

META FINANCIAL GROUP INC

Form 10-Q

May 14, 2009

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**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

WASHINGTON, D.C. 20549

**FORM 10-Q**

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

**For the quarterly period ended March 31, 2009**

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

**For the transition period from                      to**

**Commission File Number: 0-22140**

**META FINANCIAL GROUP, INC. ®**

(Exact name of registrant as specified in its charter)

**Delaware**

(State or other jurisdiction of  
incorporation or organization)

**42-1406262**

(I.R.S. Employer Identification No.)

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**121 East Fifth Street, Storm Lake, Iowa 50588**

(Address of principal executive offices)

**(712) 732-4117**

(Registrant's telephone number, including area code)

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definition of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12-b2 of the Exchange Act. (Check one):

Large accelerated filer ☐

Accelerated filer ☐

Non-accelerated filer ☐

Smaller reporting company ☒

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class:  
Common Stock, \$.01 par value

Outstanding at May 12, 2009:  
2,602,655 Common Shares

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**META FINANCIAL GROUP, INC.**

**FORM 10-Q**

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Signatures

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(Dollars in Thousands, Except Share and Per Share Data)

|                                                                                                                                                                                        | March 31, 2009    | September 30, 2008 |
|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------|--------------------|
| <b>ASSETS</b>                                                                                                                                                                          |                   |                    |
| Cash and due from banks                                                                                                                                                                | \$ 1,644          | \$ 2,963           |
| Interest-bearing deposits in other financial institutions                                                                                                                              | 15,081            |                    |
| <b>Total cash and cash equivalents</b>                                                                                                                                                 | <b>16,725</b>     | <b>2,963</b>       |
| Federal funds sold                                                                                                                                                                     | 216               | 5,188              |
| Investment securities available for sale                                                                                                                                               | 14,482            | 19,711             |
| Mortgage-backed securities available for sale                                                                                                                                          | 321,057           | 184,123            |
| Loans receivable - net of allowance for loan losses of \$11,224 at March 31, 2009 and \$5,732 at September 30, 2008                                                                    | 419,275           | 427,928            |
| Federal Home Loan Bank Stock, at cost                                                                                                                                                  | 6,787             | 8,092              |
| Accrued interest receivable                                                                                                                                                            | 4,089             | 4,497              |
| Bond insurance receivable                                                                                                                                                              | 4,143             | 6,098              |
| Premises and equipment, net                                                                                                                                                            | 22,605            | 21,992             |
| Bank-owned life insurance                                                                                                                                                              | 13,016            | 12,758             |
| Foreclosed real estate and repossessed assets                                                                                                                                          | 3,755             |                    |
| Goodwill and intangible assets                                                                                                                                                         | 2,449             | 2,206              |
| MPS accounts receivable                                                                                                                                                                | 49,603            | 50,046             |
| Other assets                                                                                                                                                                           | 12,297            | 11,654             |
| <b>Total assets</b>                                                                                                                                                                    | <b>\$ 890,499</b> | <b>\$ 757,256</b>  |
| <b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>                                                                                                                                            |                   |                    |
| <b>LIABILITIES</b>                                                                                                                                                                     |                   |                    |
| Non-interest-bearing checking                                                                                                                                                          | \$ 485,655        | \$ 355,020         |
| Interest-bearing checking                                                                                                                                                              | 16,200            | 15,029             |
| Savings deposits                                                                                                                                                                       | 9,833             | 9,394              |
| Money market deposits                                                                                                                                                                  | 34,098            | 43,038             |
| Time certificates of deposit                                                                                                                                                           | 140,856           | 123,491            |
| <b>Total deposits</b>                                                                                                                                                                  | <b>686,642</b>    | <b>545,972</b>     |
| Advances from Federal Home Loan Bank                                                                                                                                                   | 100,950           | 132,025            |
| Securities sold under agreements to repurchase                                                                                                                                         | 22,259            | 5,348              |
| Subordinated debentures                                                                                                                                                                | 10,310            | 10,310             |
| Accrued interest payable                                                                                                                                                               | 744               | 578                |
| Contingent liability                                                                                                                                                                   | 4,293             | 4,293              |
| Accrued expenses and other liabilities                                                                                                                                                 | 17,148            | 11,923             |
| <b>Total liabilities</b>                                                                                                                                                               | <b>842,346</b>    | <b>710,449</b>     |
| <b>SHAREHOLDERS' EQUITY</b>                                                                                                                                                            |                   |                    |
| Preferred stock, 800,000 shares authorized, no shares issued or outstanding                                                                                                            |                   |                    |
| Common stock, \$.01 par value; 5,200,000 shares authorized, 2,957,999 shares issued, 2,602,655 and 2,601,103 shares outstanding at March 31, 2009 and September 30, 2008, respectively | 30                | 30                 |

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|                                                                                                                    |                   |                   |
|--------------------------------------------------------------------------------------------------------------------|-------------------|-------------------|
| Additional paid-in capital                                                                                         | 23,348            | 23,058            |
| Retained earnings - substantially restricted                                                                       | 36,689            | 35,516            |
| Accumulated other comprehensive (loss)                                                                             | (5,139)           | (5,022)           |
| Treasury stock, 355,344 and 356,896 common shares, at cost, at March 31, 2009 and September 30, 2008, respectively | (6,775)           | (6,775)           |
| <b>Total shareholders' equity</b>                                                                                  | <b>48,153</b>     | <b>46,807</b>     |
| <b>Total liabilities and shareholders' equity</b>                                                                  | <b>\$ 890,499</b> | <b>\$ 757,256</b> |

See Notes to Condensed Consolidated Financial Statements.

[Table of Contents](#)**META FINANCIAL GROUP, INC.****AND SUBSIDIARIES****Condensed Consolidated Statements of Operations (Unaudited)**

(Dollars in Thousands, Except Share and Per Share Data)

|                                                                    | <b>Three Months Ended<br/>March 31,</b> |               | <b>Six Months Ended<br/>March 31,</b> |               |
|--------------------------------------------------------------------|-----------------------------------------|---------------|---------------------------------------|---------------|
|                                                                    | <b>2009</b>                             | <b>2008</b>   | <b>2009</b>                           | <b>2008</b>   |
| Interest and dividend income:                                      |                                         |               |                                       |               |
| Loans receivable, including fees                                   | \$ 7,536                                | \$ 6,599      | \$ 13,908                             | \$ 12,877     |
| Mortgage-backed securities                                         | 2,797                                   | 2,339         | 4,805                                 | 3,846         |
| Other investments                                                  | 200                                     | 957           | 547                                   | 2,071         |
|                                                                    | 10,533                                  | 9,895         | 19,260                                | 18,794        |
| Interest expense:                                                  |                                         |               |                                       |               |
| Deposits                                                           | 1,429                                   | 2,031         | 2,973                                 | 4,455         |
| FHLB advances and other borrowings                                 | 860                                     | 1,648         | 1,882                                 | 2,849         |
|                                                                    | 2,289                                   | 3,679         | 4,855                                 | 7,304         |
| <b>Net interest income</b>                                         | <b>8,244</b>                            | <b>6,216</b>  | <b>14,405</b>                         | <b>11,490</b> |
| Provision for loan losses                                          | 10,270                                  | 200           | 12,399                                | 70            |
| <b>Net interest income (loss) after provision for loan losses</b>  | <b>(2,026)</b>                          | <b>6,016</b>  | <b>2,006</b>                          | <b>11,420</b> |
| Non-interest income:                                               |                                         |               |                                       |               |
| Card fees                                                          | 32,988                                  | 11,514        | 48,086                                | 16,957        |
| Loan fees                                                          | 231                                     | 207           | 330                                   | 405           |
| Deposit fees                                                       | 177                                     | 177           | 378                                   | 371           |
| Bank-owned life insurance income                                   | 131                                     | 124           | 258                                   | 246           |
| Gain on sale of securities available for sale, net                 | 9                                       | 198           | 9                                     | 207           |
| Other income                                                       | 75                                      | 65            | 85                                    | 229           |
| <b>Total non-interest income</b>                                   | <b>33,611</b>                           | <b>12,285</b> | <b>49,146</b>                         | <b>18,415</b> |
| Non-interest expense:                                              |                                         |               |                                       |               |
| Card processing expense                                            | 14,861                                  | 5,044         | 20,111                                | 8,101         |
| Compensation and benefits                                          | 8,342                                   | 6,451         | 15,781                                | 12,168        |
| Occupancy and equipment expense                                    | 2,049                                   | 1,795         | 3,853                                 | 3,040         |
| Legal and consulting expense                                       | 925                                     | 790           | 2,045                                 | 1,229         |
| Data processing expense                                            | 816                                     | 322           | 1,272                                 | 582           |
| Marketing                                                          | 474                                     | 394           | 812                                   | 738           |
| Other expense                                                      | 2,183                                   | 1,559         | 4,328                                 | 3,283         |
| <b>Total non-interest expense</b>                                  | <b>29,650</b>                           | <b>16,355</b> | <b>48,202</b>                         | <b>29,141</b> |
| <b>Income from continuing operations before income tax expense</b> | <b>1,935</b>                            | <b>1,946</b>  | <b>2,950</b>                          | <b>694</b>    |
| Income tax expense from continuing operations                      | 760                                     | 743           | 1,102                                 | 281           |
| <b>Income from continuing operations</b>                           | <b>1,175</b>                            | <b>1,203</b>  | <b>1,848</b>                          | <b>413</b>    |

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|                                                        |    |       |              |       |    |              |
|--------------------------------------------------------|----|-------|--------------|-------|----|--------------|
| Gain on sale from discontinued operations before taxes |    |       | 2,309        |       |    | 2,309        |
| Income from discontinued operations before taxes       |    |       | 4            |       |    | 76           |
| Income tax expense from discontinued operations        |    |       | 478          |       |    | 500          |
| <b>Income from discontinued operations</b>             |    |       | <b>1,835</b> |       |    | <b>1,885</b> |
| <b>Net Income</b>                                      | \$ | 1,175 | \$           | 3,038 | \$ | 1,848        |
|                                                        |    |       |              |       | \$ | 2,298        |
| <b>Basic earnings per common share:</b>                |    |       |              |       |    |              |
| Income from continuing operations                      | \$ | 0.45  | \$           | 0.47  | \$ | 0.71         |
| Income from discontinued operations                    |    |       |              | 0.71  |    | 0.73         |
| Net income                                             | \$ | 0.45  | \$           | 1.18  | \$ | 0.71         |
|                                                        |    |       |              |       | \$ | 0.89         |
| <b>Diluted earnings per common share:</b>              |    |       |              |       |    |              |
| Income from continuing operations                      | \$ | 0.45  | \$           | 0.46  | \$ | 0.71         |
| Income from discontinued operations                    |    |       |              | 0.70  |    | 0.71         |
| Net income                                             | \$ | 0.45  | \$           | 1.16  | \$ | 0.71         |
|                                                        |    |       |              |       | \$ | 0.87         |
| <b>Dividends declared per common share:</b>            | \$ | 0.13  | \$           | 0.13  | \$ | 0.26         |
|                                                        |    |       |              |       | \$ | 0.26         |

See Notes to Condensed Consolidated Financial Statements.



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**META FINANCIAL GROUP, INC.®**

**AND SUBSIDIARIES**

**Condensed Consolidated Statements of Comprehensive Income (Unaudited)**

(Dollars in Thousands)

|                                                                             | <b>Three Months Ended<br/>March 31,</b> |             | <b>Six Months Ended<br/>March 31,</b> |             |
|-----------------------------------------------------------------------------|-----------------------------------------|-------------|---------------------------------------|-------------|
|                                                                             | <b>2009</b>                             | <b>2008</b> | <b>2009</b>                           | <b>2008</b> |
| Net income                                                                  | \$ 1,175                                | \$ 3,038    | \$ 1,848                              | \$ 2,298    |
| Other comprehensive income (loss):                                          |                                         |             |                                       |             |
| Change in net unrealized gains (losses) on securities<br>available for sale | (1,243)                                 | 1,749       | (196)                                 | 3,800       |
| Gains realized in net income                                                | 9                                       | 198         | 9                                     | 207         |
|                                                                             | (1,234)                                 | 1,947       | (187)                                 | 4,007       |
| Deferred income tax effect                                                  | (460)                                   | 726         | (70)                                  | 1,495       |
| Total other comprehensive income (loss)                                     | (774)                                   | 1,221       | (117)                                 | 2,512       |
| Total comprehensive income                                                  | \$ 401                                  | \$ 4,259    | \$ 1,731                              | \$ 4,810    |

See Notes to Condensed Consolidated Financial Statements.

