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S T R A T E G I E S



Summit Savings *1991* Annual Report

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C O R P O R A T E  
P R O F I L E

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Summit Savings Bank is a state-chartered stock savings and loan association which was organized in 1981.

The Bank has recently applied to the regulators for conversion to a state-chartered stock savings bank and for approval of the formation of a bank holding company which will offer Summit greater flexibility for expansion. Summit Savings is located in Bellevue and serves the Puget Sound region from one office.

Total assets of the Bank were \$131.2 million at June 30, 1991. Shareholders' equity was \$10.2 million or 7.8% of total assets. The Bank offers consumers a full range of financial services and products. They include accepting deposits from the general public and making consumer loans and residential real estate loans. Summit's common stock trades over the counter on the NASDAQ national market system under the symbol SMMT.

FINANCIAL  
HIGHLIGHTS

<i>Dollars in thousands, except per share data</i>	1991	1990	1989
<i>At June 30</i>			
Total assets	\$131,232	\$113,339	\$109,970
Loans receivable and mortgage- backed securities	115,506	94,296	79,789
Deposits	93,959	81,586	80,267
Advances from Federal Home Loan Bank	11,600	7,600	9,600
Shareholders' equity	10,232	8,859	2,915
Book value per share	5.09	4.41	4.66
Shareholders' equity to assets	7.8%	7.8%	2.7%
<i>For the year ended June 30</i>			
Weighted average yield:			
Loans and mortgage- backed securities	10.27%	11.08%	10.58%
Cash and investments	7.46	8.32	8.29
Combined	9.97	10.54	10.33
Weighted average cost of funds:			
Deposits	7.66	8.55	8.17
Borrowings	9.60	9.99	9.93
Combined	8.08	8.89	8.59
Interest rate spread	1.89	1.65	1.74
Net interest margin	2.46	2.03	1.87
Net income (loss) before federal income tax expense and extraordinary item	\$ 1,485	\$ 553	\$ (1,629)
Federal income tax expense (benefit)	80		(477)
Extraordinary item, net of tax	39		
Net income (loss)	1,366	553	(1,152)
Net income (loss) per share	.68	.42	(1.84)
Real estate loans originated and purchased	161,401	100,638	41,063
Return on average assets	1.12%	.50%	(1.11)%
Return on average shareholders' equity	14.37	9.40	(32.99)

The twelve months ending June 30, 1991 saw continued earnings improvement by Summit Savings Bank. Net income for fiscal 1991 was a record \$1.4 million, an increase of 147% over \$553,000 for fiscal 1990. Per share performance improved to \$.68 compared with \$.42 per share in fiscal 1990. Earnings for our fourth fiscal quarter were an especially strong \$503,000 or \$.25 per share compared to \$239,000 or \$.12 per share for the same period last year. This marks the eighth consecutive increase in our quarterly earnings.

We are pleased to be able to report such strong earnings growth in a challenging economic, regulatory and competitive environment. Our performance resulted from a number of factors. We were fortunate in that the economy

of our market area remained solid, unlike many other parts of the country. Additionally, the Federal Reserve policy of lowering short-term interest rates helped us to improve our net interest margin, significantly contributing to an increase in net interest income of \$839,000 over fiscal 1991. An important component of our success has been the achievement of our mortgage banking business. Our loan production increased dramatically as did our loan sales. As a result, mortgage banking income increased 76% from \$1.1 million to \$2.0 million. There were many other factors contributing to our successful year. These are discussed in detail by our senior officers in the following section of this report.



*Return on Shareholders'*

*Equity, Percent : During*

*a year of continuing re-*

*structuring, we achieved*

*an ROE of more than 14%.*

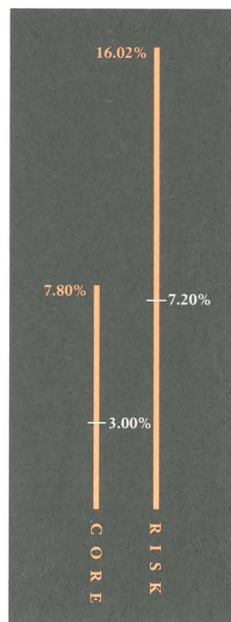


Our earnings provided additional capital allowing us to significantly increase our asset size. Assets at June 30, 1991 totaled \$131 million compared to \$113 million one year earlier, an increase of 16%. Our strong capital base allows us to continue expanding our existing business and to pursue any favorable acquisition opportunities.

In June the Board of Directors voted to convert Summit Savings Bank from a state-chartered savings and loan to a state-chartered savings bank. Additionally, the Board voted to form a bank holding company. We are taking these steps to provide greater flexibility in our expansion efforts and because we believe more options will be available to us in offering

financial services and products to our customers. We also believe that the market will attach a higher value to our franchise. We are hopeful of receiving prompt regulatory approval of our improved structure and expect to ask for shareholder approval at the annual meeting scheduled for November.

Fiscal 1991 recorded other accomplishments by your Bank. After receiving shareholder approval at last year's annual meeting, we changed our name to Summit Savings Bank. During the year, Bauer Financial Reports and Veribanc, Inc., independent companies which analyze and rate financial institutions in the United States, gave Summit their highest rating. The Office of Thrift



*Capital Ratios, Percent :*

*Both our Core and Risk-based capital far exceed regulatory requirements of 3.00% and 7.20%, respectively.*

Supervision gave the Bank an "Outstanding" rating in its most recent Community Reinvestment Act (CRA) examination, an important achievement for us as the regulators pay close attention to CRA ratings when evaluating an institution's growth plans. In July of last year, we began offering consumer loans. This new business line has been well received. To maintain and continually enhance the performance of your Bank, the Board of Directors and senior management have developed a strategic plan. In implementing this plan we hope to build on the improvement your Bank has already achieved.

All in all, fiscal 1991 was a very good year for Summit Savings Bank. We experienced

much good fortune which, when combined with careful planning and lots of hard work, is a solid formula for success. Achievement of a return of shareholders' equity of 14.37% during a year when we were still restructuring is especially gratifying.

It is obvious that those who are most responsible for the results of the past year are the members of our fine staff. We have built a top-notch team which we are very proud of and upon whom we depend for our continuing success. On behalf of the rest of the Board, we take this opportunity to sincerely thank them for a job well done. Our thanks also go out to our customers. Their confidence in Summit Savings is the true measure of our success.



*James F. Grabicki*

JAMES F. GRABICKI

*President and  
Chief Executive Officer*

*John D. Cadigan*

JOHN D. CADIGAN

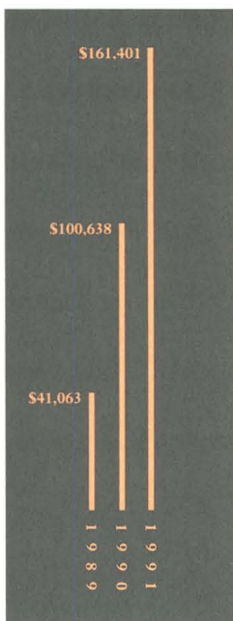
*Chairman of the Board*

*August 16, 1991*

# *S* T R A T E G I E S



*In early 1989 we began to restructure our lending strategy. Our focus changed from higher risk loans secured by income producing real estate to a more stable and conservative mortgage banking business specializing in home loans. Today, this transition has resulted in improved asset quality, much higher loan volumes and greater profitability. While our market, ranging from Pierce County in the south to Whatcom County in the north, maintains a strong and vibrant housing market, it also attracts significant competition both from local and out-of-state based companies. To remain competitive and achieve our goals of outstanding service and efficiency required that we completely automate our loan processing functions. A diversified system of loan originations was developed, including a Construction Loan Department specializing in financing new, affordable housing. Loan officers are assigned to each contractor and individual building project to provide financing alternatives to purchasers of these new homes. Our loan officers also call on the real estate community and various other professionals as resources for referral business. Additionally, loans originate through a network of experienced mortgage brokers who have earned our trust. This group submits fully processed loans, adding to Summit's volume without adding the overhead associated with more traditional methods of originations. Other loans originate through a loan purchase program*



*Loan Originations,*

*Dollars in thousands : Loan*

*originations increased 60%*

*during 1991 and 145%*

*during 1990, reflecting*

*effective lending strategies.*

*offered to a group of FHA approved correspondent lenders. These loans allow Summit even greater market penetration especially in the area of FHA/VA loan originations. We offer our customers a wide variety of mortgage programs that*

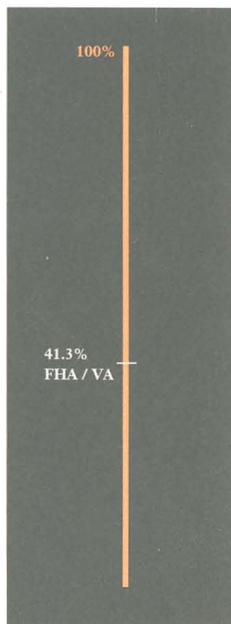
**GARY R. WILSON**

*Executive Vice President*

*Chief Lending Officer and oversees other areas of the Bank including  
Loan Servicing, Branch Operations, and Secondary Marketing.*

