant
Accounting
Policies**

————— The accounting principles followed by the Association and its subsidiaries and the methods of applying them conform with generally accepted accounting principles and with general practice within the savings and loan industry. The more significant accounting policies are summarized below.

Organization

————— Summit Savings Association was incorporated as a Washington State chartered savings and loan association on May 29, 1981. Costs of \$214,355 incurred during this period were capitalized and amortized, using the straight-line method, over a period of five years. Accumulated amortization for the years ended June 30, 1989, 1988 and 1987 was \$214,355, \$214,355, and \$182,202, respectively.

**Principles
of Consolidation**

————— The accompanying consolidated financial statements include Summit Savings Association and its wholly-owned subsidiaries, Summit Services, Inc. and Summit Capital Corporation. All significant intercompany transactions and balances have been eliminated in consolidation.

**Investment
Securities**

————— Investment securities are designated at the date of purchase as portfolio securities or securities held for sale. Investments held for sale are recorded at the lower of aggregate cost or market. Portfolio investments are recorded at cost, net of discounts and premiums, which are amortized to maturity. The cost of investments sold is computed using the specific identification method. In 1987, other investments were written down as a decline in market value was considered by management to be a permanent impairment of value. The write-downs are included in "Investment securities losses."

**Futures
Contracts**

————— The Association has invested in futures contracts and options to hedge fixed-rate mortgage loans against interest rate fluctuations. Loans are hedged during the period between the date the interest rate is guaranteed to the customer and the date of the loan's sale in the secondary market. Gains and losses on futures contracts were taken into income or expensed immediately if the loan did not close or when the loan was sold. The cost of the option is amortized against gain on sale of loans over the life of the option, with any remaining cost written off at the time the loans are sold.

————— The Association has invested in Eurodollar futures options to hedge its large certificates of deposit against rising interest rates. The cost of these options was amortized over the life of the option, while gains are amortized over the estimated life of the certificates.

**Mortgage Backed
Securities**

————— Mortgage backed securities are recorded at cost less principal repayments as it is management's intention to hold the securities to maturity.



Notes to Consolidated Financial Statements

Note A - Summary of Significant Accounting Policies (continued)

Real Estate Owned

Real estate owned consists of real estate acquired through foreclosure or deed in lieu of foreclosure. It is recorded at the lower of the loan balance on the property (including related foreclosure costs) at the date of acquisition or the net realizable value. Any anticipated losses at the date of acquisition are recognized as loan losses prior to transfer to real estate owned.

Leasehold Improvements, and Furniture and Equipment

Leasehold improvements, and furniture and equipment are recorded at cost. Amortization of leasehold improvements is computed by the straight-line method over the shorter of the estimated useful life or the remaining term of the lease. Depreciation of furniture and equipment is computed on the straight-line method over the estimated useful lives of the assets. Maintenance and repairs are expensed as incurred. Gains and losses on disposals are recognized in the year of disposal.

Income Taxes

The Association files a consolidated federal income tax return with its subsidiaries. Investment tax credits are recognized using the flow-through method in the year utilized.

Earnings (Loss) Per Share

Earnings per share is computed based on common stock equivalents and common stock outstanding. Loss per share is computed on the number of shares outstanding.

Statement of Cash Flows

In November 1987, the Financial Accounting Standards Board issued Statement No. 95, "Statement of Cash Flows." As permitted by the Statement, the Association has presented a Statement of Cash Flows for 1989 and a Statement of Changes in Financial Position for 1988 and 1987. Cash equivalents include cash and interest-bearing deposits.

Financial Statement Reclassifications

Certain amounts in the June 30, 1988 and 1987 financial statements have been reclassified to conform with the presentation of these amounts in the June 30, 1989 financial statements.

Note B - Investment Securities and Investment Securities Held For Sale

The recorded values and aggregate market values of investment securities and investments held for sale at June 30, 1989 and 1988 consisted of the following:

	1989		1988	
	Recorded Value	Market Value	Recorded Value	Market Value
Investment Securities				
U.S. Treasury and Agency	\$2,734,794	\$2,597,032	\$2,742,352	\$2,483,177
Bankers' Acceptances	4,972,983	4,971,381		
CDs with other financial institutions	499,000	499,000	1,000,000	1,000,000
	<u>\$8,206,777</u>	<u>\$8,067,413</u>	<u>\$3,742,352</u>	<u>\$3,483,177</u>
Investment Securities Held for Sale				
U.S. Treasury and Agency	\$1,013,862	\$1,024,688		
Corporate bonds and notes .	1,947,121	1,965,500		
	<u>\$2,960,983</u>	<u>\$2,990,188</u>		



Notes to Consolidated Financial Statements

Note A - Summary of Significant Accounting Policies (continued)

Real Estate Owned

Real estate owned consists of real estate acquired through foreclosure or deed in lieu of foreclosure. It is recorded at the lower of the loan balance on the property (including related foreclosure costs) at the date of acquisition or the net realizable value. Any anticipated losses at the date of acquisition are recognized as loan losses prior to transfer to real estate owned.