[Table of Contents](#)**META FINANCIAL GROUP, INC.®****AND SUBSIDIARIES****Condensed Consolidated Statements of Changes in Shareholders' Equity (Unaudited)****For the Six Months Ended March 31, 2009 and 2008**

(Dollars in Thousands, Except Share and Per Share Data)

|                                                                                            | Common<br>Stock | Additional<br>Paid-in<br>Capital | Retained<br>Earnings | Accumulated<br>Other<br>Comprehensive<br>(Loss),<br>Net of Tax | Unearned<br>Employee<br>Stock<br>Ownership<br>Plan Shares | Treasury<br>Stock | Total<br>Shareholders'<br>Equity |
|--------------------------------------------------------------------------------------------|-----------------|----------------------------------|----------------------|----------------------------------------------------------------|-----------------------------------------------------------|-------------------|----------------------------------|
| Balance, September 30, 2007                                                                | \$ 30           | \$ 21,958                        | \$ 36,805            | \$ (3,345)                                                     | \$ (377)                                                  | \$ (6,973)        | \$ 48,098                        |
| Cash dividends declared on common stock<br>(\$ .26 per share)                              |                 |                                  | (668)                |                                                                |                                                           |                   | (668)                            |
| Issuance of 3,967 common shares from<br>treasury stock due to exercise of stock<br>options |                 | 10                               |                      |                                                                |                                                           | 78                | 88                               |
| Stock compensation                                                                         |                 | 224                              |                      |                                                                |                                                           |                   | 224                              |
| 6,378 common shares committed to be<br>released under the ESOP                             |                 | 107                              |                      |                                                                | 217                                                       |                   | 324                              |
| Change in net unrealized losses on securities<br>available for sale, net                   |                 |                                  |                      | 2,512                                                          |                                                           |                   | 2,512                            |
| Net income for six months ended March 31,<br>2008                                          |                 |                                  | 2,298                |                                                                |                                                           |                   | 2,298                            |
| Balance, March 31, 2008                                                                    | \$ 30           | \$ 22,299                        | \$ 38,435            | \$ (833)                                                       | \$ (160)                                                  | \$ (6,895)        | \$ 52,876                        |
| Balance, September 30, 2008                                                                | \$ 30           | \$ 23,058                        | \$ 35,516            | \$ (5,022)                                                     | \$                                                        | \$ (6,775)        | \$ 46,807                        |
| Cash dividends declared on common stock<br>(\$ .26 per share)                              |                 |                                  | (675)                |                                                                |                                                           |                   | (675)                            |
| Stock compensation                                                                         |                 | 290                              |                      |                                                                |                                                           |                   | 290                              |
| Change in net unrealized losses on securities<br>available for sale, net                   |                 |                                  |                      | (117)                                                          |                                                           |                   | (117)                            |
| Net income for six months ended March 31,<br>2009                                          |                 |                                  | 1,848                |                                                                |                                                           |                   | 1,848                            |
| Balance, March 31, 2009                                                                    | \$ 30           | \$ 23,348                        | \$ 36,689            | \$ (5,139)                                                     | \$                                                        | \$ (6,775)        | \$ 48,153                        |

See Notes to Condensed Consolidated Financial Statements.



Table of Contents**META FINANCIAL GROUP, INC.®****AND SUBSIDIARIES****Condensed Consolidated Statements of Cash Flows (Unaudited)**

(Dollars in Thousands)

|                                                                                             | <b>Six Months Ended March 31,</b> |                 |
|---------------------------------------------------------------------------------------------|-----------------------------------|-----------------|
|                                                                                             | <b>2009</b>                       | <b>2008</b>     |
| <b>Cash flows from operating activities:</b>                                                |                                   |                 |
| Net income                                                                                  | \$ 1,848                          | \$ 2,298        |
| Adjustments to reconcile net income to net cash provided by (used in) operating activities: |                                   |                 |
| Effect of contribution to employee stock ownership plan                                     |                                   | 324             |
| Depreciation, amortization and accretion, net                                               | 1,983                             | 1,545           |
| Provision for loan losses                                                                   | 12,399                            | 70              |
| Gain on sale of other                                                                       | (48)                              | (52)            |
| Net change in accrued interest receivable                                                   | 408                               | 289             |
| Net change in other assets                                                                  | 1,254                             | (1,741)         |
| Net change in accrued interest payable                                                      | 166                               | (82)            |
| Net change in accrued expenses and other liabilities                                        | 5,225                             | (20,176)        |
| Net cash provided by (used in) operating activities-continuing operations                   | 23,235                            | (17,525)        |
| Net cash provided by operating activities-discontinued operations                           |                                   | 6,029           |
| <b>Net cash provided by (used in) operating activities</b>                                  | <b>23,235</b>                     | <b>(11,496)</b> |
| <b>Cash flow from investing activities:</b>                                                 |                                   |                 |
| Purchase of securities available for sale                                                   | (156,114)                         | (102,790)       |
| Net change in federal funds sold                                                            | 4,972                             | 75,000          |
| Proceeds from sales of securities available for sale                                        | 903                               |                 |
| Proceeds from maturities and principal repayments of securities available for sale          | 23,040                            | 15,725          |
| Loans purchased                                                                             | (7,054)                           | (7,313)         |
| Net change in loans receivable                                                              | (408)                             | (41,348)        |
| Proceeds from sales of foreclosed real estate                                               |                                   | 329             |
| Net change in Federal Home Loan Bank stock                                                  | 1,305                             | (3,555)         |
| Proceeds from the sale of premises and equipment                                            | 1                                 | 97              |
| Purchase of premises and equipment                                                          | (2,309)                           | (3,759)         |
| Other, net                                                                                  | 70                                | (1,208)         |
| Net cash used in investing activities-continuing operations                                 | (135,594)                         | (68,822)        |
| Net cash provided by investing activities-discontinued operations                           |                                   | 17,598          |
| <b>Net cash used in investing activities</b>                                                | <b>(135,594)</b>                  | <b>(51,224)</b> |
| <b>Cash flows from financing activities:</b>                                                |                                   |                 |
| Net change in checking, savings, and money market deposits                                  | 123,305                           | 87,297          |
| Net change in time deposits                                                                 | 17,365                            | (16,352)        |
| Net change in advances from Federal Home Loan Bank                                          | (31,075)                          | (13,000)        |
| Net change in securities sold under agreements to repurchase                                | 16,911                            | 81,990          |
| Cash dividends paid                                                                         | (675)                             | (668)           |
| Stock compensation                                                                          | 290                               | 312             |
| Net cash provided by financing activities-continuing operations                             | 126,121                           | 139,579         |
| Net cash used in financing activities-discontinued operations                               |                                   | (33,210)        |
| <b>Net cash provided by provided by financing activities</b>                                | <b>126,121</b>                    | <b>106,369</b>  |

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|                                                                              |    |        |    |        |
|------------------------------------------------------------------------------|----|--------|----|--------|
| <b>Net change in cash and cash equivalents</b>                               |    | 13,762 |    | 43,649 |
| Cash and cash equivalents at beginning of period                             |    | 2,963  |    | 20,903 |
| Cash and cash equivalents at end of period                                   | \$ | 16,725 | \$ | 64,552 |
| <b>Supplemental disclosure of cash flow information</b>                      |    |        |    |        |
| Cash paid during the period for:                                             |    |        |    |        |
| Interest                                                                     | \$ | 4,689  | \$ | 7,984  |
| Income taxes                                                                 |    | 2,055  |    |        |
| <b>Supplemental schedule of non-cash investing and financing activities:</b> |    |        |    |        |
| Loans transferred to foreclosed real estate                                  | \$ | 3,775  | \$ | 301    |
| Cash received on sale of commercial bank                                     |    |        |    | 8,224  |

See Notes to Condensed Consolidated Financial Statements.

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**META FINANCIAL GROUP, INC. ®**

**AND SUBSIDIARIES**

Notes to Condensed Consolidated Financial Statements (Unaudited)

**NOTE 1. BASIS OF PRESENTATION**

The interim unaudited condensed consolidated financial statements contained herein should be read in conjunction with the audited consolidated financial statements and accompanying notes to the consolidated financial statements for the fiscal year ended September 30, 2008 included in Meta Financial Group, Inc.'s (the "Company") Annual Report on Form 10-K filed with the Securities and Exchange Commission on December 12, 2008. Accordingly, footnote disclosures, which would substantially duplicate the disclosure contained in the audited consolidated financial statements, have been omitted.

The financial information of the Company included herein has been prepared in accordance with U.S. generally accepted accounting principles for interim financial reporting and has been prepared pursuant to the rules and regulations for reporting on Form 10-Q and Rule 10-01 of Regulation S-X. Such information reflects all adjustments (consisting of normal recurring adjustments), that are, in the opinion of management, necessary for a fair presentation of the financial position and results of operations for the periods presented. The results of the interim period ended March 31, 2009, are not necessarily indicative of the results expected for the year ending September 30, 2009.

**NOTE 2. DISCONTINUED BANK OPERATIONS**

**Sale of MetaBank West Central**

On November 29, 2007, the Company entered into an agreement to sell MetaBank West Central ("MetaBank WC"). On March 28, 2008 the Company consummated the sale of MetaBank WC to Anita Bancorporation (Iowa). MetaBank WC had three offices in Stuart, Casey, and Menlo, Iowa and was a state chartered commercial bank whose primary federal regulator is the Federal Reserve Bank of Chicago. The transaction involved the sale of the stock of MetaBank WC for approximately \$8.2 million and generated a pre-tax gain on sale of \$2.3 million. The activity related to Meta Bank WC is accounted for as discontinued operations.

Activities related to discontinued bank operations have been recorded separately with prior period amounts reclassified as discontinued operations on the condensed consolidated statements of operations and cash flows. The notes to the condensed consolidated financial statements have also been adjusted to eliminate the effect of discontinued bank operations.

**NOTE 3. ALLOWANCE FOR LOAN LOSSES**

At March 31, 2009 the Company's allowance for loan losses was \$11.2 million, an increase of \$5.5 million from \$5.7 million at September 30, 2008. During the six months ended March 31, 2009 the Company recorded a provision for loan losses of \$12.4 million. \$7.4 million related to the Company's Meta Payment Systems® (MPS) division and the start-up and completion of loan originations offered in collaboration with MPS tax preparation partner. In addition to the Company's loss provision, the contractual arrangement with this partner provides for substantial, but not full, credit loss protection mechanisms which the Company does not foresee the need to utilize during the current fiscal year due to satisfactory portfolio performance. During the six months ended March 31, 2009 the Company also recorded a provision for loan losses in the amount of \$5.0 million due to two commercial borrowers, one of which the Company believes committed fraud. As disclosed in the Company's 8-K filing of October 8, 2008, a borrower of the Bank has likely participated in a fraud on the Bank

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and other banks. Based on the Bank's investigation at that time, it concluded that, as of September 30, 2008, it was appropriate to establish an allowance for loan losses of \$1.8 million. After subsequent review was completed on April 20, 2009, the Bank concluded that a \$1.3 million increase to the loan loss allowance was warranted, primarily due to lower collateral values caused in large part by weaker economic conditions. Potential total losses range from \$2.1 million to \$4.2 million with an expected loss of \$3.1 million. The allowance was recorded during the three months ended March 31, 2009.

During the three months ended March 31, 2009, the Company recorded a provision for loan losses in the amount of \$6.1 million primarily related to the MPS tax loan portfolio and \$4.2 million related to the two commercial borrowers. The Company's total net charge-offs for the three months ended March 31, 2009 were \$6.8 million. Further discussion of this change in the allowance is included in Non-performing Assets and Allowance for Loan Loss in Management's Discussion and Analysis.



Table of Contents**NOTE 4. EARNINGS PER COMMON SHARE ( EPS )**

Basic EPS is computed by dividing income available to common shareholders (the numerator) by the weighted average number of common shares outstanding (the denominator) during the period. Shares issued during the period and shares reacquired during the period are weighted for the portion of the period that they were outstanding. Diluted EPS shows the dilutive effect of additional common shares issuable pursuant to stock option agreements.

A reconciliation of the income and common stock share amounts used in the computation of basic and diluted EPS for the three and six months ended March 31, 2009 and 2008 is presented below.

| <b>Three Months Ended March 31,<br/>(Dollars in Thousands, Except Share and Per Share Data)</b> | <b>2009</b> | <b>2008</b> |
|-------------------------------------------------------------------------------------------------|-------------|-------------|
| <b>Earnings</b>                                                                                 |             |             |
| Income from continuing operations                                                               | \$ 1,175    | \$ 1,203    |
| Discontinued operations, net of tax                                                             |             | 1,835       |
| Net income                                                                                      | \$ 1,175    | \$ 3,038    |
| <b>Basic EPS</b>                                                                                |             |             |
| Weighted average common shares outstanding                                                      | 2,602,655   | 2,595,165   |
| Less weighted average unallocated ESOP and nonvested shares                                     | (5,000)     | (19,334)    |
| Weighted average common shares outstanding                                                      | 2,597,655   | 2,575,831   |
| <b>Earnings Per Common Share</b>                                                                |             |             |
| Income from continuing operations                                                               | \$ 0.45     | \$ 0.47     |
| Discontinued operations, net of tax                                                             |             | 0.71        |
| Net income                                                                                      | \$ 0.45     | \$ 1.18     |
| <b>Diluted EPS</b>                                                                              |             |             |
| Weighted average common shares outstanding for basic earnings per common share                  | 2,597,655   | 2,575,831   |
| Add dilutive effect of assumed exercises of stock options, net of tax benefits                  |             | 44,634      |
| Weighted average common and dilutive potential common shares outstanding                        | 2,597,655   | 2,620,465   |
| <b>Earnings Per Common Share</b>                                                                |             |             |
| Income from continuing operations                                                               | \$ 0.45     | \$ 0.46     |
| Discontinued operations, net of tax                                                             |             | 0.70        |
| Net income                                                                                      | \$ 0.45     | \$ 1.16     |

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Six Months Ended March 31,  
(Dollars in Thousands, Except Share and Per Share Data)

|                                                                                | 2009      | 2008      |
|--------------------------------------------------------------------------------|-----------|-----------|
| <b>Earnings</b>                                                                |           |           |
| Income from continuing operations                                              | \$ 1,848  | \$ 413    |
| Discontinued operations, net of tax                                            |           | 1,885     |
| Net income                                                                     | \$ 1,848  | \$ 2,298  |
| <b>Basic EPS</b>                                                               |           |           |
| Weighted average common shares outstanding                                     | 2,602,655 | 2,593,860 |
| Less weighted average unallocated ESOP and nonvested shares                    | (5,000)   | (19,758)  |
| Weighted average common shares outstanding                                     | 2,597,655 | 2,574,102 |
| <b>Earnings Per Common Share</b>                                               |           |           |
| Income from continuing operations                                              | \$ 0.71   | \$ 0.16   |
| Discontinued operations, net of tax                                            |           | 0.73      |
| Net income                                                                     | \$ 0.71   | \$ 0.89   |
| <b>Diluted EPS</b>                                                             |           |           |
| Weighted average common shares outstanding for basic earnings per common share | 2,597,655 | 2,574,102 |
| Add dilutive effect of assumed exercises of stock options, net of tax benefits |           | 64,231    |
| Weighted average common and dilutive potential common shares outstanding       | 2,597,655 | 2,638,333 |
| <b>Earnings Per Common Share</b>                                               |           |           |
| Income from continuing operations                                              | \$ 0.71   | \$ 0.16   |
| Discontinued operations, net of tax                                            |           | 0.71      |
| Net income                                                                     | \$ 0.71   | \$ 0.87   |

Stock options totaling 34,395 and 39,933 were not considered in computing diluted EPS for the three and six months ended March 31, 2009, respectively, because they were not dilutive. Stock options totaling 125,018 were not considered in computing diluted EPS for the three months ended March 31, 2008 because they were not dilutive. Stock options totaling 111,018 and 6,000 were not considered in computing diluted EPS for the six months ended March 31, 2008 and 2007, respectively, because they were not dilutive.