*range from fixed rate loans to adjustable rate mortgages. In addition, we participate in the Washington State Housing Bond Program and place a high emphasis on programs that target affordable housing*

*and first-time buyers. Our activities in these areas have earned an "Outstanding" rating by the Office of Thrift Supervision for Community Reinvestment. But Summit is only as good as the people it employs. We have been extremely fortunate in attracting a premier group of experienced professionals who are dedicated to providing the best service possible to our customers. An independent market study stated "The mortgage loan staff received excellent evaluations on their willingness to satisfy the customers' needs, friendliness, timeliness, updating information and overall satisfaction." Their dedication and hard work has helped make Summit Savings a leading home mortgage lender in the Puget Sound area. Summit will continue to capture greater market share by building on the strength, knowledge and commitment of our excellent staff.*



*FHA / VA Loans, Percent :*

*Affordable housing is vital.*

*In fiscal 1991, FHA and*

*VA loans accounted for more*

*than 41% of our total loan*

*originations.*









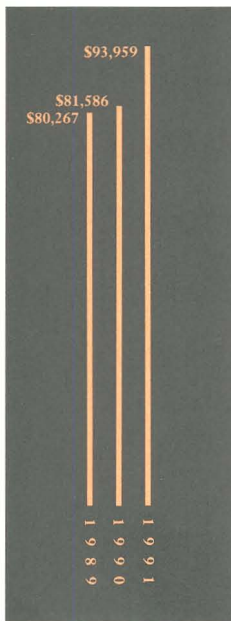
*In fiscal 1991, we substantially restructured our deposit mix. We have continued our effort to serve Summit deposit customers with new and better products. Improvement in products has lead to improvement in our base of*

**KATHY J. BURKE**

*Vice President of Savings Administration and Marketing  
and Director of Personnel.*

*core deposits. We began this fiscal year with \$81.6 million in deposits with a weighted average cost of 8.15% and ended the year with balances of \$94.0 million at 6.88%. These numbers are a direct re-*

*flection of the successful effort of our team of financial services professionals. They continue to provide consistently high customer service with solid expertise that gives us the ability to retain a very loyal client base while enhancing our ability to reach our goals. We have been fortunate to have experienced no turnover in our Financial Services staff throughout this fiscal year. This high degree of loyalty has contributed to increased efficiency in our systems and service. An independent marketing survey confirmed that we are reaching our goals. Respondents reported that the ease of opening an account and conducting ongoing business with Summit was very good, with an evaluation of 9.25 and 8.97, respectively, using a scale of 1-10. This high rating will serve to continually motivate the Financial Services personnel as they strive for greater efficiency and even higher levels of personal, prompt service. This*




*Deposit Growth, Dollars*

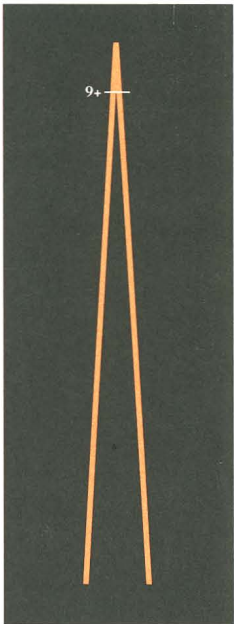
*in thousands : As deposits*

*grew to \$94 million, cost of*

*deposits decreased to 6.88%*

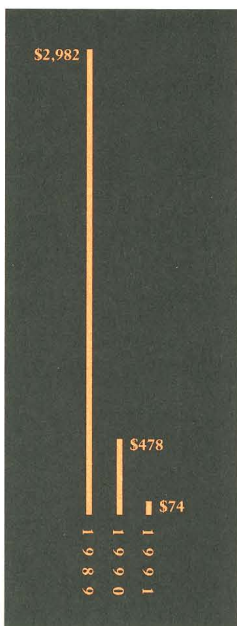
*at June 30, 1991.*

attitude and a carefully developed, competitive menu of accounts and services combine to meet the needs of the communities we serve, strengthening Summit's favorable market position. Programs are added or enhanced as we recognize a demand from our target markets. The senior community continues to be a vital segment, and Summit has remained in direct contact through sponsorship of local senior center activities, marketing special senior accounts and services and assigning Summit Representatives to provide personal service to these loyal and valued clients. Supporting the local senior center baseball teams and hosting their annual Halloween party has helped to keep our staff actively involved with these individuals and our community. To further broaden Summit services, consumer lending programs were introduced one year ago. These services continue to progress and have expanded to include Home Equity Lines of Credit, Second Mortgages, Auto Loans and Visa/MasterCard credit accounts. We are anticipating the addition of Recreational Vehicle and Boat Loans early in fall 1991. Our unique combination of financial strength and personable size are proving to be the right mix for both maintaining our loyal customers while attracting new customers. These attributes, together with our local management and ownership, have helped give Summit a favorable position in an environment that is as competitive as it is full of potential. 



An independently conducted marketing survey ranked our people better than 9 out of 10 on ease of opening an account and conducting ongoing business.

*Effectively monitoring and managing portfolio risk is essential in maintaining the health of any financial institution. In this time of federal re-regulation, one of the greatest challenges facing banks is in maintaining compliance with changing federal regulations. During fiscal 1991, Summit implemented a standard federal compliance policy to ensure adherence to state and federal laws, regulation, internal procedures and policies. Applying this policy calls for periodic reporting directly to the Board of Directors, supported by staff education classes. All written policies of the Bank are reviewed, updated and, when adopted by the Board of Directors, communicated directly to the staff. This comprehensive approach enables us to maintain our commitment to high asset quality as we continue to generate increasing levels of loan volume. As a direct result, problem loans and foreclosed properties that negatively impacted the Bank in past years have been substantially reduced. Summit's Real Estate Owned as of June 30, 1991 is \$74,000 compared to \$478,000 at June 30, 1990 and \$3.0 million at June 30, 1989. A healthy Northwest economy and a dedicated team effort combined with an effective internal asset classification system made this dramatic improvement possible. Assets are classified through an early detection and prevention system. Specified reserves are analyzed monthly in order to insure that properties*



*Real Estate Owned, Dollars*

*in thousands : REO was comprised of one single family property at June 30, 1991, down from \$ 2.98 million in 1989.*



*with potential losses have adequate reserves. In addition to specified reserves, Summit Savings analyzes the adequacy of its general reserves on a monthly basis. Funds are reserved in sufficient amounts, appropriately reflecting the level of risk*

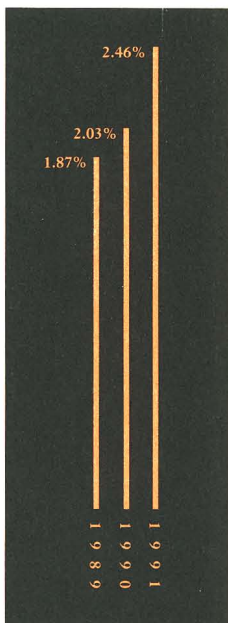
**M E R R I   A N N   S I M O N S O N**

*Vice President, Loan Administration*

*Loan servicing, regulatory compliance and special credits.*

*posed to the Bank based on historical experience of actual losses and management's evaluation of prevailing market conditions. Portfolio management requires an annual review of all income property*

*loans regardless of size. This includes review of all current operating statements, as well as a physical site inspection. Changes from the prior year are analyzed and property values are revised based on the current income approach. All files receive an internal rating and are classified in accordance with regulatory guidelines, if appropriate. Classified files receive priority monitoring until the problem is corrected. During the next fiscal year, the Servicing Department staff will continue its efforts to reduce both problem loans and Real Estate Owned resulting in improved asset quality. As the first line of contact with all our loan customers, the professionalism and efficiency of the Servicing Department goes a long way toward determining how Summit Savings Bank is perceived. Our focus will always remain on enhancing the reputation and profitability of your Bank.*



*Net Interest Margin,*

*Percent : The steady*

*increase in Net Interest*

*Margin is largely a result*

*of putting our non-earning*

*assets back to work.*







*Stay ahead of our competitors. Measure and manage risk. That is the purpose of the Asset/Liability Committee. Weekly meetings are held to review our mortgage banking activities, deposit gathering and product pricing. Interest rate*

**PATRICIA L. WALDOW**

*Vice President, Treasurer*

*Accounting, Data Processing and Secondary Marketing Departments,*

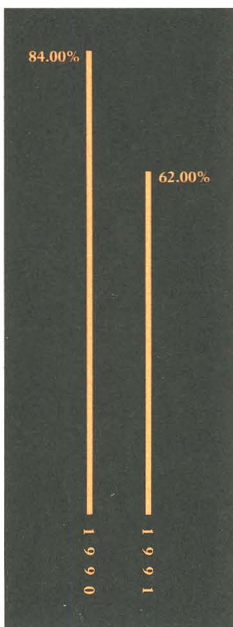
*Member of Asset/Liability Committee.*

*risk management and maintaining liquidity are the primary responsibilities of the Committee.*