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Leasehold improvements, and furniture and equipment are recorded at cost. Amortization of leasehold improvements is computed by the straight-line method over the shorter of the estimated useful life or the remaining term of the lease. Depreciation of furniture and equipment is computed on the straight-line method over the estimated useful lives of the assets. Maintenance and repairs are expensed as incurred. Gains and losses on disposals are recognized in the year of disposal.

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	Recorded Value	Market Value	Recorded Value	Market Value
Investment Securities				
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Bankers' Acceptances	4,972,983	4,971,381		
CDs with other financial institutions	499,000	499,000	1,000,000	1,000,000
	<u>\$8,206,777</u>	<u>\$8,067,413</u>	<u>\$3,742,352</u>	<u>\$3,483,177</u>
Investment Securities Held for Sale				
U.S. Treasury and Agency	\$1,013,862	\$1,024,688		
Corporate bonds and notes	1,947,121	1,965,500		
	<u>\$2,960,983</u>	<u>\$2,990,188</u>		

Notes to Consolidated Financial Statements

**Note C - Loans
Receivable and
Loans Receivable
Held For Sale**

Loans receivable and loans receivable held for sale at June 30, 1989 and 1988 consisted of the following:

	1989	1988
Loans on existing property:		
1-4 family	\$17,559,254	\$21,120,358
Multi-family	6,460,892	7,172,050
Commercial	9,052,970	8,834,446
Construction loans:		
1-4 family	12,730,659	11,384,937
Multi-family	7,348,174	16,241,916
Commercial	8,972,886	15,378,712
Land loans	4,687,015	4,551,988
Lines of credit	377,164	503,966
Other loans	265,049	253,890
	<u>67,454,063</u>	<u>85,442,263</u>
Less:		
Deferred loan fees	(399,811)	(355,559)
Loans in process of completion	(5,057,154)	(17,699,769)
Allowance for loan losses	<u>(374,458)</u>	<u>(751,772)</u>
Loans receivable	<u>61,622,640</u>	<u>66,635,163</u>
Mortgage loans held for sale:		
1-4 family	<u>1,130,081</u>	
Total loans	<u>\$62,752,721</u>	<u>\$66,635,163</u>
Changes in the allowance for loan losses were as follows:		
Balance at July 1, 1986	\$402,518	
Provision charged to operations	995,087	
Loans charged off	<u>(754,162)</u>	
Balance at June 30, 1987	643,443	
Provision charged to operations	134,072	
Loans charged off	<u>(25,743)</u>	
Balance at June 30, 1988	751,772	
Provision charged to operations	322,774	
Loans charged off	<u>(700,088)</u>	
Balance at June 30, 1989	<u>\$374,458</u>	

Loans serviced for the benefit of others totaled \$99,929,133, \$104,372,980, and \$99,259,944 at June 30, 1989, 1988 and 1987, respectively.

Certain officers and directors of Summit Savings Association were loan customers of the Association in the ordinary course of business. At June 30, 1989 and 1988, such loans totaled approximately \$108,000 and \$313,000, respectively. The net reduction resulted from the departure of certain officers and promotion of others.

Loan commitments outstanding at June 30, 1989 were approximately \$12,892,300, of which \$292,400 were 15 to 30 year fixed-rate commitments with rates ranging from 10% to 10.75%. In addition, the Association has committed to interest rates of 9.50% to 10.63% in connection with applications for \$1,807,000 of fixed-rate loans. The balance of the loan commitments are at rates which adjust to market at the time the loan is closed.