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**NOTE 5. COMMITMENTS AND CONTINGENCIES**

At March 31, 2009 and September 30, 2008, the Company had outstanding commitments to originate and purchase loans totaling \$52.3 million and \$64.2 million, respectively. It is expected that outstanding loan commitments will be funded with existing liquid assets. At March 31, 2009, the Company had no commitments to purchase or sell securities available for sale.

**Legal Proceedings**

*First Federal Bank Littlefield Texas ssb, formerly known as First Federal Savings and Loan Association, Littlefield, Texas v. MetaBank, formerly known as First Federal Savings Bank of the Midwest, filed in the 154th Judicial District Court of Lamb County (Cause No. 17435); The Frost National Bank v. MetaBank and Meta Financial Group, Inc., filed in the United States District Court for the Northern District of Texas (Cause No. 3:08-CV-625-M).* On April 3, 2008, First Federal Bank filed suit against MetaBank in Texas State Court in Lubbock seeking recovery of a purported MetaBank certificate of deposit (CD) that it claims it purchased. On April 11, 2008, Frost National Bank filed suit against MetaBank in the United States District Court for the District of Texas seeking a similar recovery. However, this suit has since been dismissed without prejudice. On June 25, 2008, an action was filed in the 95th Judicial District Court for Dallas County, Texas entitled *Methodist Hospitals of Dallas v MetaBank and Meta Financial Group* seeking recovery of a purported MetaBank CD purchased in May, 2001. Additionally, on July 14, 2008, a class action complaint was filed in the United States District Court for the District of New Hampshire entitled *Guardian Angel Credit Union v MetaBank* (Cause No. 08-CV-261-PB) and was filed on behalf of Guardian Angel Credit Union and all other CD purchasers similarly situated, to recover funds in connection with purported MetaBank CDs. Further, on November 18, 2008, Coreplus Federal Credit Union (Cause No. 3.08 cv 1763 AVC) filed a civil action in the Superior Court for New London County in the state of Connecticut seeking recovery of funds connected to a purported MetaBank CD. Since the last filing, a subrogation action has been filed in the U.S. District Court, Northern District of Illinois, entitled *St. Paul Mercury Insurance Company, as assignee and subrogee of Lemont National Bank v- MetaBank, individually and as successor in interest to First Federal Savings Bank of the Midwest, (Case 1:09-cv-01031)*. In addition, the matter of *Hamilton Federal Credit Union-v- MetaBank*, (CV 09 1059) has been filed in the U.S. District Court for the Northern District of California. Recently, a related action was filed in the District Court, 7th Judicial District, State of Idaho, *East Idaho Credit Union v- MetaBank* (CV -2008-0007801). These cases arose after MetaBank was contacted by another institution, but could find no record of the CD it had allegedly purchased, and commenced an investigation. As a result of that investigation, it appears that a former MetaBank employee had been selling fraudulent CDs, using MetaBank's name and a form of CD, to various financial institutions through an independent broker and instructing purchasers to wire the purchase money into one of a number of false accounts she had created at MetaBank. The Bank has received a number of demands from purchasers of these fraudulent CDs in addition to the lawsuits listed above. All evidence currently available indicates that the former employee ran this fraud for her own benefit and regularly took money from the MetaBank accounts to which the purchase monies had been wired. As a result of the interruption of this fraud, there are some \$4.2 million of bogus CDs still outstanding to various financial institutions. As the former employee was apparently using the funds of new victims to pay off the previous victims of her scheme, it does not appear at this time that she stole any Bank money as part of this fraud. MetaBank therefore does not appear at this time to have suffered any direct loss as a result of the fraud, but it may suffer a loss to the extent it is exposed to liability for claims such as these. There are unresolved questions as whether, under what theory and to what degree the Bank might be liable for the former employee's actions. At this time, MetaBank's insurer has agreed to provide a defense to the litigation filed under a reservation of rights.

Other than the matters set forth above, there are no other material pending legal proceedings to which the Company or its subsidiaries is a party other than ordinary routine litigation to their respective businesses.

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**NOTE 6. STOCK OPTION PLAN**

The Company maintains the 2002 Omnibus Incentive Plan, which, among other things, provides for the awarding of stock options and nonvested (restricted) shares to certain officers and directors of the Company. Awards are granted by the Stock Option Committee of the Board of Directors based on the performance of the award recipients or other relevant factors.

In accordance with SFAS No. 123(R), compensation expense for share based awards is recorded over the vesting period at the fair value of the award at the time of grant. The exercise price of options or fair value of nonvested shares granted under the Company's incentive plans is equal to the fair market value of the underlying stock at the grant date. The Company assumes no projected forfeitures on its stock based compensation, since actual historical forfeiture rates on its stock based incentive awards has been negligible.

A summary of option activity for the six months ended March 31, 2009 is presented below:

|                                                         | Number<br>of<br>shares | Weighted<br>Average<br>Exercise<br>Price | Weighted<br>Average<br>Remaining<br>Contractual<br>Term (Yrs) | Aggregate<br>Intrinsic<br>Value |
|---------------------------------------------------------|------------------------|------------------------------------------|---------------------------------------------------------------|---------------------------------|
| (Dollars in Thousands, Except Share and Per Share Data) |                        |                                          |                                                               |                                 |
| Options outstanding, September 30, 2008                 | 514,328                | \$ 23.85                                 | 7.53                                                          | \$ 329                          |
| Granted                                                 | 23,000                 | 14.77                                    |                                                               |                                 |
| Exercised                                               |                        |                                          |                                                               |                                 |
| Forfeited or expired                                    | (500)                  | 22.05                                    |                                                               |                                 |
| Options outstanding, March 31, 2009                     | 536,828                | \$ 23.46                                 | 7.14                                                          | \$ 58                           |
| Options exercisable, March 31, 2009                     | 409,970                | \$ 22.23                                 | 6.98                                                          | \$ 1                            |

A summary of nonvested share activity for the six months ended March 31, 2009 is presented below:

|                                                         | Number<br>of<br>Shares | Weighted<br>Average<br>Fair Market Value<br>At Grant |
|---------------------------------------------------------|------------------------|------------------------------------------------------|
| (Dollars in Thousands, Except Share and Per Share Data) |                        |                                                      |
| Nonvested shares outstanding, September 30, 2008        | 12,500                 | \$ 32.93                                             |
| Granted                                                 | 5,200                  | 16.00                                                |
| Vested                                                  | (5,200)                | 16.00                                                |
| Forfeited or expired                                    |                        |                                                      |
| Nonvested shares outstanding, March 31, 2009            | 12,500                 | \$ 32.93                                             |

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As of March 31, 2009, stock based compensation expense not yet recognized in income totaled \$474,100 which is expected to be recognized over a weighted average remaining period of 1.01 years.

Table of Contents**NOTE 7. SEGMENT INFORMATION**

An operating segment is generally defined as a component of a business for which discrete financial information is available and whose results are reviewed by the chief operating decision-maker. Operating segments are aggregated into reportable segments if certain criteria are met. The Company has determined that it has two reportable segments. The first reportable segment, Traditional Banking, consists of its banking subsidiary, MetaBank. MetaBank operates as a traditional community bank providing deposit, loan and other related products to individuals and small businesses, primarily in the communities where their offices are located. The second reportable segment, Meta Payment Systems® ( MPS ), is a division of MetaBank. MPS provides a number of products and services, to financial institutions and other businesses. These products and services include issuance of prepaid debit cards, sponsorship of ATMs into the debit networks, credit programs, ACH origination services, gift card programs, rebate programs, travel programs and tax related programs. Other programs are in the process of development. The remaining grouping under the caption All Others consists of the operations of Meta Financial Group, Inc. and Meta Trust Company® and inter-segment eliminations. MetaBank WC is accounted for as discontinued bank operations. It is reported as part of the traditional banking segment and has been separately classified to show the effect of continuing operations. Transactions between affiliates, the resulting revenues of which are shown in the intersegment revenue category, are conducted at market prices, meaning prices that would be paid if the companies were not affiliates. The following tables present segment data for the Company for the three and six months ended March 31, 2009 and 2008, respectively.

|                                                     | <b>Traditional<br/>Banking(1)</b> | <b>Meta Payment<br/>Systems®</b> | <b>All Others</b> | <b>Total</b> |
|-----------------------------------------------------|-----------------------------------|----------------------------------|-------------------|--------------|
| <b>Three Months Ended March 31, 2009</b>            |                                   |                                  |                   |              |
| Interest income                                     | \$ 7,126                          | \$ 3,378                         | \$ 29             | \$ 10,533    |
| Interest expense                                    | 1,864                             | 271                              | 154               | 2,289        |
| Net interest income (loss)                          | 5,262                             | 3,107                            | (125)             | 8,244        |
| Provision for loan losses                           | 4,173                             | 6,097                            |                   | 10,270       |
| Non-interest income                                 | 584                               | 33,009                           | 18                | 33,611       |
| Non-interest expense                                | 4,781                             | 24,455                           | 414               | 29,650       |
| Income (loss) from continuing operations before tax | (3,108)                           | 5,564                            | (521)             | 1,935        |
| Income tax expense (benefit)                        | (1,167)                           | 2,092                            | (165)             | 760          |
| Income (loss) from continuing operations            | \$ (1,941)                        | \$ 3,472                         | \$ (356)          | \$ 1,175     |
| Inter-segment revenue (expense)                     | \$ 2,203                          | \$ (2,203)                       | \$                | \$           |
| Total assets                                        | 384,175                           | 504,704                          | 1,620             | \$ 890,499   |
| Total deposits                                      | 220,535                           | 466,487                          | (380)             | \$ 686,642   |

(1) For the three months ended March 31, 2009 there was no information to report on MetaBank WC.

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|                                                     | Traditional<br>Banking(1) | Meta Payment<br>Systems® | All Others | Total    |
|-----------------------------------------------------|---------------------------|--------------------------|------------|----------|
| <b>Three Months Ended March 31, 2008</b>            |                           |                          |            |          |
| Interest income                                     | \$ 5,792                  | \$ 3,698                 | \$ 405     | \$ 9,895 |
| Interest expense                                    | 2,723                     | 472                      | 484        | 3,679    |
| Net interest income (loss)                          | 3,069                     | 3,226                    | (79)       | 6,216    |
| Provision for loan losses                           | 200                       |                          |            | 200      |
| Non-interest income                                 | 693                       | 11,528                   | 64         | 12,285   |
| Non-interest expense                                | 4,449                     | 11,588                   | 318        | 16,355   |
| Income (loss) from continuing operations before tax | (887)                     | 3,166                    | (333)      | 1,946    |
| Income tax expense (benefit)                        | (157)                     | 1,009                    | (109)      | 743      |
| Income (loss) from continuing operations            | \$ (730)                  | \$ 2,157                 | \$ (224)   | \$ 1,203 |
| Inter-segment revenue (expense)                     | \$ 1,448                  | \$ (1,448)               | \$         | \$       |
| Total assets                                        | 457,923                   | 349,610                  | 3,002      | 810,535  |
| Total deposits                                      | 258,721                   | 335,202                  |            | 593,923  |

|                                                | West Central |
|------------------------------------------------|--------------|
| <b>Three Months Ended March 31, 2008</b>       |              |
| Net interest income                            | \$ 91        |
| Provision for loan losses                      | (21)         |
| Non-interest income                            | 2,346        |
| Non-interest expense                           | 145          |
| Income from discontinued operations before tax | 2,313        |
| Income tax expense                             | 478          |
| Income from discontinued operations            | \$ 1,835     |
| Inter-segment revenue                          | \$ 83        |
| Total assets                                   |              |
| Total deposits                                 |              |

|                                                     | Traditional<br>Banking(1) | Meta Payment<br>Systems® | All Others | Total     |
|-----------------------------------------------------|---------------------------|--------------------------|------------|-----------|
| <b>Six Months Ended March 31, 2009</b>              |                           |                          |            |           |
| Interest income                                     | \$ 12,997                 | \$ 6,205                 | \$ 58      | \$ 19,260 |
| Interest expense                                    | 3,887                     | 630                      | 338        | 4,855     |
| Net interest income (loss)                          | 9,110                     | 5,575                    | (280)      | 14,405    |
| Provision for loan losses                           | 5,023                     | 7,376                    |            | 12,399    |
| Non-interest income                                 | 972                       | 48,133                   | 41         | 49,146    |
| Non-interest expense                                | 9,649                     | 37,866                   | 687        | 48,202    |
| Income (loss) from continuing operations before tax | (4,590)                   | 8,466                    | (926)      | 2,950     |
| Income tax expense (benefit)                        | (1,696)                   | 3,122                    | (324)      | 1,102     |
| Income (loss) from continuing operations            | \$ (2,894)                | \$ 5,344                 | \$ (602)   | \$ 1,848  |
| Inter-segment revenue (expense)                     | \$ 4,076                  | \$ (4,076)               | \$         | \$        |
| Total assets                                        | 384,175                   | 504,704                  | 1,620      | 890,499   |
| Total deposits                                      | 220,535                   | 466,487                  | (380)      | 686,642   |

(1) For the six months ended March 31, 2009 there was no information to report on MetaBank WC.