*Rate risk is managed through a variety of financial instruments available to us, including adjustable rate*

*mortgages, interest rate swap transactions and Federal Home Loan Bank advances.*

*We monitor the Bank's sensitivity to interest rates in several ways; the difference between interest bearing assets and liabilities maturing and loan repricing, modeling projected changes in interest rates and calculating the change in the Bank's equity given instantaneous changes in interest rates. The combination of these methods provides management with current information needed to make accurate adjustments on an ongoing basis. The growth that we've experienced was possible in part because of increased internal efficiency and effectively utilizing the wide range of data supplied by newly implemented technology. Our Data Processing and Accounting Departments interact with all areas of the Bank, providing technical support and encouraging the innovative use of the systems available to us. Timely*

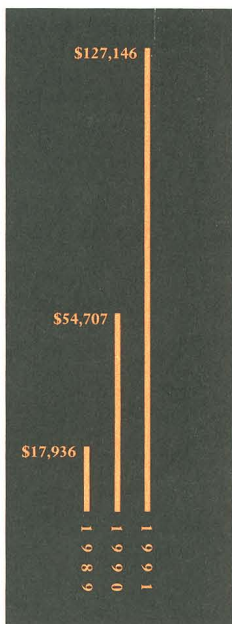


*Efficiency Ratio, Percent:*

*This ratio demonstrates the improvement Summit has made in reducing operating expenses as they relate to net revenues.*



and accurate data processing yields up to 400 monthly reports, enhancing the decision making process while maintaining our high level of customer service. Reporting extends from processing entries to regulatory reports and reports to shareholders. Careful attention is given to the development of accurate data used to assist management in keeping overhead expenses to a minimum -- one measure of success is our much improved efficiency ratio. Measuring and managing interest rate risk and the effect of interest rate changes on earnings, while continuing to provide competitive services, is our primary focus. One highly successful approach comes from our utilization of the Secondary Mortgage Market. Our Secondary Marketing Department sold \$127.1 million in loans in fiscal 1991, compared to \$54.7 million in fiscal 1990. This strategy minimizes the interest rate risk inherent in holding long-term fixed-rate mortgages while providing liquidity -- enhancing our ability to originate larger loan volumes with the additional cash provided by the sales. Our performance improvement of the past years has been extremely gratifying. As we strive to continue that trend, we anticipate the coming year to be just as challenging. In facing and overcoming those challenges, our department has assembled an outstanding group of professionals that work together, sharing their experience and acumen to maximize the opportunities that lie ahead. 🏡



Loan Sales, Dollars in  
thousands : 1991 loan sales  
hit an all-time high of  
\$127.1 million, providing  
liquidity for our successful  
mortgage banking operations.







Summit Savings Bank ("Summit" or "Association") is a Washington state-chartered stock savings and loan association serving the Puget Sound area of Washington. The administrative and branch facility is located in Bellevue, Washington. Summit has two wholly owned subsidiaries, Summit Services, Inc. and Summit Capital Corporation. Summit Services, Inc. discontinued the sale of life insurance and annuities in fiscal 1991 and currently serves to assist the existing client base for these products. Summit Capital Corporation is a finance subsidiary formed in fiscal 1988 to issue a collateralized mortgage obligation.

The Association is regulated, supervised and examined by the State of Washington, as well as by federal regulators. During 1989, the Financial Institutions Reform, Recovery and Enforcement Act (FIRREA) significantly altered the regulatory environment. FIRREA's key provisions replaced the Federal Home Loan Bank Board (FHLBB) with the Office of Thrift Supervision (OTS), abolished the Federal Savings and Loan Insurance Corporation (FSLIC), vested the prior insurance responsibilities of the FSLIC in the Federal Deposit Insurance Corporation (FDIC) and placed the Federal Home Loan Banks (FHLBs) under the jurisdiction of the Federal Housing Finance Board. As a result, Summit is now examined by the OTS, with oversight by the FDIC. Its deposits are insured by the FDIC under the Savings Association Insurance Fund.

In July 1991, the Association announced its intention to submit application to the State of Washington to convert its charter to a state-chartered savings bank. It was also announced that a bank holding company would be formed concurrently with the charter conversion. This structure will offer Summit greater flexibility for expansion. Under the Plan of Conversion and Plan of Reorganization, shareholders of Summit Savings will exchange their shares for an equal number of shares under the newly formed holding company. The proposed plan must be approved by shareholders, the Washington State Supervisor of Banking and the Office of Thrift Supervision.

Total assets of the Association increased to \$131.2 million at June 30, 1991, up 16% from \$113.3 million at June 30, 1990. Shareholders' equity increased from \$8.9 million at June 30, 1990 to \$10.2 million at June 30, 1991, due primarily to net income of \$1.4 million for the year.

#### *Lending and Investing Activities*

Summit's combined loans receivable held for investment and held for sale portfolios increased \$18.8 million or 26% to \$92.1 million at June 30, 1991. This was largely due to increased loan originations of \$161.4 million in fiscal 1991 compared to \$100.6 million in 1990. Mortgage-backed securities increased \$2.4 million, from \$21.0 million at June 30, 1990 to \$23.4 million at June 30, 1991.

Interest-bearing deposits decreased \$7.3 million during the year, from \$10.5 million to \$3.2 million at June 30, 1991 and 1990 respectively, as these funds were used to originate higher yielding mortgage loans. Debt securities increased \$4.9 million during the year, reflecting purchases of \$9.9 million, offset by sales and maturities of \$5.0 million during the year. Debt securities are generally used to add to the Association's regulatory liquidity and to diversify and enhance asset yield.

#### *Deposit and Borrowing Activities*

Deposits for the year increased \$12.4 million or 15%, to \$94.0 million at June 30, 1991. Jumbo certificates comprised 9.4% of the deposits. Summit has no brokered deposits.

Federal Home Loan Bank advances increased \$4.0 million to \$11.6 million at June 30, 1991 from \$7.6 million at June 30, 1990. Collateralized mortgage obligations decreased \$966,000 during the year in conjunction with principal reductions on the underlying securities.

## RESULTS OF OPERATIONS

Net income for the year ended June 30, 1991 was \$1,366,000, compared to \$553,000 at June 30, 1990 and a net loss of \$1,152,000 at June 30, 1989. An extraordinary item of \$39,000 for the year ended June 30, 1991 represents prepayment penalties, net of tax effect, on Federal Home Loan Bank advances.

Net interest income after provision for loan losses was \$2,816,000 at June 30, 1991 compared to \$1,977,000 and \$1,510,000 at June 30, 1990 and 1989 respectively. The 42% increase from 1990 to 1991 was due to large increases in volumes of loans originated and net purchases of mortgage-backed securities, partially offset by a decrease in interest-bearing deposits. Also contributing was the reduction in the combined cost of deposits and borrowings; 8.08% for the year ended June 30, 1991 compared to 8.89% for June 30, 1990. The \$467,000 increase in net interest income, after provision for loan losses, from June 30, 1989 to June 30, 1990 resulted primarily from increases in interest-bearing deposit balances resulting from the proceeds of the sale of additional stock, offset by decreases in loan and mortgage-backed security balances and increases in deposit balances.

Interest on loans and mortgage-backed securities increased \$1,621,000 from 1990 to 1991 and decreased \$86,000 from 1989 to 1990. The increase in fiscal 1991 is due to an increase in average balances of \$22.7 million, while the decrease in fiscal 1990 was due to a \$4.8 million decrease in average balances, slightly offset by an increase in interest yield, from 10.6% to 11.1%.

Interest income from interest-bearing deposits, debt securities and FHLB stock dividends decreased \$708,000 from 1990 to 1991 and increased \$802,000 from 1989 to 1990. The decrease during the year reflects both a decrease in overnight deposits as those funds were used to originate higher yielding mortgage loans and a decrease in average interest rates, from 8.32% for 1990 to 7.46% for 1991. The increase during the prior year was largely due to additional funds available in interest-bearing deposits due to the proceeds from the additional stock offering.

Interest expense on deposits decreased \$23,000 during the year and increased \$468,000 from June 30, 1989 to June 30, 1990. The decrease this year, in spite of an increase in total deposits of \$12.4 million, is the result of a reduction in cost of deposits from an average of 8.55% in fiscal 1990 to 7.66% in fiscal 1991. The increase during the prior fiscal year was due both to an increase of \$2.2 million in total deposits and a slight increase in average rates.

Interest expense on borrowings increased \$41,000 from June 30, 1990 to June 30, 1991 and decreased \$4,000 from June 30, 1989 to June 30, 1990. The increase during the year is due to an increase in average balances of \$1.2 million, offset by a reduction in average rates, from 9.99% to 9.60%. The \$4,000 decrease during the prior fiscal year was due to a decrease of \$205,000 in average balances, slightly offset by an increase in rates of 9.93% to 9.99%.