Notes to Consolidated Financial Statements

Note D - Real Estate Owned

Real estate owned at June 30, 1989 and 1988 consisted of the following:

	<u>1989</u>	<u>1988</u>
Real estate in judgment		\$ 212,907
Allowance for estimated losses		<u>(8,987)</u>
		203,920
Real estate acquired through foreclosure or deed in lieu of foreclosure	\$4,001,452	2,224,687
Allowance for estimated losses	<u>(1,019,396)</u>	<u>(165,005)</u>
	2,982,056	2,059,682
	<u>\$ 2,982,056</u>	<u>\$2,263,602</u>

Changes in the allowance for estimated losses on real estate owned and real estate in judgment were as follows:

Balance at July 1, 1986	\$ 35,000
Provision charged to operations	70,262
Losses realized on real estate sold	<u>(19,808)</u>
Balance at June 30, 1987	85,454
Provision charged to operations	96,398
Losses realized on real estate sold	<u>(7,860)</u>
Balance at June 30, 1988	173,992
Provision charged to operations	926,711
Losses realized on real estate sold	<u>(81,307)</u>
Balance at June 30, 1989	<u>\$1,019,396</u>

————— The provision charged to operations is included in the net cost of operations of real estate owned in the consolidated statements of operation.

Notes to Consolidated Financial Statements

Note E - Leasehold Improvements, and Furniture and Equipment

Leasehold improvements, and furniture and equipment at June 30, 1989 and 1988 consisted of the following:

	Estimated Useful Lives	1989	1988
Leasehold improvements	Life of lease	\$134,938	\$ 97,149
Furniture and equipment	3-5 years	618,906	624,640
		753,844	721,789
Allowance for depreciation		(539,610)	(419,556)
		\$214,234	\$302,233

Note F - Deposits

Deposits by interest rate at June 30, 1989 and 1988 consisted of the following:

	Stated Rate at June 30, 1989	1989		1988	
		Amount	Percent	Amount	Percent
Business checking	0.00%	\$ 48,039	.1%	\$ 51,050	.1%
Non-interest checking	0.00	347,458	.4	204,577	.3
Treasury, tax, and loan deposits	0.00	25,166		27,496	
Checking with interest	4.45-5.20*	875,171	1.1	1,097,226	1.6
Statement savings	5.50	294,620	.4	418,521	.6
Money market checking	4.80	719,173	.9	628,041	.9
Money market plus	7.50-8.25*	5,649,505	7.0	9,473,363	13.6
		7,959,132	9.9	11,900,274	17.1
Certificates:					
5.01 - 6.00		105,034	.1	401,226	.6
6.01 - 7.00		153,591	.2	4,916,440	7.1
7.01 - 8.00		4,318,023	5.4	44,723,207	64.3
8.01 - 9.00		18,456,782	23.0	6,028,277	8.7
9.01 - 10.00		32,197,345	40.1	1,303,088	1.9
10.01 - 11.00		16,813,516	21.0	8,185	
11.01 - 12.00		100,429	.1	100,383	.1
13.01 - 14.00		150,000	.2	150,000	.2
		72,294,720	90.1	57,630,806	82.9
Deferred hedging gain		12,972			
		\$80,266,824	100.0%	\$69,531,080	100.0%

* Tiered rates

Certificate accounts will mature as of June 30 as follows:

	1989		1988	
	Amount	Percent	Amount	Percent
Within one year	\$64,663,559	89.4%	\$51,964,861	90.2%
From one to two years	4,494,885	6.2	2,014,132	3.5
Thereafter	3,149,248	4.4	3,651,813	6.3
	\$72,307,692	100.0%	\$57,630,806	100.0%

— Federal Reserve Board regulations require that the Association maintain certain reserve balances on deposit with the Federal Reserve Bank. At June 30, 1989, this amount was approximately \$558,000.

— Public funds of \$4,862,848 and \$6,626,368, included in deposits at June 30, 1989 and 1988, are collateralized by investment securities with book values of \$1,229,092 and \$1,232,975 and market values of \$1,122,188 and \$1,020,025 at June 30, 1989 and 1988, respectively.



Notes to Consolidated Financial Statements

Note G - Advances From Federal Home Loan Bank

Advances from the Federal Home Loan Bank of Seattle at June 30, 1989 and 1988 consisted of the following:

Payable during year ending June 30	Average interest rate at June 30, 1989	1989	1988
1989			\$1,000,000
1990	8.95%	\$2,000,000	2,000,000
1991	10.32	3,000,000	
1992	8.66	4,000,000	3,000,000
1993	9.45	600,000	600,000
	9.29	<u>\$9,600,000</u>	<u>\$6,600,000</u>

Advances are collateralized by mortgage loans with a market value of not less than 120% of outstanding Bank advances and by Federal Home Loan Bank stock with a recorded value of \$1,071,000.