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|                                                     | Traditional<br>Banking | Meta Payment<br>Systems® | All Others | Total      |
|-----------------------------------------------------|------------------------|--------------------------|------------|------------|
| <b>Six Months Ended March 31, 2008</b>              |                        |                          |            |            |
| Interest income                                     | \$ 11,260              | \$ 6,892                 | \$ 642     | \$ 18,794  |
| Interest expense                                    | 5,748                  | 615                      | 941        | 7,304      |
| Net interest income (loss)                          | 5,512                  | 6,277                    | (299)      | 11,490     |
| Provision for loan losses                           | 70                     |                          |            | 70         |
| Non-interest income                                 | 1,276                  | 17,038                   | 101        | 18,415     |
| Non-interest expense                                | 8,604                  | 20,116                   | 421        | 29,141     |
| Income (loss) from continuing operations before tax | (1,886)                | 3,199                    | (619)      | 694        |
| Income tax expense (benefit)                        | (631)                  | 1,119                    | (207)      | 281        |
| Income (loss) from continuing operations            | \$ (1,255)             | \$ 2,080                 | \$ (412)   | \$ 413     |
| Inter-segment revenue (expense)                     | \$ 2,671               | \$ (2,671)               | \$         | \$         |
| Total assets                                        | 457,923                | 349,610                  | 3,002      | \$ 810,535 |
| Total deposits                                      | 258,721                | 335,202                  |            | \$ 593,923 |

|                                                | West Central |
|------------------------------------------------|--------------|
| <b>Six Months Ended March 31, 2008</b>         |              |
| Net interest income                            | \$ 262       |
| Provision for loan losses                      | (57)         |
| Non-interest income, including gain on sale    | 2,440        |
| Non-interest expense                           | 374          |
| Income from discontinued operations before tax | 2,385        |
| Income tax expense                             | 500          |
| Income from discontinued operations            | \$ 1,885     |
| Inter-segment revenue (expense)                | \$ 175       |
| Total assets                                   |              |
| Total deposits                                 |              |

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**NOTE 8. NEW ACCOUNTING PRONOUNCEMENTS**

In June 2006 the FASB issued FASB Interpretation No. 48, ( FIN No. 48 ), *Accounting for Uncertainty in Income Taxes*, an Interpretation of Statement No. 109, *Accounting for Income Taxes*. FIN No. 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN No. 48 was effective for the Company on October 1, 2007. As a result of the adoption and implementation of FIN No. 48, the Company determined that no liability for unrecognized tax benefits existed at October 1, 2007. There have been no changes to this amount since adoption.

At its September 2006 meeting, the Emerging Issues Task Force ( EITF ) reached a final consensus on Issue No. 06-04, *Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements*. The consensus stipulates that an agreement by an employer to share a portion of the proceeds of a life insurance policy with an employee during the postretirement period is a postretirement benefit arrangement required to be accounted for under Statement No. 106 ( SFAS No. 106 ) or Accounting Principles Board ( APB ) Opinion No. 12, *Omnibus Opinion - 1967*. The consensus concludes that the purchase of a split-dollar life insurance policy does not constitute a settlement under SFAS No. 106 and, therefore, a liability for the postretirement obligation must be recognized under SFAS No. 106 if the benefit is offered under an arrangement that constitutes a plan or under APB No. 12 if it is not part of a plan. The Company implemented Issue No. 06-04 beginning October 1, 2008 with no impact on the Company's financial position, results of operation or cash flows.

In September 2006, the FASB issued Statement No. 157, ( SFAS No. 157 ), *Fair Value Measurements*. SFAS No. 157 defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. It clarifies that fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants in the market in which the reporting entity transacts. SFAS No. 157 does not require any new fair value measurements, but rather, it provides enhanced guidance to other pronouncements that require or permit assets or liabilities to be measured at fair value. The Company adopted SFAS No. 157 beginning October 1, 2008 with no material impact on the Company's financial position, results of operation or cash flows.

In February 2007, the FASB issued FASB Statement No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities - Including an Amendment of FASB Statement No. 115* ( SFAS No. 159 ). SFAS No. 159 permits companies to choose to measure many financial instruments and certain other items at fair value that are not currently required to be measured at fair value. The objective of SFAS No. 159 is to provide opportunities to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply hedge accounting principles. SFAS No. 159 also establishes presentation and disclosure requirements designed to facilitate comparisons between companies that choose different measurement attributes for similar types of assets and liabilities. The Company adopted SFAS No. 159 beginning October 1, 2008 with no material impact on the Company's financial position, results of operation or cash flows.

At its March 2007 meeting, the EITF reached a final consensus on Issue No. 06-10, *Accounting for Collateral Assignment Split-Dollar Life Insurance Arrangements*. A consensus was reached that an employer should recognize a liability for the postretirement benefit related to a collateral assignment split-dollar life insurance arrangement in accordance with either FASB Statement No. 106 or APB Opinion No. 12, as appropriate, if the employer has agreed to maintain a life insurance policy during the employee's retirement or provide the employee with a death benefit based on the substantive agreement with the employee. A consensus also was reached that an employer should recognize and measure an asset based on the nature and substance of the collateral assignment split-dollar life insurance arrangement. The consensus is effective for the Company beginning October 1, 2008, including interim periods within those fiscal years, with early application permitted. Implementation of Issue No. 06-10 did not have an impact on the Company's financial position, results of operation or cash flows.



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In December 2007, the FASB issued FASB Statement No. 141R, *Business Combinations* ( SFAS No. 141R ). SFAS No. 141R improves reporting by creating greater consistency in the accounting and financial reporting of business combinations, resulting in more complete, comparable, and relevant information for investors and other users of financial statements. SFAS No. 141R is effective July 1, 2009. The Company is currently evaluating the impact that the Statement will have on its consolidated financial statements.

In December 2007, the FASB issued FASB Statement No. 160, *Noncontrolling Interests in Consolidated Financial Statements an amendment of ARB No. 51* ( SFAS No. 160 ) which is effective for the Company beginning July 1, 2009. SFAS 160 improves the relevance, comparability, and transparency of financial information provided to investors by requiring all entities to report noncontrolling (minority) interest in subsidiaries in the same way as equity in the consolidated financial statements. The Company does not currently have any noncontrolling interest in the consolidated financial statements.

In March 2008, the FASB issued FASB Statement No. 161, *Disclosures about Derivative Instruments and Hedging Activities* ( SFAS No. 161 ). SFAS No. 161 is intended to improve financial reporting about derivative instruments and hedging activities by requiring enhanced disclosures to enable investors to better understand their effects on an entity's financial position, financial performance, and cash flows. The Company adopted SFAS 161 effective January 1, 2009. Management has reviewed SFAS No. 161 and does not expect the adoption of this statement to have a material impact on the Company's consolidated financial condition, results of operations or cash flow.

In May 2008, the FASB issued FASB Statement No. 162, *The Hierarchy of Generally Accepted Accounting Principles* ( SFAS No. 162 ). SFAS No. 162 makes the hierarchy explicitly and directly applicable to preparers of financial statements, a step that recognizes preparers responsibilities for selecting the accounting principles for their financial statements. SFAS No. 162 provides for slight modifications to the current hierarchy in place by adding FASB Staff Positions, Statement No. 133 Implementation Issues and EITF D-Topics to it. The Company adopted SFAS No. 162 effective November 15, 2008.

In April 2009, the FASB issued FASB Staff Position FAS 157-4, *Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly* ( FSP FAS 157-4 ). FSP FAS 157-4 provides additional guidance for estimating fair value in accordance with SFAS No. 157, when the volume and level of activity for the asset or liability have significantly decreased. FSP FAS 157-4 also provides guidance on identifying circumstances that indicate a transaction is not orderly. FSP FAS 157-4 is effective for financial statements issued after June 15, 2009. The adoption of FSP FAS 157-4 will not have a significant effect on the Company's consolidated financial statements.

In April 2009, the FASB issued FASB Staff Position FAS 115-2 and FAS 124-2, *Recognition and Presentation of Other-Than-Temporary Impairments* ( FSP FAS 115-2 and FAS 124-2 ). FSP FAS 115-2 and FAS 124-2 amends the other-than-temporary impairment guidance in U.S. GAAP for debt securities to make the guidance more operational and to improve the presentation and disclosure of other-than-temporary impairments on debt and equity securities in the financial statements. FSP FAS 115-2 and FAS 124-2 does not amend existing recognition and measurement guidance related to other-than-temporary impairment of equity securities. FSP FAS 115-2 and FAS 124-2 is effective for financial statements issued after June 15, 2009. The adoption of FSP FAS 115-2 and FAS 124-2 will not have a significant effect on the Company's consolidated financial statements.

In April 2009, the FASB issued FASB Staff Position FAS 107-1 and APB 28-1, *Interim Disclosures about Fair Value of Financial Instruments* ( FSP FAS 107-1 and APB 28-1 ). FSP FAS 107-1 and APB 28-1 amends FASB Statement No. 107, *Disclosures about Fair Value of Financial Instruments*, to require disclosures about fair value of financial instruments for interim reporting periods of publicly traded companies as well as in annual financial statements. FSP FAS 107-1 and APB 28-1 also amends APB Opinion No. 28, *Interim Financial Reporting*, to require those

disclosures in summarized financial information at interim reporting periods. FSP FAS 107-1 and

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APB 28-1 is effective for financial statements issued after June 15, 2009. The adoption of FSP FAS 107-1 and APB 28-1 will not have a significant effect on the Company's consolidated financial statements.

**NOTE 9. FAIR VALUE MEASUREMENTS**

Effective October 1, 2008, the Company adopted the provisions of SFAS No. 157, *Fair Value Measurements*. SFAS No. 157 defines fair value, establishes a framework for measuring the fair value of assets and liabilities using a hierarchy system and expands disclosures about fair value measurement. It clarifies that fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants in the market in which the reporting entity transacts.

The fair value hierarchy is as follows:

Level 1 Inputs Valuation is based upon quoted prices for identical instruments traded in active markets that the Company has the ability to access at measurement date.

Level 2 Inputs Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in active markets that are not active and model-based valuation techniques for which significant assumptions are observable in the market.

Level 3 Inputs Valuation is generated from model-based techniques that use significant assumptions not observable in the market and are used only to the extent that observable inputs are not available. These unobservable assumptions reflect the Company's own estimates of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include use of option pricing models, discounted cash flow models and similar techniques.

A description of the valuation methodologies used for instruments measured at fair value, as well as the general classification of such instruments pursuant to the valuation hierarchy, is set forth below. These valuation methodologies were applied to all of the Company's financial assets and liabilities carried at fair value effective October 1, 2008.

*Securities Available for Sale.* Securities available for sale are recorded at fair value on a recurring basis. Fair value measurement is based upon quoted prices, if available. If quoted prices are not available, fair values are measured using an independent pricing service. Level 1 securities include those traded on an active exchange, such as the New York Stock Exchange, as well as U.S. Treasury and other U.S. government and agency securities that are traded by dealers or brokers in active over-the-counter markets. The Company had no Level 1 securities at March 31, 2009. Level 2 securities include agency mortgage-backed securities and private collateralized mortgage obligations, municipal bonds and corporate debt securities.



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The following table summarizes the assets of the Company for which fair values are determined on a recurring basis as of March 31, 2009.

| (Dollars in Thousands)        | Total   | Fair Value at March 31, 2009 |            |         |
|-------------------------------|---------|------------------------------|------------|---------|
|                               |         | Level 1                      | Level 2    | Level 3 |
| Securities available for sale | 335,539 | \$                           | \$ 335,539 | \$      |

Included in securities available for sale are trust preferred securities as follows:

## At March 31, 2009

| Issuer(1)                                 | Book Value | Fair Value<br>(Dollars in Thousands) | Unrealized<br>Gain (Loss) | S&P<br>Credit Rating | Moody<br>Credit Rating |
|-------------------------------------------|------------|--------------------------------------|---------------------------|----------------------|------------------------|
| Key Corp. Capital I                       | \$ 4,979   | \$ 2,813                             | \$ (2,166)                | BB+                  | A3                     |
| Huntington Capital Trust II SE            | 4,968      | 1,287                                | (3,681)                   | BB                   | Baa3                   |
| Bank Boston Capital Trust IV (2)          | 4,959      | 2,736                                | (2,223)                   | BB-                  | Baa3                   |
| Bank America Capital III                  | 4,946      | 1,657                                | (3,289)                   | BB-                  | Baa3                   |
| PNC Capital Trust                         | 4,947      | 3,158                                | (1,789)                   | BBB                  | A2                     |
| Cascade Capital Trust I 144A (3)          | 500        | 250                                  | (250)                     |                      |                        |
| CNB Invt Tr II Exchangeable Pfd Ser B (3) | 500        | 300                                  | (200)                     |                      |                        |
| Total                                     | \$ 25,799  | \$ 12,201                            | \$ (13,598)               |                      |                        |

(1) Trust preferred securities are single-issuance. There are no known deferrals, defaults or excess subordination.