Other operating income increased \$846,000 from June 30, 1990 to June 30, 1991 and \$654,000 from June 30, 1989 to June 30, 1990. The increases this fiscal year and last fiscal year were primarily due to increases in mortgage banking activities resulting in additional gains on the sale of loans.

Other expense increased \$753,000 in fiscal 1991, from \$2.7 million at June 30, 1990 to \$3.5 million at June 30, 1991. Other expense decreased \$1.1 million from June 30, 1989 to June 30, 1990. Compensation increased \$520,000 for the fiscal year ended June 30, 1991 and decreased \$16,000 during the prior year. Primary factors for the increase were commissions expense on increased loan originations, management incentive compensation, increase in number of personnel and an adjustment of loan origination costs deferred.

Increases in occupancy expenses and data processing costs are attributable to added costs associated with increased production. Another factor in increased occupancy expense was the opening of a lending office in Bellingham, Washington in August 1990. This office was subsequently consolidated into



the main office in July 1991 after determining that the market could be served through the correspondent and wholesale lending programs. Insurance increased as a result of increased deposit insurance premiums.

Professional services increased \$53,000 during the past fiscal year ended June 30, 1991, primarily due to expenses associated with the charter conversion plan. The prior fiscal year ended June 30, 1990 reflected a decrease of \$38,000 over fiscal 1989.

In fiscal 1990, the tax bad debt deduction for fiscal 1987 was recalculated based upon interpretive rulings from the Internal Revenue Service. This resulted in \$1.8 million in additional tax losses which were carried forward and used to offset all book taxable income in fiscal 1990 and part in fiscal 1991. There are no additional loss carryforwards to offset future book taxable income. Federal income tax will be provided for at normal rates for the coming fiscal year.

## LIQUIDITY AND CAPITAL RESOURCES

The Association is required by applicable federal 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 was 8.7% and 13.9% for the months of June 1991 and 1990, respectively.

The principle sources of funds are principal and interest payments on mortgage loans and mortgage-backed securities, totaling \$19.6 million and \$36.5 million in fiscal 1991 and 1990, respectively, sale of loans in the secondary market, sales and maturities of debt securities, FHLB advances and deposits.

The Association's ability to continue to originate loans is dependent on its ability to sell loans in the secondary mortgage market. Most of the Association's new originations are underwritten, documented and priced for sale in the secondary market. Loan sales in fiscal 1991 and 1990 were \$126.8 million and \$56.0 million, respectively.

Capital increased approximately \$1.4 million in fiscal 1991, resulting primarily from net income of \$1,366,000 and \$7,000 from stock options exercised.

On November 6, 1989, the OTS issued a new regulation prescribing uniformly applicable capital standards for savings associations. The standards include a tangible capital requirement of 1.5% of adjusted total assets, a core capital requirement of 3% of adjusted tangible assets and a phased-in, risk-based capital requirement, which requires a risk-based capital level of 7.2% from December 31, 1990 to December 31, 1992 and 8% thereafter. At June 30, 1991, Summit exceeded the fully phased-in capital requirements by \$6.1 million. See Note M to the consolidated financial statements.

### *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 of the Association's assets.

During 1991, advances totaling \$6.0 million and bearing average interest rates of 8.81% were repaid as part of a restructuring strategy that included the sale of \$4.0 million in fixed-rate mortgage-backed securities. The result of the restructure was to reduce future cost of funds, increase liquidity and narrow the one-year asset liability gap.

Interest rate risk at June 30, 1991, as measured by calculating the dollar difference between liabilities and assets repricing or maturing over a one-year period is a negative 12%, within the acceptable ratio of 15% of assets established by the Board of Directors. Net interest margin is gradually but steadily increasing as a result of decreasing non-earning assets, restructuring the deposit mix and increasing total loans and mortgage-backed securities.

Board of Directors  
Summit Savings Bank  
400 112th Avenue N.E.  
Bellevue, WA 98004

We have audited the accompanying consolidated statements of financial condition of Summit Savings Bank and subsidiaries as of June 30, 1991 and 1990, and the related statements of operations, shareholders' equity and cash flows for the years then ended. These financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these financial statements based on our audits. The consolidated financial statements of Summit Savings Bank and subsidiaries for the year ended June 30, 1989 were audited by other auditors whose report, dated August 4, 1989, expressed an unqualified opinion on those financial statements and included a paragraph referring to the changes in accounting as described in Notes A and L to the financial statements.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial condition of Summit Savings Bank and subsidiaries as of June 30, 1991 and 1990, and the results of their operations and cash flows for the years then ended in conformity with generally accepted accounting principles.

*Deloitte & Touche*

*August 2, 1991  
Seattle, Washington*



CONSOLIDATED STATEMENTS  
OF FINANCIAL CONDITION

<i>June 30 / Dollars in thousands</i>	1991	1990
<i>Assets</i>		
Cash	\$ 711	\$ 1,186
Interest-bearing deposits	3,210	10,485
Debt securities	3,692	2,723
(Market value of \$3,557 and \$2,562)		
Mortgage-backed securities	23,441	19,004
(Market value of \$22,567 and \$17,887)		
Investments held for sale	3,955	2,005
(Market value of \$3,967 and \$2,010)		
Federal Home Loan Bank stock, at cost	928	1,186
Loans receivable, net:		
Held for investment	79,222	67,634
Held for sale	12,843	5,653
Accrued interest receivable	1,095	1,029
Real estate owned, net	74	478
Excess servicing premium on loan sales	1,179	1,088
Other assets	882	868
	<u>\$131,232</u>	<u>\$113,339</u>
<i>Liabilities</i>		
Deposits	\$ 93,959	\$ 81,586
Advances from Federal Home Loan Bank	11,600	7,600
Short-term borrowings	398	261
Collateralized mortgage obligations	12,400	13,366
Convertible subordinated debentures	521	521
Accrued interest payable	630	662
Other liabilities	1,492	484
	121,000	104,480
<i>Shareholders' equity</i>		
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 2,011,324 and 2,008,974 shares	20	20
Additional paid-in capital	8,323	8,316
Retained earnings	1,889	523
	10,232	8,859
	<u>\$131,232</u>	<u>\$113,339</u>

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS  
OF OPERATIONS

<i>Year ended June 30 / Dollars in thousands</i>	1991	1990	1989
Interest income:			
Loans receivable	\$ 9,231	\$ 7,907	\$ 8,036
Mortgage-backed securities	1,733	1,436	1,393
Interest-bearing deposits	513	1,346	234
Other	464	339	649
Total interest income	11,941	11,028	10,312
Interest expense:			
Deposits	6,609	6,632	6,164
Federal Home Loan Bank advances	944	791	750
Collateralized mortgage obligations	1,348	1,460	1,503
Other	60	60	62
Total interest expense	8,961	8,943	8,479
Net interest income	2,980	2,085	1,833
Provision for loan losses	164	108	323
Net interest income after provision for loan losses	2,816	1,977	1,510
Other income:			
Loan servicing income	436	479	280
Gain on sale of loans	1,543	646	135
Gain on sale of securities	38	32	
Other	147	161	249
	2,164	1,318	664
Other expense:			
Compensation and benefits	1,811	1,291	1,307
Occupancy	388	379	478
Insurance	213	196	184
Data processing	175	141	137
Professional services	214	161	199
Net cost of real estate owned	16	2	976
Other	678	572	522
	3,495	2,742	3,803
Income (Loss) before income taxes and extraordinary item	1,485	553	(1,629)
Provision (Benefit) for deferred federal income taxes	80		(477)
Income (Loss) before extraordinary item	1,405	553	(1,152)
Extraordinary item net of tax (Note I)	(39)		
Net income (loss)	\$ 1,366	\$ 553	\$ (1,152)
Earnings (Loss) per share:			
Net income (loss) before extraordinary item	\$ .70	\$ .42	\$ (1.84)
Extraordinary item	(.02)		
Net income (loss)	<u>\$ .68</u>	<u>\$ .42</u>	<u>\$ (1.84)</u>

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS  
OF SHAREHOLDERS' EQUITY

<i>Dollars in thousands</i>	<i>Number of Shares Outstanding</i>	<i>Common Stock</i>	<i>Additional Paid-in Capital</i>	<i>Retained Earnings (Deficit)</i>	<i>Total</i>
Balance at July 1, 1988	626	\$ 6	\$ 2,939	\$ 1,122	\$ 4,067
Net loss				(1,152)	(1,152)
Balance at June 30, 1989	626	6	2,939	(30)	2,915
Proceeds from sale of stock	1,380	14	5,364		5,378
Stock options exercised	3		13		13
Net income				553	553
Balance at June 30, 1990	2,009	20	8,316	523	8,859
Stock options exercised	2		7		7
Net income				1,366	1,366
Balance at June 30, 1991	<u>2,011</u>	<u>\$20</u>	<u>\$ 8,323</u>	<u>\$ 1,889</u>	<u>\$10,232</u>

See notes to consolidated financial statements.