Note H - Collateralized Mortgage Obligations

The Association's wholly-owned subsidiary, Summit Capital Corporation, issued collateralized mortgage obligations (bonds), which are collateralized by Federal Home Loan Mortgage Corporation (FHLMC) mortgage backed securities, with aggregate unpaid principal balances (net of deferred loan fees) of \$17,035,586 as of June 30, 1989 and \$17,908,280 as of June 30, 1988. The mortgage backed securities are held by a bond trustee for the benefit of the bond holders.

The net cash flow from these mortgage backed securities together with the reinvestment income thereon provide for the repayment of the underlying bonds.

The bonds consisted of the following at June 30:

	Interest Rate	Stated Maturity	1989 Principal	1988 Principal
Sequence 1-A	9.70%	April 1, 2013	\$14,027,906	\$14,750,000
Sequence 1-Z	9.95	January 1, 2018	525,063	487,751
Unamortized discount			(505,147)	(551,850)
			<u>\$14,047,822</u>	<u>\$14,685,901</u>

The bonds will be repaid in quarterly installments from the proceeds received on the underlying collateral on a proportionate basis with the mortgage backed securities. Because it is possible that the underlying collateral for the mortgage backed securities may prepay, it is expected that the actual lives of the bonds will be substantially less than their stated maturities.

Bond maturities for the succeeding five years are estimated, on the basis of past prepayment experience of the pledged mortgage backed securities, as follows:

Year Ending June 30	
1990	\$ 530,000
1991	526,000
1992	523,000
1993	520,000
1994	519,000
Thereafter	<u>11,429,822</u>
	<u>\$14,047,822</u>

Summit Savings Association and Subsidiaries

Notes to Consolidated Financial Statements

Note I - Short-Term Borrowings and Convertible Subordinated Debentures

Short-term borrowings consist of consumer repurchase agreements which bore interest rates of 4.65% at June 30, 1989 and 5.25% at June 30, 1988 and are collateralized by investment securities with book values of \$499,630 and \$499,465 and market values of \$483,281 and \$475,014 at June 30, 1989 and 1988, respectively.

There were no reverse repurchase agreements outstanding during fiscal 1989.

During the years ended June 30, 1988 and 1987, the Association sold \$520,509 of 9% convertible subordinated debentures due December 31, 1996. The debentures are convertible at any time prior to maturity, unless previously redeemed, into common stock of the Association at a conversion price of \$5.50 per share. The debentures are redeemable in whole or in part, at the option of the Association, at premiums at any time after January 1, 1990. The debentures are subordinated in right of payment to all of the Association's existing and future indebtedness.

Note J - Federal Income Taxes

The Association has qualified under provisions of the Internal Revenue Code which permit it to deduct from taxable income an allowance for bad debts which differs from the provision for such losses charged to income. Accordingly, retained earnings (deficit) at June 30, 1989 includes approximately \$967,000 for which no provision for federal income taxes has been made. If this portion of retained earnings is used for any purpose other than to absorb bad debt losses, an additional deferred tax liability of approximately \$328,600 will be required.

Deferred federal income tax provisions result from temporary differences. Temporary differences are differences between the tax basis of assets and liabilities and their reported amounts on financial statements that will result in differences between income for tax purposes and income for financial statement purposes in future years. Cumulative temporary differences as of June 30, 1989 were approximately \$3,750,000.

Temporary differences and their tax effects for the years ended June 30, 1989, 1988 and 1987 are as follows:

	1989	1988	1987
Market value adjustment for investment securities		\$ 45,300	\$ (45,300)
FHLB stock dividends	\$ 42,840	30,500	48,300
Gain on sale of loans	(134,995)	(49,400)	678,400
Loan fees	(98,957)	93,500	(27,600)
Current year effect of changing from cash to accrual basis reporting for tax purposes	(207,431)	(220,200)	375,800
Tax net operating loss carryforward . .	(64,156)	228,300	(1,128,000)
Other	(14,383)	2,000	(600)
Cumulative effect of benefit of change in accounting for income taxes . . .		(190,000)	
Total	<u>\$ (477,082)</u>	<u>\$ (60,000)</u>	<u>\$ (99,000)</u>



Notes to Consolidated Financial Statements

Note J - Federal Income Taxes (continued)

The provision for deferred federal income taxes is different from that which would result by applying the statutory income tax rate to pretax income or loss.