(2) Bank Boston now known as Bank of America.

(3) Securities not rated.

The Company's management reviews the status and potential impairment of the trust preferred securities on a monthly basis. In its review, management discusses duration of unrealized losses and reviews credit rating changes. Other factors, but necessarily all, considered are: that the risk of loss is minimized and easier to determine due to the single-issuer, rather than pooled, nature of the securities, the condition of the five banks listed, and whether there have been any payment deferrals or defaults to-date. Such factors are subject to change over time.

*Federal Home Loan Bank ( FHLB ) Stock.* FHLB stock is recorded at cost which is assumed to represent fair value since the Company is generally able to redeem this stock at par value.



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*Foreclosed Real Estate and Repossessed Assets.* Real estate properties and repossessed assets are initially recorded at the lower of cost or fair value less selling costs at the date of foreclosure, establishing a new cost basis. The carrying amount at March 31, 2009 represents the fair value and related losses that were measured at fair value subsequent to their initial classification as foreclosed assets.

*Loans.* The Company does not record loans at fair value on a recurring basis. However, if a loan is considered impaired, an allowance for loan losses is established. Once a loan is identified as individually impaired, management measures impairment in accordance with SFAS No. 114, *Accounting for Creditors for Impairment of*

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*a Loan.* When the fair value of the collateral is based on an observable market price or current appraised value, the Company records the impaired loan as non-recurring level 2.

The following table summarizes the assets of the Company for which fair values are determined on a non-recurring basis as of March 31, 2009.

| (Dollars in Thousands) | Total     | Fair Value at March 31, 2009 |         |         |    |
|------------------------|-----------|------------------------------|---------|---------|----|
|                        |           | Level 1                      | Level 2 | Level 3 |    |
| FHLB Stock             | 6,787     | \$                           | \$      | 6,787   | \$ |
| Foreclosed Assets, net | 3,755     |                              |         | 3,755   |    |
| Loans                  | 23,448    |                              |         | 23,448  |    |
| Total                  | \$ 33,990 | \$                           | \$      | 33,990  | \$ |

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**NOTE 10. GOODWILL AND INTANGIBLE ASSETS**

The changes in the carrying amount of the Company's goodwill and intangible assets for the six months ended March 31, 2009 and 2008, are as follows:

|                                | <b>Traditional<br/>Banking<br/>Goodwill</b> | <b>Meta Payment<br/>Systems®<br/>Goodwill<br/>(Dollars in Thousands)</b> | <b>Meta Payment<br/>Systems®<br/>Patents</b> | <b>Total</b> |
|--------------------------------|---------------------------------------------|--------------------------------------------------------------------------|----------------------------------------------|--------------|
| Balance as of October 1, 2008  | \$ 1,508                                    | \$ 425                                                                   | \$ 273                                       | \$ 2,206     |
| Acquisitions during the period |                                             |                                                                          | 243                                          | 243          |
| Balance as of March 31, 2009   | \$ 1,508                                    | \$ 425                                                                   | \$ 516                                       | \$ 2,449     |

|                                | <b>Traditional<br/>Banking<br/>Goodwill</b> | <b>Meta Payment<br/>Systems®<br/>Goodwill<br/>(Dollars in Thousands)</b> | <b>Meta Payment<br/>Systems®<br/>Patents</b> | <b>Total</b> |
|--------------------------------|---------------------------------------------|--------------------------------------------------------------------------|----------------------------------------------|--------------|
| Balance as of October 1, 2007  | \$ 1,508                                    | \$                                                                       | \$                                           | \$ 1,508     |
| Acquisitions during the period |                                             | 425                                                                      |                                              | 425          |
| Balance as of March 31, 2008   | \$ 1,508                                    | \$ 425                                                                   | \$                                           | \$ 1,933     |

**Discontinued Operations-Traditional Banking**

|                                    |          |
|------------------------------------|----------|
| Balance as of October 1, 2007      | \$ 1,895 |
| Dispositions during the period (1) | (1,895)  |
| Balance as of March 31, 2008       | \$       |

(1) MetaBank WC was sold during the quarter ended March 31, 2008.

The Company tests goodwill and intangible assets for impairment at least annually or more often if conditions indicate a possible impairment. There was no impairment to goodwill during the six months ended March 31, 2009 and 2008.

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Part I. Financial Information

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

**META FINANCIAL GROUP, INC®.**

**AND SUBSIDIARIES**

**FORWARD LOOKING STATEMENTS**



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Meta Financial Group, Inc.®, ( Meta Financial or the Company ) and its wholly-owned subsidiaries, MetaBank (the Bank ), and Meta Trust Company® ( Meta Trust or the Trust Company ), may from time to time make written or oral forward-looking statements, including statements contained in its filings with the Securities and Exchange Commission ( SEC ), in its reports to shareholders, and in other communications by the Company, which are made in good faith by the Company pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995.

These forward-looking statements include statements with respect to the Company's beliefs, expectations, estimates, and intentions that are subject to significant risks and uncertainties, and are subject to change based on various factors, some of which are beyond the Company's control. Such statements address, among others, the following subjects: future operating results; customer retention; loan and other product demand; important components of the Company's balance sheet and income statements; growth and expansion; new products and services, such as those offered by MetaBank or Meta Payment Systems® ( MPS ), a division of MetaBank; credit quality and adequacy of reserves; technology; and our employees. The following factors, among others, could cause the Company's financial performance to differ materially from the expectations, estimates, and intentions expressed in such forward-looking statements: the strength of the United States economy in general and the strength of the local economies in which the Company conducts operations; the effects of, and changes in, trade, monetary, and fiscal policies and laws, including interest rate policies of the Federal Reserve Board, as well as efforts of the United States Treasury in conjunction with bank regulatory agencies to stimulate the economy and protect the financial system; inflation, interest rate, market, and monetary fluctuations; the timely development of and acceptance of new products and services offered by the Company as well as risks (including litigation) attendant thereto and the perceived overall value of these products and services by users; the risks of dealing with or utilizing third-party vendors; the impact of changes in financial services laws and regulations; technological changes, including but not limited to the protection of electronic files or databases; acquisitions; litigation risk in general, including but not limited to those risks involving the MPS division; the growth of the Company's business as well as expenses related thereto; changes in consumer spending and saving habits; and the success of the Company at managing and collecting assets of borrowers in default.

The foregoing list of factors is not exclusive. Additional discussions of factors affecting the Company's business and prospects are contained in the Company's periodic filings with the SEC. The Company expressly disclaims any intent or obligation to update any forward-looking statement, whether written or oral, that may be made from time to time by or on behalf of the Company or its subsidiaries.

### GENERAL



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The Company, a registered unitary savings and loan holding company, is a Delaware corporation, the principal assets of which are all the issued and outstanding shares of MetaBank, a federal savings bank. The Company also owns all the issued and outstanding shares of Meta Trust. The Company was incorporated in 1993 as a unitary non-diversified savings and loan holding company that, on September 20 of that year, acquired all of the capital stock of MetaBank in connection with MetaBank's conversion from mutual to stock form of ownership. On September 30, 1996, the Company became a bank holding company for regulatory purposes upon its acquisition



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of MetaBank WC until its sale of MetaBank WC in March 2008, at which time the Company became a unitary savings and loan holding company again. Unless the context otherwise requires, references herein to the Company include Meta Financial and MetaBank, and all subsidiaries of Meta Financial, direct or indirect, on a consolidated basis.

The following discussion focuses on the consolidated financial condition of the Company and its subsidiaries, at March 31, 2009, compared to September 30, 2008, and the consolidated results of operations for the three and six months ended March 31, 2009 and 2008. This discussion should be read in conjunction with the Company's consolidated financial statements, and notes thereto, for the year ended September 30, 2008.

## **CORPORATE DEVELOPMENTS AND OVERVIEW**

The MPS division continued to demonstrate significant growth on a year-over-year basis. Fiscal second quarter 2009 MPS-related fee income grew by \$21.5 million, or 187%, as all business lines were higher than the same period in fiscal 2008. In collaboration with one of MPS's tax preparation partners, MPS introduced a new credit-related product that functions in concert with the Meta-issued prepaid card during the first fiscal quarter. This program, along with the division's rebate, Simplexus, and credit business lines were major contributors to the increase in revenue in the fiscal second quarter. The division also continued to exhibit product innovation as 8 additional patents were filed during the quarter.

The traditional bank segment is continuing to build its customer base from the previous expansion in the growing metropolitan areas of Sioux Falls, South Dakota and Des Moines, Iowa. The Bank has added seven branches in approximately the past seven years in these markets. The Bank focuses primarily on establishing lending and deposit relationships with commercial businesses and commercial real estate developers in these communities. The Bank currently operates 13 retail banking branches: in Brookings (1) and Sioux Falls (4), South Dakota, in Des Moines (6) and Storm Lake (2), Iowa and a non-retail service branch in Memphis, Tennessee.

The Company's stock trades on the NASDAQ Global Market under the symbol CASH.

## **FINANCIAL CONDITION**

As of March 31, 2009, the Company's assets grew by \$133.2 million, or 17.6%, to \$890.5 million compared to \$757.3 million at September 30, 2008. The increase in assets was reflected primarily in increases in the Company's mortgage-backed securities and to a lesser extent in total cash and cash equivalents, offset in part by decreases in the Company's investment in federal funds sold, investment securities available for sale, net loans and loans receivable and bond insurance receivable.

Total cash and cash equivalents and federal funds sold were \$16.9 million at March 31, 2009, an increase of \$8.7 million from \$8.2 million at September 30, 2008. The increase primarily was the result of the Company's excess liquidity due to an increase in deposits, primarily due to seasonal deposits at MPS. In general, the Company maintains its cash investments in interest-bearing overnight deposits with various correspondent banks. Federal funds sold deposits may be maintained at the FHLB of Des Moines or various commercial banks, including, but not limited to the following: CitiBank, JP Morgan Chase, LaSalle Bank, M&I Bank, BNP Paribas, Bank of America and Bankers Bank, all but

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one with assets in excess of \$1.0 billion. At March 31, 2009 the Company held \$216,000 in federal funds sold.

The total of mortgage-backed securities and investment securities available for sale increased \$131.7 million, or 64.6%, to \$335.5 million at March 31, 2009, as investment purchases exceeded related maturities, sales, and principal paydowns. The Company's portfolio of securities available for sale consists primarily of mortgage-backed securities, which have relatively short expected lives. Approximately 46% of the mortgage-backed securities have balloons which further limit maturity extension risk. During the six month period ended March

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31, 2009, the Company purchased \$155.4 million of mortgage-backed securities with average lives of five years or less and stated finals of approximately 30 years or less.

The Company's portfolio of net loans receivable decreased \$8.6 million, or 2.0%, to \$419.3 million at March 31, 2009. This decrease primarily relates to a decrease of \$17.6 million in commercial business and agricultural operating loans due to pay downs and transfers to other repossessed assets and an increase in the allowance for loan losses of \$5.5 million primarily related to the seasonal tax business line. Offsetting the above was an increase in commercial and multi-family real estate loans of \$13.6 million.

FHLB stock, at cost, decreased \$1.3 million primarily due to decreased borrowings with the FHLB of Des Moines, IA. Bond insurance receivable decreased \$2.0 million as management revised the expected receipt of insurance proceeds.

Foreclosed real estate and foreclosed assets increased to \$3.8 million as compared to none at September 30, 2008 due to the Company's foreclosure of assets and loan collateral related to previously reported non-performing loans. See Non-performing Assets and Allowance for Loan Losses below for further discussion.

Total deposits increased \$140.6 million, or 25.8%, to \$686.6 million at March 31, 2009. The Company continues to grow its low- and no-cost deposit portfolio. Total MPS deposits were up \$135.5 million, or 40.9%, at March 31, 2009, as compared to September 30, 2008. A portion of this increase results from seasonal gift card deposits that remain unspent and were not present at September 30, 2008 as well as new program growth.

Total borrowings decreased \$14.2 million, or 9.6%, much of which is due to the influx of deposits at the end of the quarter, from \$147.7 million at September 30, 2008 to \$133.5 million at March 31, 2009.

At March 31, 2009, the Company's shareholders' equity totaled \$48.2 million, up \$1.4 million from \$46.8 million at September 30, 2008. The increase was related to 2009 year-to-date net income (see Results of Operations below) partially offset by the payment of dividends on the Company's common stock and an unfavorable change in the accumulated other comprehensive loss on the Company's available for sale portfolio. At March 31, 2009, MetaBank continues to exceed regulatory requirements for classification as well-capitalized institution.

**Non-performing Assets and Allowance for Loan Losses**

Generally, when a loan becomes delinquent 90 days or more or when the collection of principal or interest becomes doubtful, the Company will place the loan on a non-accrual status and, as a result of this action, previously accrued interest income on the loan is taken out of current income. The loan will remain on non-accrual status until the loan has been brought current or until other circumstances occur that provide adequate assurance of full repayment of interest and principal.

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At March 31, 2009, the Company's loan portfolio exhibited stable delinquency trends with 30+ day delinquencies of \$12.2 million, or 2.8% of total loans compared to \$17.1 million, or 3.9% of total loans, at September 30, 2008.