**CONSOLIDATED STATEMENTS  
OF CASH FLOWS**

<i>Year ended June 30 / Dollars in thousands</i>	1991	1990	1989
<i>Operating activities:</i>			
Net income (loss)	\$ 1,366	\$ 553	\$ (1,152)
Adjustments to reconcile net income (loss) to net cash used by operating activities:			
Proceeds from sale of loans receivable	126,806	54,707	17,936
Loans originated, net of changes in loans in process	(162,436)	(94,301)	(53,008)
Amortization of fees, discounts and premiums, net	12	(685)	(43)
Gain on sale of assets, net	(209)	(54)	
Federal Home Loan Bank (FHLB) stock dividends	(212)	(115)	(126)
Excess servicing gains on loans sold	(312)	(54)	(11)
Increase in accrued interest receivable	(66)	(48)	(70)
Provisions for (recovery of) losses on loans and real estate owned	195	(10)	1,250
Net increase in other assets	(14)	(55)	(6)
Decrease in accrued interest payable	(32)	(32)	(57)
Increase (Decrease) in other liabilities	1,008	(1,032)	(452)
Net cash used by operating activities	(33,894)	(41,126)	(35,739)
<i>Investing activities:</i>			
Proceeds from debt securities sold and maturing	4,968	31,832	11,701
Purchase of debt securities	(9,858)	(22,965)	(18,968)
Purchase of FHLB stock	(8,245)		
Principal collected on mortgage- backed securities	1,644	1,335	873
Purchase of mortgage-backed securities	(15,888)	(7,262)	
Proceeds from sale of mortgage- backed securities	11,960	1,961	
Proceeds from sale of FHLB stock	8,715		
Principal collected on loans receivable	17,980	35,176	39,186
Purchase of loans	(1,073)	(5,776)	(262)
Proceeds from sale of real estate owned	495	2,666	514
Additions to real estate owned	(105)	(26)	(2,159)
Net cash provided by investing activities	10,593	36,941	30,885

*See notes to consolidated financial statements.*

CONSOLIDATED STATEMENTS  
OF CASH FLOWS

<i>Year ended June 30 / Dollars in thousands</i>	1991	1990	1989
<i>Financing activities:</i>			
Net increase (decrease) in demand deposits, NOW accounts and savings	\$ 935	\$ 1,925	\$ (3,941)
Net increase (decrease) in certificates of deposit	11,438	(606)	14,677
Proceeds from advances from Federal Home Loan Bank	23,000		15,000
Repayment of advances from Federal Home Loan Bank	(19,000)	(2,000)	(12,000)
Net increase (decrease) in short-term borrowings	137	(148)	139
Repayment of collateralized mortgage obligations	(966)	(682)	(638)
Net proceeds from issue of additional stock and exercise of stock options	7	5,391	
Net cash provided by financing activities	15,551	3,880	13,237
Increase (Decrease) in cash and cash equivalents	(7,750)	(305)	8,383
Cash and cash equivalents at beginning of year	11,671	11,976	3,593
Cash and cash equivalents at end of year	<u>\$ 3,921</u>	<u>\$11,671</u>	<u>\$11,976</u>
<i>Supplemental cash flow information:</i>			
Cash paid during the year:			
Interest	\$ 8,993	\$ 8,975	\$ 8,390
Federal income taxes	\$ 57	\$ 11	\$ 10

*See notes to consolidated financial statements.*

NOTE **A** SUMMARY OF SIGNIFICANT  
ACCOUNTING POLICIES

*Basis of Presentation:* The accompanying consolidated financial statements include Summit Savings Bank ("Association") and its wholly owned subsidiaries, Summit Services, Inc. and Summit Capital Corporation. All significant intercompany transactions and balances have been eliminated. Certain reclassifications have been made to the 1990 and 1989 financial statements to conform to the 1991 presentation.

*Debt Securities:* Debt securities are designated at the date of purchase as securities held for investment or securities held for sale. Securities held for investment are recorded at cost, net of discounts and premiums, which are amortized to maturity. Securities held for sale are recorded at the lower of aggregate cost or market. The cost of investments sold is computed using the specific identification method. At June 30, 1991 and 1990, the Association had the intent and ability to hold to maturity debt securities not specifically held for sale.

*Mortgage-Backed Securities:* Mortgage-backed securities are designated at date of purchase as securities held for investment or securities held for sale. Securities held for investment are recorded at cost less principal repayments. Securities held for sale are recorded at the lower of cost or market on an aggregate portfolio basis. At June 30, 1991 and 1990, the Association had the intent and ability to hold to maturity mortgage-backed securities not specifically held for sale.

*Loans Receivable and Interest Income:* Each loan receivable is designated, at the closing date, as a loan held for sale or as a portfolio loan. Loans held for sale are recorded at the lower of cost or market as determined by outstanding commitments from investors or current investor yield requirements calculated on an aggregate portfolio basis. Portfolio loans are stated at the principal amount outstanding, net of deferred fees and discounts.

Interest on loans is recorded as income is earned. If the collectibility of the interest is in doubt, the loan is placed on non-accrual status and accrued but unpaid interest is charged against current income.

*Reserve for Loan Losses:* A reserve for losses is provided for specific loans when any significant permanent decline in value is deemed to have occurred. The reserve is established by charges against operations in the period those losses are identified. This analysis includes determination of the existence and net realizable value of the collateral, principally through real estate appraisals or discounted cash flow analyses and guarantees securing such loans.

General loan loss reserves are established to provide for inherent loan portfolio risks not specifically provided for. The level of general reserves is based on analysis of potential exposures existing in the Association's loans held for investment portfolio including evaluation of identified risk factors, historical trends, current market conditions and other relevant factors.

The level of general and specific reserves is based on management's continuing evaluation of the pertinent factors underlying the quality of the loan portfolio, including actual loan loss experience and current and anticipated economic conditions.

*Loan Origination Fee Income:* Effective July 1, 1988, the Association implemented Statement of Financial Accounting Standards (SFAS) No. 91, "Accounting for Nonrefundable Fees and Costs Associated with Originating or Acquiring Loans and Initial Direct Costs of Leases," which changed the generally accepted accounting principles applicable to loan fees. Loan origination fees and certain direct loan origination costs are deferred and the net amount is amortized as an adjustment of the yield over the contractual life of the loan. This accounting change resulted in an estimated increase in pre-tax net loss of \$53,000 for the year ended June 30, 1989.

Prior to July 1, 1988, the Association recognized loan fees as current income at the time loans were originated to the extent they were a reimbursement of related origination costs. Excess fees, if any, were accounted for as an adjustment of the loan yield and recognized over the approximate average life of the loan.



*Excess Servicing Premium on Loan Sales:* Premiums on the sale of loans represent the present value of the portion of estimated future cash flows retained on loans sold (based upon certain prepayment assumptions and net of a normal servicing fee), which are recognized as gains on sale of loans at the time the sales occur. Premiums are amortized over the estimated life of the loan. During fiscal 1991, 1990 and 1989, amortization of such premiums totaled \$221,000, \$156,000 and \$408,000, respectively. Management periodically re-evaluates the recoverability of the recorded premium balance and the level of amortization.

*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 at the date of acquisition or the fair value which becomes the new cost basis. Any anticipated losses at the date of acquisition are recognized as loan losses prior to transfer to real estate owned. Any additional anticipated losses identified in subsequent ongoing analysis of the property are recorded in operations when identified and reflected as a reserve on real estate owned.

*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.

*Cash and Cash Equivalents:* Cash and cash equivalents include cash and interest-bearing overnight deposits. Overnight funds are held at the Federal Home Loan Bank or in federal funds sold to a member of the Federal Reserve system.

## NOTE B DEBT SECURITIES

The amortized cost and market values of investments in debt securities at June 30 were as follows (in thousands):

	<i>Amortized Cost</i>	<i>Unrealized Gains</i>	<i>Unrealized Losses</i>	<i>Market Value</i>
<i>1991</i>				
U.S. Government and Agency Securities	<u>\$3,692</u>	<u>\$ 7</u>	<u>\$ (142)</u>	<u>\$3,557</u>
<i>1990</i>				
U.S. Government and Agency Securities	<u>\$2,723</u>		<u>\$ (161)</u>	<u>\$2,562</u>

The amortized cost and market values of investments in debt securities at June 30, 1991, by contractual maturity are shown below (in thousands):

	<i>Amortized Cost</i>	<i>Market Value</i>
Due in one year or less	\$ 500	\$ 502
Due after one year through five years	1,980	1,985
Due after five years through ten years		
Due after ten years	1,212	1,070
	<u>\$3,692</u>	<u>\$3,557</u>

At June 30, 1991, debt securities held for investment totaling \$1.7 million were pledged as collateral for public deposits and customer repurchase accounts.