A reconciliation of the difference for the years ended June 30, 1989, 1988 and 1987 follows:

	1989	1988	1987
Statutory Rate	34%	34%	46%
Tax (benefit) at statutory rate	\$(553,852)	\$ 123,997	\$(101,829)
Bad debt deduction based on experience method (net of minimum tax)	(375,725)	(55,400)	(488,987)
Surtax exemption			20,250
Loan loss and real estate owned reserve additions	424,825	78,400	490,061
Other	27,670	(16,997)	(18,495)
Provision (Benefit) for Deferred Federal Income Taxes Before Accounting Change	(477,082)	130,000	(99,000)
Cumulative effect of benefit of change in accounting for income taxes		(190,000)	
Total	\$(477,082)	\$ (60,000)	\$ (99,000)

At June 30, 1989, the following federal income tax carryforwards were available:

	Expiration Dates	Amount
Net Operating Loss Carryforwards	1992	\$1,184,300
	1993	1,382,200
	1994	516,400
	2000	10,100
	2001	14,400
	2002	102,700
	2004	261,100
		<u>\$3,471,200</u>
Investment Tax Credit Carryforwards, net of 35% reduction	1998	\$ 2,773
	1999	3,437
	2000	3,756
	2001	1,167
		<u>\$ 11,133</u>

In 1988 the Association adopted Statement of Financial Accounting Standards No. 96, "Accounting for Income Taxes," effective July 1, 1987. The most significant change for the Association under this statement is that deferred tax liabilities are adjusted in the period of change in tax laws or rates. As the Association had originally provided for deferred tax liabilities at higher than current rates, the adoption of this Statement resulted in a reduction in deferred income taxes payable. The impact of the change on years prior to fiscal 1988 was \$190,000 which is reported as the cumulative effect of an accounting change. Prior period financial statements have not been restated.

Summit Savings Association and Subsidiaries

Notes to Consolidated Financial Statements

Note K - Shareholders' Equity

Shareholders' equity in the consolidated financial statements differs from that reported to the Federal Home Loan Bank and is reconciled as follows:

	1989	1988
Shareholders' equity under generally accepted accounting principles	\$2,915,320	\$4,067,216
Subordinated debentures	520,509	520,509
Non-specified loss reserves	329,920	185,000
Regulatory capital	3,765,749	4,772,725
Regulatory capital requirement	2,780,757	3,182,504
Excess over requirement	\$ 984,992	\$1,590,221

— In connection with obtaining an organizing permit from the State of Washington, the Association agreed to "earmark", for initial operating expenses, \$.75 per share (\$212,513) of the additional paid-in capital resulting from the sale of common stock. These funds are restricted as to distribution to shareholders unless approval is obtained from the State.

Note L - Lease Commitments

— On July 1, 1986, the Association entered into a 5-year lease for an administrative and branch facility. Two floors of a new building were leased and approximately 42% of the space was subleased at June 30, 1989. Rent is payable as follows: Zero for the first year, \$30,845 per month for the second and third years, and \$32,773 per month for the fourth and fifth years. The Association has the option to extend the lease for two additional five-year periods following the expiration of the initial lease.

— On September 28, 1987, the Association entered into a 1-year lease for a loan office in Puyallup. In April 1989, the Puyallup office was closed.

— Rent expense for the years ending June 30, 1989, 1988 and 1987 was approximately \$334,000, \$371,000 and \$251,000, respectively.

Future minimum rental commitments are as follows:

Year Ending June 30	Amount
1990	\$391,300
1991	393,300
1992	32,800
	817,400
Proceeds from sublease	(243,100)
	\$574,300



Notes to Consolidated Financial Statements

Note M - Stock Options and Warrants

The Association granted options to officers and full-time employees under its Incentive Stock Plan adopted September 19, 1984. Under this plan, 87,388 shares of the Association's common stock are reserved for future issuance. The option price at which the common stock may be purchased upon exercise of an option must not be less than the fair market value of such shares at the time the option is granted. Options granted are for five years. The last of the outstanding options expire April 7, 1994.

Changes in stock options are as follows:

Option Shares	1989	1988
Outstanding beginning of fiscal year	52,363	56,688
Granted	31,664	
Expired	(41,200)	(4,325)
Outstanding June 30	42,827	52,363
Exercisable June 30	7,587	16,613

At June 30, 1989, 44,561 shares were available for future grants under the Incentive Stock Plan. At June 30, 1989, the price of options outstanding ranged from \$2.90 to \$6.50 and the price of options exercisable ranged from \$3.19 to \$5.19.