At March 31, 2009, commercial and multi-family real estate 30+ day delinquencies totaled \$2.8 million, or 0.6% of total loans. This compares to \$6.9 million or 1.6% of total loans at September 30, 2008. Multi-family and commercial real estate loans generally present different risks than loans secured by one-to-four family residences, including, but not limited to, the concentration of principal in a limited number of loans and borrowers, the effect of general economic conditions on income producing properties and the higher level of difficulty of evaluating and monitoring these types of loans.

At March 31, 2009, commercial business 30+ day delinquencies totaled \$224,000, or 0.1% of total loans. This compares to \$9.0 million, or 2.1% of total loans, at September 30, 2008. Risks being associated with commercial business lending include, but are not limited to: payments on loans are typically dependent on the cash flows

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derived from the operation or management of the business to which the loan is made. Repayment of such loans may also be affected by factors outside the control of the business, such as unforeseen changes in economic conditions for the business, the industry in which the business operates or the general economic environment.

At March 31, 2009, agricultural loans 30+ day delinquencies totaled \$4.1 million, or 0.9% of total loans. This compares to \$221,000, or 0.1% of total loans, at September 30, 2008. The increase was primarily related to one borrower. Agricultural lending also typically involves larger loan amounts. In addition, payments on loans are dependent on the successful operation or management of the farm property securing the loan or for which an operating loan is utilized. The success of the loan may also be affected by factors outside the control of the agricultural borrower, such as the weather and grain and livestock prices.

The Company believes that the level of allowance for loan losses at March 31, 2009 adequately reflects potential risks related to these loans; however, there can be no assurance that all loans will be fully collectible or that the present level of the allowance will be adequate in the future. See Allowance for Loan Losses.

The table below sets forth the amounts and categories of non-performing assets in the Company's loan portfolio. Foreclosed assets include assets acquired in settlement of loans. Balances related to discontinued bank operations have been eliminated for all periods presented.

| Non-Performing Assets As Of                |    |                    |          |
|--------------------------------------------|----|--------------------|----------|
| March 31, 2009                             |    | September 30, 2008 |          |
| (Dollars in Thousands)                     |    |                    |          |
| Non-Accruing Loans:                        |    |                    |          |
| 1-4 Family                                 | \$ | 4,759              | \$ 942   |
| Commercial & Multi Family                  |    | 1,617              | 1,302    |
| Agricultural Real Estate                   |    |                    | 12       |
| Consumer                                   |    | 1                  | 1        |
| Commercial Business                        |    | 882                | 538      |
| Total                                      |    | 7,259              | 2,795    |
|                                            |    |                    |          |
| Accruing Loans Delinquent 90 Days or More: |    |                    | 4,600    |
| Total                                      |    |                    | 4,600    |
|                                            |    |                    |          |
| Restructured Loans:                        |    |                    |          |
| Agricultural Operating                     |    |                    | 121      |
| Total                                      |    |                    | 121      |
|                                            |    |                    |          |
| Foreclosed Assets:                         |    |                    |          |
| Consumer                                   |    | 15                 |          |
| Commercial Business                        |    | 3,740              |          |
| Total                                      |    | 3,755              |          |
|                                            |    |                    |          |
| Total Non-Performing Assets                | \$ | 11,014             | \$ 7,516 |
| Total as a Percentage of Total Assets      |    | 1.24%              | 0.99%    |

The 2009 second quarter increase in non-performing loans, specifically one- to four-family, relates to one commercial borrower that the Company believes participated in a fraud on the Bank and other banks, as first disclosed in the Company's June 30, 2008 Quarterly Report on

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Form 10-Q. The Company had increased its allowance for loan losses by \$1.8 million for this matter during the quarter ending September 30, 2008 and again by \$1.3 million in the March 31, 2009 quarter before charging-off certain loans. While the Company's non-performing

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loan balance increased during the second quarter of fiscal 2009 due to this borrower, no systemic loan portfolio issues were noted during the period.

*Classified assets.* Federal regulations provide for the classification of loans and other assets such as debt and equity securities considered by the OTS to be of lesser quality as substandard, doubtful or loss. An asset is considered substandard if it is inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Substandard assets include those characterized by the distinct possibility that the savings association will sustain some loss if the deficiencies are not corrected. Assets classified as doubtful have all the weaknesses inherent in those classified as substandard, with the added characteristic that the weaknesses present make collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable and improbable. Assets classified as loss are those considered uncollectible and of such minimal value that their continuance as assets without the establishment of a specific reserve is not warranted. When assets are classified as either substandard or doubtful, the Bank may establish general allowances for loan losses in an amount deemed prudent by management. General allowances represent loss allowances which have been established to recognize the inherent risk associated with lending activities, but which, unlike specific allowances, have not been allocated to particular problem assets. When assets are classified as loss, the Bank is required either to establish a specific allowance for loan losses equal to 100% of that portion of the asset so classified or to charge-off such amount. The Bank's determination as to the classification of its assets and the amount of its valuation allowances are subject to review by its regulatory authorities, who may overrule the Bank's classifications and require the establishment of additional general or specific loss allowances. The discovery of additional information in the future may also affect both the level of classification and the amount of loss allowances.

In connection with the Bank's recent examination by the Office of Thrift Supervision (OTS), the Bank was informed that four of its trust preferred securities should be classified as substandard assets as of March 31, 2009. The four securities are: Huntington Capital Trust II SE, Bank Boston Capital Trust IV, Bank America Capital III, and Key Corp. Capital I. The criterion for the determination was OTS' policy that the recent assignment of a sub-investment grade rating by one nationally recognized rating agency, notwithstanding the fact that other nationally recognized rating agencies have assigned an investment grade rating to the securities in question, mandates the categorization of the asset as substandard. Despite the classification, the actual performance of the four securities continues to be satisfactory; interest payments are being made on a timely basis and there have been no requests for payment deferrals.

On the basis of management's review of its loans and other assets, at March 31, 2009, the Company had classified a total of \$37.6 million of its assets as substandard, \$4.8 million as doubtful and none as loss. This compares to classifications at September 30, 2008 of \$15.8 million as substandard, \$88,000 as doubtful and none as loss. As of March 31, 2009, \$19.9 million out of a total of \$37.6 million of substandard assets is attributable to the trust preferred securities identified above. See Note 9 to Notes to Consolidated Financial Statement.

*Allowance for loan losses.* The Company establishes its provision for loan losses, and evaluates the adequacy of its allowance for loan losses based upon a systematic methodology consisting of a number of factors including, among others, historic loss experience, the overall level of classified assets and non-performing loans, the composition of its loan portfolio and the general economic environment within which the Company and its borrowers operate.

Management closely monitors economic developments both regionally and nationwide, and considers these factors when assessing the adequacy of its allowance for loan losses. While the Company has no direct exposure to sub-prime mortgage loans, management reiterates and restates its concern that developments in the sub-prime mortgage market may have a direct effect on residential real estate prices and an indirect effect on the economy in general. In addition, the economic slowdown is straining the financial condition of some borrowers. Management therefore believes that future losses in the residential portfolio may be somewhat higher than historical experience. Over the past six years, loss rates in the commercial and multi-family real estate market have remained moderate. Management concludes that future losses in this portfolio may be somewhat higher than recent historical experience, excluding loan losses related to fraud by borrowers. On the other hand, current trends in

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agricultural markets continue to be mostly positive. Higher commodity prices as well as higher yields have created strong economic conditions for most farmers. Nonetheless, management still expects that future losses in this portfolio, which have been very low, could be higher than recent historical experience. Management believes that the slowdown in economic growth during this fiscal year may also negatively impact consumers' repayment capacities. Additionally, a sizable portion of the Company's consumer loan portfolio is secured by residential real estate, as discussed above, and is an area to be closely monitored by management in view of its stated concerns. Recent weather-related events, such as flooding, have occurred in the Bank's markets. However, this has not resulted in any material impairment to the loans originated by the Bank.



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Management believes that, based on a detailed review of the loan portfolio, historic loan losses, current economic conditions, the size of the loan portfolio, and other factors, the current level of the allowance for loan losses at March 31, 2009 reflects an adequate allowance against probable losses from the loan portfolio. Although the Company maintains its allowance for loan losses at a level that it considers to be adequate, investors and others are cautioned that there can be no assurance that future losses will not exceed estimated amounts, or that additional provisions for loan losses will not be required in future periods. In addition, the Company's determination of the allowance for loan losses is subject to review by its regulatory agencies, which can require the establishment of additional general or specific allowances.

At March 31, 2009, the Company has established an allowance for loan losses totaling \$11.2 million, or 154.6% of non-performing loans, compared to \$5.7 million, or 76.3% of non-performing loans at September 30, 2008. Excluding the current period allowance related to MPS and its seasonal tax business line, the ratio of allowance to non-performing loans would have been 53.6% at March 31, 2009.

The following table sets forth an analysis of the activity in the Company's allowance for loan losses for the three and six months ended March 31, 2009 and 2008.

| (Dollars in Thousands)    | Three Months Ended<br>March 31, |          | Six Months Ended<br>March 31, |          |
|---------------------------|---------------------------------|----------|-------------------------------|----------|
|                           | 2009                            | 2008     | 2009                          | 2008     |
| Beginning balance         | \$ 7,741                        | \$ 4,370 | \$ 5,732                      | \$ 4,493 |
| Provision for loan losses | 10,270                          | 200      | 12,399                        | 70       |
| Charge-offs               | (7,293)                         | (5)      | (7,414)                       | (30)     |
| Recoveries                | 506                             | 16       | 507                           | 48       |
| Ending balance            | \$ 11,224                       | \$ 4,581 | \$ 11,224                     | \$ 4,581 |

The allowance for loan losses reflects management's best estimate of probable losses inherent in the portfolio based on currently available information. In addition to the factors mentioned above, future additions to the allowance for loan losses may become necessary based upon changing economic conditions, increased loan balances or changes in the underlying collateral of the loan portfolio.

## CRITICAL ACCOUNTING POLICIES



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The Company's financial statements are prepared in accordance with U.S. generally accepted accounting principles ( GAAP ). The financial information contained within these statements is, to a significant extent, financial information that is based on approximate measures of the financial effects of transactions and events that have already occurred. Based on its consideration of accounting policies that: (i) involve the most complex and subjective decisions and assessments which may be uncertain at the time the estimate was made and (ii) different estimates that reasonably could have been used in the current period, or changes in the accounting estimate that are reasonably likely to occur from period to period, would have a material impact on the financial statements, management has identified the policies described below as Critical Accounting Policies. This discussion and analysis should be read in conjunction with the Company's financial statements and the accompanying notes presented in Part II, Item 8 Financial Statements and Supplementary Data of its Annual Report on Form 10-K for the year ended September 30, 2008 and contained herein.

*Allowance for Loan Losses.* The Company's allowance for loan loss methodology incorporates a variety of risk considerations, both quantitative and qualitative, in establishing an allowance for loan loss that management believes is appropriate at each reporting date. Quantitative factors include the Company's historical loss

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experience, delinquency and charge-off trends, collateral values, changes in nonperforming loans, and other factors. Quantitative factors also incorporate known information about individual loans, including borrowers' sensitivity to interest rate movements. Qualitative factors include the general economic environment in the Company's markets, including economic conditions throughout the Midwest and, in particular, the state of certain industries. Size and complexity of individual credits in relation to loan structure, existing loan policies, and pace of portfolio growth are other qualitative factors that are considered in the methodology. As the Company adds new products and increases the complexity of its loan portfolio, it will enhance its methodology accordingly. Management may have reported a materially different amount for the provision for loan losses in the statement of operations to change the allowance for loan losses if its assessment of the above factors were different. Although management believes the levels of the allowance as of both March 31, 2009 and September 30, 2008 were adequate to absorb probable losses inherent in the loan portfolio, a decline in local economic conditions or other factors could result in increasing losses.

*Goodwill and Intangible Assets.* Goodwill represents the excess of acquisition costs over the fair value of the net assets acquired in a purchase acquisition. Intangible assets include patents filed by the MPS Division. Goodwill and intangible assets are tested annually for impairment or more often if conditions indicate a possible impairment. Determining the fair value of a reporting unit involves the use of significant estimates and assumptions. These estimates and assumptions include revenue growth rates and operating margins used to calculate future cash flows, risk-adjusted discount rates, future economic and market conditions, comparison of the Company's market value to book value and determination of appropriate market comparables. Actual future results may differ from those estimates.

Each quarter the Company evaluates the estimated useful lives of intangible assets and whether events or changes in circumstances warrant a revision to the remaining periods of amortization. In accordance with FASB Statement No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, recoverability of these assets is measured by comparison of the carrying amount of the asset to the future undiscounted cash flows the asset is expected to generate. If the asset is considered to be impaired, the amount of any impairment is measured as the difference between the carrying value and the fair value of the impaired asset.

Assumptions and estimates about future values and remaining useful lives of the Company's intangible and other long-lived assets are complex and subjective. They can be affected by a variety of factors, including external factors such as industry and economic trends, and internal factors such as changes in the Company's business strategy and internal forecasts. Although the Company believes the historical assumptions and estimates used are reasonable and appropriate, different assumptions and estimates could materially impact the reported financial results.

*Self-Insurance.* The Company has a self-insured healthcare plan for its employees up to certain limits. To mitigate a portion of these risks, the Company has a stop-loss insurance policy through a commercial insurance carrier for coverage in excess of \$50,000 per individual occurrence with a maximum aggregate limit for each employee of \$2.0 million. The estimate of self-insurance liability is based upon known claims and an estimate of incurred, but not reported (IBNR) claims. IBNR claims are estimated using historical claims lag information received by a third party claims administrator. Due to the uncertainty of health claims, the approach includes a process which may differ significantly from other methodologies and still produce an estimate in accordance with GAAP. Although management believes it uses the best information available to determine the accrual, unforeseen health claims could result in adjustments to the accrual.