NOTE **C** MORTGAGE - BACKED SECURITIES

Mortgage-backed securities consisted of the following at June 30 (in thousands):

	<i>Amortized Cost</i>	<i>Unrealized Gains</i>	<i>Unrealized Losses</i>	<i>Market Value</i>
<i>1991</i>				
FNMA Certificates	\$ 3,706	\$ 7	\$ (10)	\$ 3,703
GNMA Certificates	4,871		(14)	4,857
FHLMC Certificates:				
Security for collateralized mortgage obligations	14,864		(857)	14,007
	<u>\$23,441</u>	<u>\$ 7</u>	<u>\$ (881)</u>	<u>\$22,567</u>
<i>1990</i>				
FNMA Certificates	\$ 2,177		\$ (10)	\$ 2,167
FHLMC Certificates:				
Security for collateralized mortgage obligations	15,824		(1,095)	14,729
Other	1,003		(12)	991
	<u>\$19,004</u>		<u>\$(1,117)</u>	<u>\$17,887</u>

NOTE **D** INVESTMENTS HELD FOR SALE

Investments held for sale consisted of the following at June 30 (in thousands):

	<i>Amortized Cost</i>	<i>Unrealized Gains</i>	<i>Unrealized Losses</i>	<i>Market Value</i>
<i>1991</i>				
U.S. Treasury Obligations	<u>\$ 3,955</u>	<u>\$12</u>		<u>\$ 3,967</u>
<p>Proceeds from sales of investments during fiscal year 1991 were \$15,928,000. Gains of \$195,000 and losses of \$3,000 were realized on sales of investments during 1991.</p>				
<i>1990</i>				
FNMA Adjustable Rate Certificates	<u>\$ 2,005</u>	<u>\$ 5</u>		<u>\$ 2,010</u>

Loans receivable at June 30 consisted of the following (in thousands):

	1991	1990
Loans on existing property:		
1-4 family	\$41,268	\$32,293
Multi-family	11,810	11,262
Commercial	11,995	12,730
Construction loans:		
1-4 family	10,606	9,738
Commercial	4,925	5,376
Land loans	747	1,325
Consumer loans	1,294	836
	82,645	73,560
Less:		
Deferred loan fees	(836)	(386)
Loans in process of completion	(2,002)	(5,119)
Reserve for loan losses	(585)	(421)
Loans receivable held for investment	79,222	67,634
Loans receivable held for sale:		
1-4 family	12,843	5,653
Total loans	<u>\$92,065</u>	<u>\$73,287</u>

The Association originates both adjustable and fixed interest rate mortgage loans. At June 30, 1991, the composition of loans held for investment was as follows (in thousands):

<i>Fixed Rate:</i>		<i>Adjustable Rate:</i>	
<i>Term to Maturity</i>	<i>Book Value</i>	<i>Term to Rate Adjustment</i>	<i>Book Value</i>
1 month - 1 year	\$ 963	1 month - 1 year	\$40,434
1 year - 3 years	1,699	1 year - 2 years	3,733
3 years - 5 years	1,144	2 years - 3 years	467
5 years - 10 years	2,151		
10 years - 20 years	2,290		
Over 20 years	29,764		
	<u>\$38,011</u>		<u>\$44,634</u>

The adjustable rate loans have interest rate adjustment limitations and are generally indexed to the one-year U.S. Treasury Bill rate. Future market factors may affect the correlation of the interest rate adjustment with the rates the Association pays on the short-term deposits that have been primarily utilized to fund these loans.

In the past, the Association has originated and purchased commercial real estate loans. These loans are considered by management to have somewhat greater risk of uncollectibility due to the dependency on income production or future development of the real estate.

Under the Financial Institution Reform, Recovery and Enforcement Act (FIRREA), aggregate commercial real estate loans may not exceed 400% of capital as determined under the capital standards provisions of FIRREA. FIRREA does not require divestiture of any loan that was lawful when it was originated. The Association does not exceed the limitation.

FIRREA limits real estate loans to one borrower to 15% of an Association's regulatory capital. Associations meeting fully phased-in capital standards may submit a written certification form to use transition



rules granting a phase-in of this regulation until December 31, 1991. The 15% limitation results in a dollar limitation of approximately \$1,671,000, which the Association exceeds with certain borrowers. Divestiture of these loans is not required; however, additional loans to these borrowers are not allowed until such time as their aggregate balance outstanding is below the 15% limitation.

An analysis of the reserve for loan losses follows (in thousands):

<i>For the year ended June 30,</i>	1991	1990	1989
Balance, beginning of year	\$421	\$375	\$752
Provision for losses	164	108	323
Write-offs		(62)	(700)
Balance, end of year	<u>\$585</u>	<u>\$421</u>	<u>\$375</u>

Loans serviced for the benefit of others totaled \$90,181,000, \$91,135,000 and \$99,929,000 at June 30, 1991, 1990 and 1989, respectively.

Loan commitments outstanding at June 30, 1991 were approximately \$22,195,000 of which \$20,672,000 were 15 to 30 year fixed rate commitments with rates ranging from 9.0% to 10.7%. The balance of the loan commitments are at rates which adjust to market at the time the loan is closed. Commitments to extend credit generally have fixed expiration dates. Since a portion of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. Prior to extending commitments, the Association evaluates each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained upon extension of credit is based on management's credit evaluation of the borrower. Collateral held includes residential and commercial properties. Substantially all of these commitments are sold forward into the secondary mortgage market.

The Association's primary lending focus is in the greater Puget Sound area. Commercial loans are collateralized by retail office buildings and a retirement facility.

#### NOTE **F** ACCRUED INTEREST RECEIVABLE

Accrued interest receivable at June 30 consisted of the following (in thousands):

	1991	1990
Debt securities	\$ 131	\$ 140
Mortgage-backed securities	289	280
Loans receivable	675	609
	<u>\$1,095</u>	<u>\$1,029</u>

#### NOTE **G** REAL ESTATE OWNED

Real estate owned at June 30 consisted of the following (in thousands):

	1991	1990
Real estate acquired through foreclosure		
or deed in lieu of foreclosure	\$ 102	\$ 942
Reserve for estimated losses	(28)	(464)
	<u>\$ 74</u>	<u>\$ 478</u>

An analysis of the reserve for losses on real estate owned follows (in thousands):

<i>For the year ended June 30,</i>	1991	1990	1989
Balance, beginning of year	\$ 464	\$1,019	\$ 174
Provision for (recovery of) losses, net	31	(118)	927
Write-offs	(467)	(437)	(82)
Balance, end of year	<u>\$ 28</u>	<u>\$ 464</u>	<u>\$1,019</u>

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

## NOTE DEPOSITS

Deposits at June 30 consisted of the following (in thousands):

		1991		1990	
	<i>Rate at June 30, 1991</i>	<i>Amount</i>	<i>Percent</i>	<i>Amount</i>	<i>Percent</i>
Non-interest checking	0.00%	\$ 1,100	1.2%	\$ 957	1.2%
Treasury, tax and loan deposits	0.00	27		61	.1
Checking with interest	4.00 - 4.75	1,618	1.7	1,571	1.9
Statement savings	4.75	406	.4	354	.4
Money market checking	4.25	7,667	8.2	6,941	8.5
		10,818	11.5	9,884	12.1
Certificates:					
	4.5 - 5.99	2,056	2.2	410	.5
	6.00 - 6.99	44,494	47.4	20	
	7.00 - 7.99	14,600	15.5	3,849	4.7
	8.00 - 8.99	19,658	20.9	59,438	72.9
	9.00 - 9.99	2,135	2.3	7,245	8.9
	10.00 - 10.99	98	.1	640	.8
	11.00 - 11.99	100	.1	100	.1
		83,141	88.5	71,702	87.9
		<u>\$93,959</u>	<u>100.0%</u>	<u>\$81,586</u>	<u>100.0%</u>

The weighted average rate of deposits at June 30, 1991 was 7.11%.

Certificate accounts as of June 30 will mature as follows (in thousands):

	1991		1990	
	<i>Amount</i>	<i>Percent</i>	<i>Amount</i>	<i>Percent</i>
Within one year	\$43,082	51.8%	\$32,105	44.8%
From one to two years	32,225	38.8	32,046	44.7
Thereafter	7,834	9.4	7,551	10.5
	<u>\$83,141</u>	<u>100.0%</u>	<u>\$71,702</u>	<u>100.0%</u>

Interest expense on deposits consisted of the following (in thousands):

<i>For the year ended June 30,</i>	1991	1990	1989
Checking	\$ 547	\$ 578	\$ 511
Statement savings	17	14	22
Certificates of deposit	6,045	6,040	5,631
	<u>\$6,609</u>	<u>\$6,632</u>	<u>\$6,164</u>

Accrued interest payable on deposits was \$227,000 and \$268,000 at June 30, 1991 and 1990.

Public funds of \$8,021,000 and \$8,649,000, included in deposits at June 30, 1991 and 1990, respectively, were collateralized by investment securities with book values of \$1,212,000 and \$1,220,000 and market values of \$1,070,000 and \$1,075,000 at June 30, 1991 and 1990, respectively.