Note N - Subsequent Events

On July 7, 1989, the Association filed a preliminary offering circular draft with the Federal Savings and Loan Insurance Corporation ("FSLIC"), the Supervisor of Savings and Loan Associations of the State of Washington and the Federal Home Loan Bank Board ("FHLBB") for the purpose of obtaining approval for proceeding with a public offering of newly issued Summit Savings Association common stock. The shares will first be offered to eligible shareholders and then to the general public. The number of shares to be offered, estimated to be between 1,000,000 to 1,250,000, will be determined by the offering price and the offering price will be determined by market conditions at the time of the sale. The primary purpose of the proposed offering of securities is to increase the Association's capital to meet anticipated increases in capital requirements.

Summit Savings Association and Subsidiaries

Senior Management



Back Row – Left to Right
Kathy J. Burke, Merri Ann Simonson,
Gary R. Wilson

Front Row – Left to Right
Patricia L. Waldow, James F. Grabicki, Marie T. Gudger

Corporate Information



Directors

JAMES D. HUBER
Chairman of the Board
President
ATCON Services Inc.

JAMES F. GRABICKI
President
Chief Executive Officer

JOHN D. CADIGAN
President
Rio Petrol, Inc.
Vice President
Campbell Investment Co.

WILLIAM P. HURME
President
Altis Properties, Ltd.

DOUG T. MERGENTHALER
President
Ashton Corporation

WILLIAM P. NEWMAN
Director, Marketing Services
Westin Hotels & Resorts

PAUL E. NOLAN
President
Nolan Development, Inc.

NORMAN D. WINTON
Division Vice President
Measurex Corporation

Officers

JAMES F. GRABICKI
President
Chief Executive Officer

MARIE T. GUDGER
Senior Vice President
Chief Financial Officer
Corporate Secretary

GARY R. WILSON
Senior Vice President
Chief Lending Officer

KATHY J. BURKE
Vice President
Financial Services
Personnel

MERRI ANN SIMONSON
Vice President
Loan Servicing
Special Credits

PATRICIA L. WALDOW
Vice President
Controller

CORPORATE HEADQUARTERS
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Bellevue, Washington 98005
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Seattle, Washington 98104

GENERAL COUNSEL
Foster, Pepper & Shefelman
1111 Third Avenue
Seattle, Washington 98101

SPECIAL COUNSEL
Breyer & Zinski
Suite 305 East
555 13th Street, NW
Washington, D.C. 20004

STOCK LISTING NASDAQ
Symbol: SMMT

STOCK TRANSFER AGENT
First Interstate Bank, Ltd.
26610 West Agoura Road
Calabasas, CA 91302
Shareholder Relations
1-800-522-6645

ANNUAL MEETING

The 1989 Annual Meeting of Shareholders of Summit Savings will be held at the Bellevue Athletic Club, 11200 S.E. 6th, Bellevue, Washington on Thursday, November 9, 1989 at 3:00 p.m. Questions relating to stock and requests for copies of Annual Report to Shareholders, Annual Report on Form 10-K, interim reports or Form 10-Q and other published reports, which will be furnished without charge, should be addressed to:

Corporate Secretary
11711 SE 8th Street
Bellevue, WA 98005

Corporate Information (continued)

**STOCK
INFORMATION**

Summit Savings' common stock is listed on the National Association of Securities Dealers Automated Quotation System (NASDAQ) under the symbol "SMMT." The number of holders of record of the Association's common stock at June 30, 1989 was approximately 600. The following are based on the last reported sale prices in the NASDAQ National Market System for the fiscal quarters indicated as reported by the National Association of Securities Dealers:

	Bid Price for Fiscal Year Ending			
	1989		1988	
	High	Low	High	Low
Quarter Ended:				
September 30	\$3.87	\$3.12	\$5.00	\$3.63
December 31	3.12	2.12	3.75	2.13
March 31	4.75	2.25	4.38	2.38
June 30	5.50	4.13	4.25	3.25

The Association may not declare or pay a cash dividend, or purchase any of its stock, if the effect would be to reduce the net worth of the Association below either the amount of the liquidation account or the net worth requirements of the Office of Thrift Supervision. To date no cash dividends have been paid. It has been the Association's policy to retain all earnings to fund additional growth.



**SUMMIT
SAVINGS**

11711 S.E. 8th Street
Bellevue, Washington 98005