*Deferred Tax Assets.* The company accounts for income taxes according to the asset and liability method. Under this method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax basis. Deferred tax assets and liabilities are measured using the enacted tax rates applicable to income for the years in which those temporary differences are expected to be recovered or settled. Deferred tax assets are recognized subject to management's judgment that realization is more-likely-than-not. An estimate of probable



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income tax benefits that will not be realized in future years is required in determining the necessity for a valuation allowance. There was no deferred tax valuation allowance at March 31, 2009 or September 30, 2008.

*Other-Than-Temporary Impairment.* Management evaluates the Company's available for sale securities for other-than-temporary impairment at least on a quarterly basis, and more often if economic or market concerns warrant such evaluation. Such factors management uses to determine impairment are: (i) the length of time and extent to which the market value has been less than cost, (ii) the financial condition and near-term prospects of the issuer including specific events, (iii) the Company's intent and ability to hold the investment to the earlier of maturity or recovery in fair value, (iv) the implied and historical volatility of the security and (v) any downgrades by rating agencies.

## RESULTS OF OPERATIONS

*General.* The Company recorded income from continuing operations of \$1.2 million, or \$0.45 per diluted share, for the three months ended March 31, 2009 compared to \$1.2 million, or \$0.46 per diluted share, for the same period in fiscal year 2008. Including discontinued operations, net income was \$1.2 million, or \$0.45 per diluted share for the three months ended March 31, 2009 compared to \$3.0 million, or \$1.16 per diluted share for the same period in fiscal year 2008. Net earnings in the current period were primarily impacted by increased income from the successful expansion of the MPS division's program with one of its tax preparation partners and higher card fees from all of MPS' primary programs and services as well as higher net interest income. Offsetting these factors, in part, were higher operating expenses at MPS due to the seasonal tax programs, increases in new programs and cards issued and an increased provision for loan losses due to the start-up of one of MPS's credit-related programs described below. In addition, the Company recorded an additional provision in connection with two commercial borrowers.

The Company recorded income from continuing operations of \$1.8 million, or \$0.71 per diluted share, for the six months ended March 31, 2009 compared to \$413,000, or \$0.16 per diluted share, for the same period in fiscal year 2008. Including discontinued operations, net income was \$1.8 million, or \$0.71 per diluted share for the six months ended March 31, 2009 compared to \$2.3 million, or \$0.87 per diluted share for the same period in fiscal year 2008. Net earnings for the six month period ended March 31, 2009 were impacted by the aforementioned factors.

Net earnings in the prior year three and six month period ended March 31, 2008 were impacted by an after-tax gain of \$1.8 million resulting from the sale of the Company's commercial banking subsidiary, MetaBank WC. See Note 2 to the Notes to Condensed Consolidated Financial Statements for further discussion on discontinued operations. Excluding this prior year non-recurring event, earnings remained stable at \$1.2 million for both of the second quarters.

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*Net interest income.* Net interest income from continuing operations for the second quarter of fiscal year 2009 increased by \$2.0 million, or 32.3%, to \$8.2 million from \$6.2 million for the same period in the prior fiscal year. Net interest margin increased to 3.96% for the second quarter of 2009 as compared to 3.59% for the same period in 2008. The increase in net interest income is primarily attributable to two factors: lower rates paid on interest-bearing liabilities, from 2.09% in the 2008 quarter to 1.06% in 2009 and higher yields on the loan portfolio and mortgage-backed securities portfolio. As of March 31, 2009, low- and no-cost checking deposits represented 79% of total deposits compared to 76% one year earlier. The increase was driven by a 39% increase (totaling \$131.3 million) in MPS deposits as compared to one year earlier. Average non-interest-bearing deposits as a percent of total average deposits and interest-bearing liabilities was 65.5% in the current quarter compared to 51.5% for the same quarter a year ago. In addition to lower rates on all interest-bearing liabilities, the volume of borrowings also decreased due to the deposit increases.

For the six month period ended March 31, 2008 net interest income was \$14.4 million compared to \$11.5 million for the same period in the prior fiscal year. Contributing to this increase was an 18% increase in earning assets and a 22 basis point increase in net interest margin as reduced funding costs outpaced lower asset yields.

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The following tables present, for the periods indicated, the Company's total dollar amount of interest income from average interest-earning assets and the resulting yields, as well as the interest expense on average interest-bearing liabilities, expressed both in dollars and rates. No tax equivalent adjustments have been made. Non-accruing loans have been included in the table as loans carrying a zero yield. Balances related to discontinued bank operations have been reclassified to non-interest-earning assets and non-interest-bearing liabilities for all periods presented.

| Three Months Ended March 31,<br>(Dollars in Thousands)                                   | Average<br>Outstanding<br>Balance | 2009<br>Interest<br>Earned /<br>Paid | Yield /<br>Rate | Average<br>Outstanding<br>Balance | 2008<br>Interest<br>Earned /<br>Paid | Yield /<br>Rate |
|------------------------------------------------------------------------------------------|-----------------------------------|--------------------------------------|-----------------|-----------------------------------|--------------------------------------|-----------------|
| <b>Interest-earning assets:</b>                                                          |                                   |                                      |                 |                                   |                                      |                 |
| Loans receivable                                                                         | \$ 424,580                        | \$ 7,537                             | 7.20%           | \$ 426,059                        | \$ 6,599                             | 6.23%           |
| Mortgage-backed securities                                                               | 249,101                           | 2,797                                | 4.55%           | 212,773                           | 2,339                                | 4.42%           |
| Other investments and fed funds sold                                                     | 170,991                           | 200                                  | 0.47%           | 58,388                            | 957                                  | 6.59%           |
| <b>Total interest-earning assets</b>                                                     | <b>844,672</b>                    | <b>\$ 10,534</b>                     | <b>5.06%</b>    | <b>697,220</b>                    | <b>\$ 9,895</b>                      | <b>5.71%</b>    |
| Non-interest-earning assets                                                              | 98,735                            |                                      |                 | 63,773                            |                                      |                 |
| <b>Total assets</b>                                                                      | <b>\$ 943,407</b>                 |                                      |                 | <b>\$ 760,993</b>                 |                                      |                 |
| Non-interest bearing deposits                                                            | \$ 573,119                        | \$                                   | 0.00%           | \$ 364,811                        | \$                                   | 0.00%           |
| <b>Interest-bearing liabilities:</b>                                                     |                                   |                                      |                 |                                   |                                      |                 |
| Interest-bearing checking                                                                | 15,656                            | 9                                    | 0.23%           | 16,613                            | 32                                   | 0.77%           |
| Savings                                                                                  | 9,742                             | 10                                   | 0.42%           | 10,201                            | 28                                   | 1.10%           |
| Money markets                                                                            | 37,703                            | 93                                   | 1.00%           | 56,447                            | 353                                  | 2.52%           |
| Time deposits                                                                            | 155,526                           | 1,317                                | 3.43%           | 143,762                           | 1,617                                | 4.52%           |
| FHLB advances                                                                            | 55,797                            | 669                                  | 4.86%           | 70,443                            | 864                                  | 4.93%           |
| Other borrowings                                                                         | 26,930                            | 191                                  | 2.88%           | 46,578                            | 785                                  | 6.78%           |
| <b>Total interest-bearing liabilities</b>                                                | <b>301,354</b>                    | <b>2,289</b>                         | <b>3.08%</b>    | <b>344,044</b>                    | <b>3,679</b>                         | <b>4.30%</b>    |
| <b>Total deposits and interest-bearing liabilities</b>                                   | <b>874,473</b>                    | <b>\$ 2,289</b>                      | <b>1.06%</b>    | <b>708,855</b>                    | <b>\$ 3,679</b>                      | <b>2.09%</b>    |
| Other non-interest bearing liabilities                                                   | 18,685                            |                                      |                 | 9,788                             |                                      |                 |
| <b>Total liabilities</b>                                                                 | <b>893,158</b>                    |                                      |                 | <b>718,643</b>                    |                                      |                 |
| Shareholders' equity                                                                     | 50,249                            |                                      |                 | 42,350                            |                                      |                 |
| <b>Total liabilities and shareholders equity</b>                                         | <b>\$ 943,407</b>                 |                                      |                 | <b>\$ 760,993</b>                 |                                      |                 |
| Net interest income and net interest rate spread including non-interest bearing deposits |                                   | \$ 8,245                             | 4.00%           |                                   | \$ 6,216                             | 3.62%           |
| <b>Net interest margin</b>                                                               |                                   |                                      | <b>3.96%</b>    |                                   |                                      | <b>3.59%</b>    |



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| Six Months Ended March 31,<br>(Dollars in Thousands)                                     | Average<br>Outstanding<br>Balance | 2009<br>Interest<br>Earned /<br>Paid | Yield /<br>Rate | Average<br>Outstanding<br>Balance | 2008<br>Interest<br>Earned /<br>Paid | Yield /<br>Rate |
|------------------------------------------------------------------------------------------|-----------------------------------|--------------------------------------|-----------------|-----------------------------------|--------------------------------------|-----------------|
| <b>Interest-earning assets:</b>                                                          |                                   |                                      |                 |                                   |                                      |                 |
| Loans receivable                                                                         | \$ 433,217                        | \$ 13,909                            | 6.44%           | \$ 398,281                        | \$ 12,877                            | 6.47%           |
| Mortgage-backed securities                                                               | 216,333                           | 4,805                                | 4.45%           | 178,659                           | 3,846                                | 4.31%           |
| Other investments and fed funds sold                                                     | 123,860                           | 546                                  | 0.88%           | 76,079                            | 2,071                                | 5.44%           |
| <b>Total interest-earning assets</b>                                                     | <b>773,410</b>                    | <b>\$ 19,260</b>                     | <b>4.99%</b>    | <b>653,019</b>                    | <b>\$ 18,794</b>                     | <b>5.76%</b>    |
| Non-interest-earning assets                                                              | 91,152                            |                                      |                 | 50,263                            |                                      |                 |
| <b>Total assets</b>                                                                      | <b>\$ 864,562</b>                 |                                      |                 | <b>\$ 703,282</b>                 |                                      |                 |
| Non-interest bearing deposits                                                            | \$ 483,960                        | \$                                   | 0.00%           | \$ 320,809                        | \$                                   | 0.00%           |
| <b>Interest-bearing liabilities:</b>                                                     |                                   |                                      |                 |                                   |                                      |                 |
| Interest-bearing checking                                                                | 15,157                            | 20                                   | 0.26%           | 15,804                            | 75                                   | 0.95%           |
| Savings                                                                                  | 9,449                             | 21                                   | 0.45%           | 10,327                            | 75                                   | 1.45%           |
| Money markets                                                                            | 39,568                            | 236                                  | 1.20%           | 60,893                            | 910                                  | 2.99%           |
| Time deposits                                                                            | 154,833                           | 2,696                                | 3.49%           | 147,860                           | 3,395                                | 4.59%           |
| FHLB advances                                                                            | 58,325                            | 1,388                                | 4.77%           | 68,539                            | 1,795                                | 5.24%           |
| Other borrowings                                                                         | 40,152                            | 494                                  | 2.47%           | 30,925                            | 1,054                                | 6.82%           |
| <b>Total interest-bearing liabilities</b>                                                | <b>317,484</b>                    | <b>4,855</b>                         | <b>3.07%</b>    | <b>334,348</b>                    | <b>7,304</b>                         | <b>4.37%</b>    |
| <b>Total deposits and interest-bearing liabilities</b>                                   | <b>801,444</b>                    | <b>\$ 4,855</b>                      | <b>1.21%</b>    | <b>655,157</b>                    | <b>\$ 7,304</b>                      | <b>2.23%</b>    |
| Other non-interest bearing liabilities                                                   | 15,131                            |                                      |                 | 7,285                             |                                      |                 |
| <b>Total liabilities</b>                                                                 | <b>816,575</b>                    |                                      |                 | <b>662,442</b>                    |                                      |                 |
| Shareholders' equity                                                                     | 47,987                            |                                      |                 | 40,840                            |                                      |                 |
| <b>Total liabilities and shareholders equity</b>                                         | <b>\$ 864,562</b>                 |                                      |                 | <b>\$ 703,282</b>                 |                                      |                 |
| Net interest income and net interest rate spread including non-interest bearing deposits |                                   | \$ 14,405                            | 3.78%           |                                   | \$ 11,490                            | 3.53%           |
| <b>Net interest margin</b>                                                               |                                   |                                      | <b>3.74%</b>    |                                   |                                      | <b>3.52%</b>    |

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*Provision for loan loss.* The Company recorded a provision for loan losses in the second quarter of fiscal year 2009 of \$10.3 million compared to a provision of \$200,000 for the same period in the prior fiscal year. \$6.1 million related to the Company's Meta Payment Systems® (MPS) division and the start-up and completion of loan originations offered in collaboration with MPS' tax preparation partner. The loan proceeds were placed on a prepaid card issued by the Bank and generally are systematically repaid by the taxpayer's refund from the Internal Revenue Service. In addition to the Company's loss provision, the contractual arrangement with this partner provides for substantial, but not full, credit loss protection mechanisms which the Company does not foresee the need to utilize during the current fiscal year due to satisfactory portfolio performance. Most of the revenue and income for this program occurred in the fiscal second quarter and exceeds the loan loss provision. The Company's traditional bank segment also recorded an additional provision for loan losses in the amount of \$4.2 million in connection with two commercial borrowers. For the six months ended March 31, 2009 the Company recorded a provision of \$12.4 million compared to a provision of \$70,000 for the same period in the prior fiscal year due to the aforementioned factors. Also see Note 3 to the Notes to Condensed Consolidated Financial Statements and Non-performing Assets and Allowance for Loan Losses herein for further discussion.