#### NOTE I ADVANCES FROM FEDERAL HOME LOAN BANK

Advances from the Federal Home Loan Bank (FHLB) of Seattle at June 30 consisted of the following (in thousands):

<i>Payable During Year Ending June 30</i>	<i>Average Interest Rate at June 30, 1991</i>	1991	1990
1991			\$ 3,000
1992	7.62%	\$ 4,000	4,000
1993	7.58	2,600	600
1994	8.39	2,000	
1995	8.60	2,000	
1996	9.60	1,000	
		<u>\$11,600</u>	<u>\$ 7,600</u>

The weighted average rate on advances from FHLB at June 30, 1991 was 8.08%.

At June 30, 1991, the Association had outstanding commitments for \$5,000,000 of FHLB advances ranging from 18 months to 3 years in maturity and from 7.20% to 7.65% in interest rates. Advances are collateralized by mortgage loans with a book value of at least 155% of outstanding Bank advances and by FHLB stock with a recorded value of \$928,000.

An extraordinary item of \$39,000 net of \$10,000 income tax benefit for the year ended June 30, 1991 represents prepayment penalty paid on the repayment of \$6.0 million in Federal Home Loan Bank advances.

#### NOTE J SHORT - TERM BORROWINGS AND CONVERTIBLE SUBORDINATED DEBENTURES

Short-term borrowings consist of consumer repurchase agreements with interest rates of 4.0% at June 30, 1991 and 4.5% at June 30, 1990. The agreements are collateralized by investment securities with book values of \$500,000 and market values of \$502,000 and \$490,000 at June 30, 1991 and 1990, respectively.

During the years ended June 30, 1988 and 1987, the Association sold \$521,000 of 9.0% convertible subordinated debentures due December 31, 1996. The debentures are convertible at any time prior to maturity, unless previously redeemed, into 94,631 shares of common stock of the Association at the 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 and are not insured by the Federal Deposit Insurance Corporation.



NOTE **(K)** COLLATERALIZED  
MORTGAGE OBLIGATIONS

In June 1988 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 of \$14,870,000 as of June 30, 1991 and \$15,825,000 as of June 30, 1990. The mortgage-backed securities are held by a bond trustee for the benefit of the bondholders.

The bonds consisted of the following at June 30 (in thousands):

	<i>Interest Rate</i>	<i>Stated Maturity</i>	1991	1990
Sequence 1-A	9.70%	April 1, 2013	\$12,169	\$13,241
Sequence 1-Z	9.95	January 1, 2018	639	579
			12,808	13,820
Unamortized discount			(408)	(454)
			<u>\$12,400</u>	<u>\$13,366</u>

The net cash flow from the mortgage-backed securities, together with the reinvestment income thereon, provide for the proportionate repayment of the underlying bonds in quarterly installments. 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 (in thousands):

<i>Year ending June 30,</i>	
1992	\$ 680
1993	660
1994	642
1995	626
1996	610
Thereafter	9,590
	<u>\$12,808</u>

NOTE **(L)** FEDERAL INCOME TAXES

Effective for fiscal 1988, the Association elected early implementation of Statement of Financial Accounting Standards (SFAS) No. 96, Accounting for Income Taxes, under which the Association accounts for income taxes on the liability method. The liability method recognizes the amount of tax payable at the date of the financial statements as a result of all events that have been recognized in the financial statements, as measured by the provisions of currently enacted tax law and rates. The required implementation date of SFAS No. 96 has been delayed until fiscal 1993 to allow the Financial Accounting Standards Board additional time to reconsider the provisions of the Statement. It is presently unclear what final form the Statement will take; however, it does not appear that any significant modifications will be made which will impact the tax provision or liability recorded by the Association.

The Association files a consolidated federal income tax return. The Association qualifies under provisions of the Internal Revenue Code which permit as a deduction from taxable income an allowance for bad debts based on a percentage of taxable income or an experience method. The percentage bad debt deduction available was 8% for the years ended June 30, 1991, 1990 and 1989. The experience method provides financial institutions the ability to add to the reserve for losses on loans the greater of two computational alternatives: (1) the base year amount; or (2) the six-year moving average amount.

During the fiscal year ended June 30, 1990, certain interpretive rulings were issued by the Internal Revenue Service which allowed the thrift industry to calculate its experience method bad debt deduction in a more beneficial manner under the six-year moving average alternative. This alternative calculation was applied retroactively to the Association's 1987 taxable income and resulted in approximately \$1,753,000 in tax losses which were carried forward and used to offset all book taxable income for the year ended June 30, 1990 and \$945,000 of book taxable income for the year ended June 30, 1991. There are no remaining loss carryforwards available to offset future book taxable income.

Total net operating loss carryforwards for tax purposes available to offset future taxable income as of June 30, 1991 are as follows:

<i>Expiration Date</i>	<i>Amount</i>
2002	\$1,069,000
2004	309,000

Deferred federal income taxes result from temporary differences. Temporary differences are differences between the tax basis of assets and liabilities and their reported amounts on the 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, 1991 were approximately \$1,984,000.

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, 1991, 1990 and 1989 follows (in thousands):

	1991	1990	1989
Statutory rate	34%	34%	34%
Tax (Benefit) at statutory rate	\$ 488	\$ 188	\$(554)
Bad debt deduction based on experience method (net of minimum tax)	(16)	(3)	(376)
Loan loss and real estate owned reserve additions	64		425
Other		1	28
Benefit realized from net operating loss carryforward	(456)	(186)	
Provision (Benefit) for deferred federal income taxes before extraordinary item	80		(477)
Tax effect of extraordinary item	(10)		
Provision (Benefit) for deferred federal income taxes	<u>\$ 70</u>	<u>\$ 0</u>	<u>\$(477)</u>

The Association is required to maintain 60% in qualifying assets in order to use either the percentage or the experience method for bad debt deductions. The cumulative amount of tax basis bad debt reserves at June 30, 1991 totaled approximately \$2,446,000. If any portion of these amounts were to be subsequently used for purposes other than to absorb loan losses, these amounts would be subject to federal income taxes at the then prevailing corporate tax rate. The entire balance could also become taxable if the Association fails to maintain the percentage of qualifying asset level. It is not contemplated that such retained earnings will be used in any manner that would create a federal income tax liability and, therefore, no provision has been made for possible federal income taxes; however, the deferred liability for such deduction would approximate \$765,000.

Shareholders' equity in the consolidated financial statements differs from that reported to the OTS and is reconciled as follows (in thousands, regulatory capital unaudited):

	1991	1990
Shareholders' equity under generally accepted accounting principles	\$10,232	\$ 8,859
Qualifying subordinated debentures	370	448
Non-specified loss reserves	539	382
Regulatory capital	\$11,141	\$ 9,689

Under FIRREA, effective August 9, 1989, and the OTS regulatory capital regulations effective December 7, 1989, the Association is required to have tangible capital equal to 1.5% of adjusted total assets, core capital equal to 3% of adjusted total assets and total capital equal to increasing percentages (initially 6.4% increasing to 8.0% on December 31, 1992) of risk-weighted assets.

The Office of Thrift Supervision's regulatory capital regulations require that the portion of non-residential construction and land loans in excess of 80% loan-to-value ratio be deducted from total capital for purposes of the risk-based capital standard over a five-year phase-in period commencing July 1, 1990. It is not anticipated that this provision will materially impact the Association's risk-based capital calculation.

At June 30, 1991, the Association had the following capital ratios:

	<i>Requirement</i>	<i>Actual</i>	<i>Excess</i>
Tangible capital	\$ 1,968	\$10,232	\$ 8,264
Tangible capital to adjusted total assets	1.5%	7.8%	6.3%
Core capital	\$ 3,937	\$10,232	\$ 6,295
Core capital to adjusted total assets	3.0%	7.8%	4.8%
Risk-based capital	\$ 5,006	\$11,141	\$ 6,135
Risk-based capital to risk-weighted assets	7.2%	16.0%	8.8%

Summit Savings Bank, as long as it meets its fully phased-in capital requirements and requires only normal OTS supervision, may distribute up to 100% of net income earned to date during the current calendar year plus 50% of its capital surplus without prior OTS approval. To date, no cash dividends have been paid as it has been the Association's policy to retain all earnings to fund additional growth.

The Association's management believes that, under the current regulations, the Association will continue to meet its minimum capital requirements in the foreseeable future. However, events beyond the control of the Association, such as increased interest rates or a downturn in the economy in the area where the Association has most of its loans, could adversely affect future earnings and, consequently, the ability of the Association to meet its future minimum capital requirements.

At periodic intervals, both the OTS and the Federal Deposit Insurance Corporation (FDIC), and the Washington State Division of Savings and Loan Associations routinely examine the Association's financial statements as part of their legally prescribed oversight of the savings and loan industry. Based on these examinations, the regulators can direct that the Association's financial statements be adjusted in accordance with their findings.

A future examination by the OTS or the FDIC could include a review of certain transactions or other amounts reported in the Association's 1991 financial statements. The regulators have not proposed significant adjustments to the Association's financial statements in prior years. However, in view of FIRREA and the increasingly uncertain regulatory environment in which the Association now operates, the extent, if any, to which a forthcoming regulatory examination may ultimately result in adjustments to the 1991 financial statements cannot presently be determined.



## NOTE N LEASE COMMITMENTS

In June 1990, the Association entered into a seven-year lease for an administrative and branch facility consisting of 15,359 square feet on two floors of a Bellevue, Washington office building. There is an option to renew the lease for five years at market rates at date of renewal. Rent is payable as follows: \$20.00 per square foot for months 1-60 and \$23.00 per square foot for months 61-72.

Rent expense for the years ended June 30, 1991, 1990 and 1989 was approximately \$316,000, \$303,000 and \$334,000 respectively. Future minimum rental commitments at June 30, 1991 are as follows (in thousands):

<i>Year ending June 30,</i>	
1992	\$ 307
1993	307
1994	307
1995	311
1996	353
Thereafter	324
	\$1,909

## NOTE O 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, 169,485 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 June 30, 1995.

At June 30, 1991, 157,521 options were available for future grants under the Incentive Stock Plan. The price of options outstanding and the price of options exercisable ranged from \$2.90 to \$6.50. The price of options exercised in fiscal 1991 was \$3.19.

At the annual meeting held on November 8, 1990, shareholders approved a non-qualified stock option plan for non-employee directors. This plan provided for the grant of options to purchase 100,000 shares of common stock by non-employee directors. The price of the options outstanding and exercisable under this plan is \$3.69. None were exercised in fiscal 1991.

Changes in stock options are as follows:

	1991	1990
Outstanding beginning of fiscal year	104,764	42,827
Granted	14,000	65,200
Exercised	(2,350)	(3,000)
Expired	(6,800)	(263)
Outstanding June 30	109,614	104,764
Exercisable June 30	46,196	15,316

## NOTE P SUMMIT RETIREMENT PLAN

Effective July 1, 1989, the Association adopted a 401(k) retirement plan. All persons employed as of July 1, 1989 are eligible to participate. Thereafter, employees who have one year of service and have attained age 21 are eligible as of the entry date (July 1 or January 1) on or after which these requirements are met. The Association matches 25% of the employee contribution on the first 6% of compensation deferred. In

addition, the Association may make a discretionary contribution paid at fiscal year end and allocated to each employee in proportion to the compensation of all persons employed at that time. Employer contributions for the years ended June 30, 1991 and 1990 were \$46,000 and \$39,000, respectively.

#### NOTE Q INTEREST RATE RISK

The Association originates principally single-family permanent and construction loans. During fiscal 1991, approximately 85% of permanent loans originated were sold in the secondary market and were hedged against interest rate fluctuations with forward commitments from the time of loan commitment until the loans were sold.

All construction loans have variable interest rates that are tied to the prime interest rate. Approximately half of the total loan portfolio is comprised of loans with rates which adjust at least yearly to a market rate index.

The Association has been able to minimize interest rate risk by matching interest rate sensitive assets and liabilities within acceptable limits through short-term maturities, variable rates and forward commitments to sell loans.

In November 1990, the Association entered into two two-year interest rate swap agreements with the Federal Home Loan Bank. The purpose of these agreements is to lessen the Association's sensitivity to short-term liability rate changes. The Association pays fixed rates and receives variable rates which adjust quarterly. It is the intention of the Association to participate in the agreements for the entire term. The interest differential paid or received is recorded as an adjustment to current income. Interest rate swap agreements at June 30, 1991 consisted of the following:

<i>Notional Amount</i>	<i>Variable Rate Received</i>	<i>Fixed Rate Paid</i>
5,000,000	6.063%	8.31%
2,000,000	6.063%	8.38%

#### NOTE R PENDING CHARTER CONVERSION

In July 1991, the Board of Directors adopted a Plan of Conversion and Plan of Reorganization to convert from a Washington state-chartered stock savings and loan association to a Washington state-chartered bank and to concurrently form a bank holding company. It is believed that operating under this structure will offer greater flexibility for growth.

Under the Plan of Conversion, Summit will retain the name Summit Savings Bank and become a wholly owned subsidiary of the bank holding company. Under the Plan of Reorganization, shareholders of Summit Savings Bank will exchange their shares of common stock for an equal number of shares of the new holding company, which will thereafter own all of the outstanding shares of Summit Savings.

The proposed Plan of Conversion must be approved by Summit's shareholders, the Office of Thrift Supervision and the Washington State Supervisor of Banking.

## DIRECTORS



**James F. Grabicki**

*President and  
Chief Executive Officer  
Summit Savings Bank  
Age: 48  
Years as Director: 2*

**John D. Cadigan**

*Chairman of the Board  
President  
Rio Petrol, Inc.  
Vice President  
Campbell Investment Corporation  
Age: 51  
Years as Director: 2*

**William P. Newman**

*Executive Vice President  
Washington State Hotel  
and Motel Association  
Age: 55  
Years as Director: 3*

**Doug T. Mergenthaler**

*President  
Ashton Corporation  
Age: 42  
Years as Director: 5*

**Paul E. Nolan**

*President  
Nolan Development, Inc.  
Age: 54  
Years as Director: 10*



**L. Michael Riley**

*Financial Services Consultant  
and Investor  
Age: 52  
Years as Director: 1*

**William P. Hurme**

*Marketing Consultant  
Age: 49  
Years as Director: 10*

**James D. Huber**

*President  
ATCON Services, Inc.  
Age: 47  
Years as Director: 10*



# CORPORATE INFORMATION

## OFFICERS

James F. Grabicki  
*President*  
*Chief Executive Officer*

Gary R. Wilson  
*Executive Vice President*  
*Chief Lending Officer*

Kathy J. Burke  
*Vice President*  
*Savings Administration*

Merri Ann Simonson  
*Vice President*  
*Loan Administration*

Patricia L. Waldow  
*Vice President*  
*Treasurer*

Tammy Barnett  
*Assistant Vice President*  
*Lending Production Manager*

Lyn Godfrey  
*Assistant Vice President*  
*Wholesale Lending Manager*

Linda Larson  
*Assistant Vice President*  
*Wholesale Lending Operations Manager*

Katie Nelson  
*Assistant Vice President*  
*Data Processing Manager*

Barbara Tangeman  
*Assistant Vice President*  
*Branch Operations*

Theresa Stauch  
*Corporate Secretary*

## CORPORATE HEADQUARTERS

400 112th Avenue N.E.  
Bellevue, WA 98004  
(206) 451-3585  
1-800-824-6220 Washington only

## INDEPENDENT PUBLIC

ACCOUNTANTS  
Deloitte & Touche  
1111 Third Avenue  
Seattle, WA 98101

## GENERAL COUNSEL

Foster, Pepper & Shefelman  
1111 Third Avenue  
Seattle, WA 98101

## SPECIAL COUNSEL

Breyer & Zinski  
601 13th Street N.W.  
Suite 1120 South  
Washington, DC 20005

## 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

## COMMON STOCK

Summit Savings' common stock is traded in the over-the-counter market and is included in the National Market System of NASDAQ (symbol: SMMT). As of June 30, 1991, there were 2,011,324 shares of common stock outstanding held by approximately 1,500 shareholders including registered and beneficial owners.

The following table shows the high and low price range by quarter during the past two fiscal years.

### 1990

1st quarter (9-30-89)	\$ 6	\$ 4 3/4
2nd quarter (12-31-89)	6 1/2	4 1/2
3rd quarter (3-31-90)	5 1/4	4 5/8
4th quarter (6-30-90)	5 1/8	4 3/8

### 1991

1st quarter (9-30-90)	\$ 5 1/8	\$ 3 3/4
2nd quarter (12-31-90)	4 3/4	3 1/2
3rd quarter (3-31-91)	4 7/8	4
4th quarter (6-30-91)	7	4 5/8

## MARKET MAKERS

Some of the investment firms who make a market in Summit's stock are:

Dain Bosworth, Inc.  
Fahnestock & Co., Inc.  
Herzog, Heine, Geduld, Inc.  
Kemper Securities Group Inc.  
Piper, Jaffray & Hopwood, Inc.  
Ragen MacKenzie Inc.  
Troster Singer Corp.  
Wedbush Morgan Securities Inc.

## ANNUAL MEETING

The 1991 annual meeting of shareholders will be held at 7:00 p.m. on Thursday, November 7, 1991, at the Summit Building, 400 112th Avenue N.E., Bellevue, Washington. All shareholders are cordially invited to attend.

## FINANCIAL INFORMATION

Copies of Summit Savings' Annual Report to Shareholders, annual report on Form 10-K, Quarterly Reports, interim reports on Form 10-Q, and other published reports are available upon request and without charge. Please address requests to:

Corporate Secretary  
Summit Savings Bank  
400 112th Avenue N.E.  
Bellevue, WA 98004

## SHAREHOLDER INQUIRIES

First Interstate Bank, stock transfer agent for Summit Savings' stock, maintains all shareholder records and can assist you with address changes, corrections in social security or tax identification numbers and reissuance of stock certificates. If you need assistance with your Summit Savings stock, please contact the stock transfer agent at the address and phone number listed above.