*Non-interest income.* Non-interest income increased by \$21.3 million, or 173.2%, to \$33.6 million from \$12.3 million in the prior fiscal year second quarter. The increase is the result of higher fee income earned on prepaid debit cards, income tax related programs and other products and services offered by MPS. Fees earned on prepaid debit cards from tax related programs, rebate, gift, travel and other payment systems products and services were \$33.0 million for the second quarter of fiscal year 2009, compared to \$11.5 million for the same quarter in fiscal year 2008. For the six months ended March 31, 2009, non-interest income increased by \$30.7 million, or 166.8%, to \$49.1 million from \$18.4 million for the same period in the prior fiscal year. Fees earned on prepaid debit cards relating to tax programs and other payment systems products and services were \$48.1 million for the six months ended March 31, 2009, compared to \$17.0 million for the same period in fiscal year 2007.

*Non-interest expense.* Non-interest expense increased by \$13.3 million, or 81.1%, to \$29.7 million for the second quarter of fiscal year 2009 from \$16.4 million for the same quarter in fiscal year 2008. Non-interest expense increased by \$19.1 million, or 65.6%, to \$48.2 million for the six months ended March 31, 2009 from \$29.1 million for the same period in fiscal year 2008.

Costs associated with the operational support of products at MPS also increased. Card processing expenses rose \$9.9 million from \$5.0 million in the second quarter of fiscal year 2008 to \$14.9 million in the current quarter. For the six months ended March 31, 2009, card processing expense totaled \$20.1 million, compared to \$8.1 million for the same period in the prior fiscal year. These expenses primarily stem from the aforementioned tax programs and growth in other programs managed by MPS.

Compensation expense rose \$1.8 million to \$8.3 million for the three months ended March 31, 2009 as compared to \$6.5 million for the same period in fiscal 2008. For the six months ended March 31, 2009, compensation expense totaled \$15.8 million, compared to \$12.2 million for the same period in the prior fiscal year. The increase represents the addition of management, client relations, compliance and operations support staff within MPS, as well as software developers, Information Technology (IT) support staff, and other administrative support within the Company. Many of the new employees are focused on supporting new business growth and the expansion of existing MPS products and services.

The Company's occupancy and equipment expense also rose during the second quarter of fiscal year 2009 as compared to the same period in the prior fiscal year. Occupancy and equipment expense for the second quarter of fiscal year 2009 was \$2.0 million compared to \$1.8 million for the same period in fiscal year 2008. Occupancy and equipment expense for the six months ended March 31, 2009 was \$3.9 million compared to \$3.0 million for the same period in fiscal year 2008. Both quarter and year-to-date increases were due to supporting new product lines and increasing market penetration of MPS products and services.



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Legal and consulting expense was \$925,000 for the second quarter of fiscal year 2009, up \$135,000 or 17.1% from the same period in 2008. Legal and consulting expense was \$2.0 million for the six months ended March 31, 2009, up \$800,000 or 66.7% from the same period in 2008. The increase related to MPS growth and patent applications, resolution of previously disclosed customer fraud issues and general corporate matters.

The Company's data processing expense also rose during the second quarter of fiscal year 2009 as compared to the same period in the prior fiscal year due to increased transaction volumes from MPS programs. Data processing expense for the second quarter of fiscal year 2009 was \$816,000 compared to \$322,000 for the same period in fiscal year 2008. Data processing expense for the six months ended March 31, 2009 was \$1.3 million compared to \$582,000 for the same period in fiscal year 2008.

The Company's other non-interest expense totaled \$2.2 million for the second quarter of fiscal year 2009 as compared to \$1.6 million for the same period in fiscal 2008. Regulatory expense increased \$346,000 due to increased FDIC assessments and insurance and surety bond costs increased \$200,000 as compared to the same period in 2008. Other non-interest expense for the six months ended March 31, 2009 was \$4.3 million compared to \$3.3 million for the same period in fiscal year 2008. Regulatory expense increased \$547,000 and insurance and surety bond costs increased \$318,000 as compared to the same period in 2008.

Management expects that these costs will continue to increase as MPS introduces more programs and issues more cards. However, it is anticipated that overall costs will represent a gradually diminishing portion of total revenue over time. The second fiscal quarter was the second consecutive quarter that this ratio improved.

*Income tax expense.* Income tax expense from continuing operations for the second quarter of fiscal year 2009 was \$760,000, or an effective tax rate of 39.3%, compared to \$743,000, or an effective tax rate of 38.2%, for the same period in the prior fiscal year. For the six months ended March 31, 2009, the Company recorded an income tax expense from continuing operations in the amount of \$1.1 million, or an effective tax rate of 37.4%, compared to \$281,000, or an effective tax rate of 40.5% for the same period in the prior fiscal year. The change in tax expense is primarily due to the change in income from continuing operations before income tax expense. The Company's recorded income tax expense was also impacted by permanent differences between book and taxable income.

*Discontinued Operations.* The Company reported no income from discontinued operations in the current fiscal year compared to income of \$1.8 million and \$1.9 million for the prior three and six month periods ended March 31, 2008, respectively. The prior year was impacted by a \$1.8 million after-tax gain on sale of MetaBank WC. See Note 2 to the Notes to Condensed Consolidated Financial Statements for further discussion on discontinued operations.

## **LIQUIDITY AND CAPITAL RESOURCES**

The Company's primary sources of funds are deposits, borrowings, principal and interest payments on loans and mortgage-backed securities, and maturing investment activities. While scheduled loan repayments and maturing investments are relatively predictable, deposit flows and early loan repayments are influenced by the level of interest rates, general economic conditions, and competition.

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The Company uses its capital resources principally to meet ongoing commitments to fund maturing certificates of deposits and loan commitments, to maintain liquidity, and to meet operating expenses. At March 31, 2009, the Company had commitments to originate and purchase loans totaling \$52.3 million. The Company believes that loan repayment and other sources of funds will be adequate to meet its foreseeable short- and long-term liquidity needs.

Regulations require MetaBank to maintain minimum amounts and ratios of total risk-based capital and Tier 1 capital to risk-weighted assets, and a leverage ratio consisting of Tier 1 capital to average assets. The following

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table sets forth MetaBank's actual capital and required capital amounts and ratios at March 31, 2009 which, at that date, exceeded the minimum capital adequacy requirements.

| At March 31, 2009                                  | Actual    |       | Minimum Requirement For Capital Adequacy Purposes |       | Minimum Requirement to Be Well Capitalized Under Prompt Corrective Active Provisions |       |
|----------------------------------------------------|-----------|-------|---------------------------------------------------|-------|--------------------------------------------------------------------------------------|-------|
|                                                    | Amount    | Ratio | Amount<br>(Dollars in Thousands)                  | Ratio | Amount                                                                               | Ratio |
| <b>MetaBank</b>                                    |           |       |                                                   |       |                                                                                      |       |
| Tangible capital (to tangible assets)              | \$ 58,382 | 6.54% | \$ 13,384                                         | 1.50% | n/a                                                                                  | n/a   |
| Tier 1 (core) capital (to adjusted total assets)   | 58,382    | 6.54  | 35,691                                            | 4.00  | \$ 44,614                                                                            | 5.00% |
| Tier 1 (core) capital (to risk-weighted assets)    | 58,382    | 10.03 | 23,277                                            | 4.00  | 34,915                                                                               | 6.00  |
| Total risk-based capital (to risk-weighted assets) | 65,656    | 11.28 | 46,554                                            | 8.00  | 58,192                                                                               | 10.00 |

The Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA) established five regulatory capital categories and authorized the banking regulators to take prompt corrective action with respect to institutions in an undercapitalized category. At March 31, 2009, MetaBank exceeded minimum requirements for the well capitalized category.

## OTHER RECENT MATTERS

In response to the current national and international economic recession, the U.S. government has taken a variety of actions intended to stimulate the national economy, including the passage of legislation, such as the Emergency Economic Stabilization Act of 2008 (the EESA), and the implementation of certain programs by federal agencies.

The first program put forth by the U.S. Treasury pursuant to its authority under the EESA was the Troubled Asset Relief Program's Capital Purchase Program (the CPP). Pursuant to the CPP, the US Treasury, on behalf of the US government, intends to purchase up to \$250 billion of preferred stock, along with warrants to purchase common stock, from certain financial institutions that applied to receive funds. The CPP is intended to shore up bank capital and to stimulate lending.

Another recently implemented program intended to stabilize the nation's banking system is the Term Asset-Backed Securities Loan Facility (the TALF) promulgated by the Board of Governors of the Federal Reserve System. The program, which became operational in March, 2009, is intended to increase credit availability and support economic activity by facilitating renewed issuance of consumer and small business asset-backed securities (ABS) and commercial mortgage-backed securities (CMBS). Under TALF, the Federal Reserve Bank of New York will finance the purchase of eligible ABS and CMBS by investors that own eligible collateral so long as such investor maintains an account relationship with a primary dealer. Generally, eligible ABS must be newly issued, highly rated ABS collateralized by student loans, auto loans, credit card loans, and loans guaranteed by the Small Business Administration. Eligible CMBS must also meet certain requirements, including: (i) it must entitle its holders to payments of principal and interest throughout its remaining term, (ii) it must bear interest at a fixed pass-through

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rate or at a rate based on the weighted average of the underlying fixed mortgage rates, and (iii) the CMBS must not be junior to other securities with claims on the same pool of loans. Minimum loan sizes under the TALF will be \$10 million and TALF loans will generally have a three year maturity. Starting in June 2009, however, TALF loans secured by SBA Pool Certificates, SBA Development

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Company Participation Certificates, or ABS secured by student loans or commercial mortgages will have a five-year maturity if the borrower so elects.

In response to the current reserve ratios of the Deposit Insurance Fund, and the need to restore it to its statutory minimum, the Federal Deposit Insurance Corporation (the "FDIC") announced in February, 2009, a 20 basis-point special assessment on deposits as of June 30, 2009, payable on September 30, 2009. In addition, the FDIC made changes to its risk-based assessment rates effective April 1, 2009.

Finally, the FDIC promulgated a temporary liquidity guarantee program that had both a debt guarantee component, whereby the FDIC agreed to guarantee certain senior unsecured debt issued by eligible financial institutions between October 14, 2008 and June 30, 2009, and an account transaction guarantee component, whereby the FDIC agreed to insure 100% of non-interest bearing deposit transaction accounts held at eligible financial institutions, such as lawyers' trust accounts, payment processing accounts, payroll accounts and working capital accounts through December 31, 2009. MetaBank opted out of participation in both of these programs, however.

The extent to which these programs and others like them will succeed in ameliorating tight credit conditions or otherwise result in an improvement in the national economy is uncertain.

The Company utilizes various third parties for, among other things, its processing needs, both with respect to standard bank operations and with respect to its MPS division. MPS was notified in April 2008 by one of the processors that the processor's computer system had been breached, which led to the unauthorized load and spending of funds from Bank-issued cards. The Bank believes the amount in question to be approximately \$2.0 million and the processor has notified its insurer. The processor and program manager both have agreements with the Bank to indemnify it for any losses as a result of such unauthorized activity, and have additionally notified the Bank that they are sufficiently insured for such events. In addition, the Bank has given notice to its own insurer. As of the date of this filing, the Bank has been advised that the insurance claims filed by its third parties are still pending. The Company has made demand for payment and has filed a demand for arbitration to recover the unauthorized loading and spending amounts and certain damages. As a result, the Bank continues to not anticipate any loss with respect to this event.



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Part I. Financial Information

Item 3. Quantitative and Qualitative Disclosure About Market Risk

**MARKET RISK**

The Company is exposed to the impact of interest rate changes and changes in the market value of its investments.

The Company originates predominantly adjustable-rate loans and fixed-rate loans up to ten years. Long-term fixed-rate residential mortgages are generally sold into the secondary market. As a result of its lending practices, the Company's loan portfolio is relatively short in duration and yields respond quickly to the overall level of interest rates.

The Company's primary objective for its investment portfolio is to provide the liquidity necessary to meet the Company's cash demands. This portfolio may also be used in the ongoing management of interest rate risk. As a result, funds may be invested among various categories of security types and maturities based upon the Company's need for liquidity and its desire to create an economic hedge against the effects changes in interest rates may have on the overall market value of the Company.

The Company offers a full range of deposit products which are generally short term in nature. Interest-bearing checking, savings, and money market accounts generally provide a stable source of funds for the bank and also respond relatively quickly to changes in short term interest rates. The Company offers certificates of deposit with maturities of three months through five years, which serve to extend the duration of the overall deposit portfolio. A significant and increasing portion of the Company's deposit portfolio is concentrated in non-interest-bearing checking accounts. These accounts serve to decrease the Company's overall cost of funds and reduce its sensitivity to changes in short term interest rates.

The Company also maintains a portfolio of wholesale borrowings, predominantly advances from the Federal Home Loan Bank which carry fixed terms and fixed rates of interest. The Company utilizes this portfolio to manage liquidity demands and also, when appropriate, in the ongoing management of interest rate risk.

The Board of Directors, as well as the Office of Thrift Supervision, has established limits on the level of acceptable interest rate risk. There can be no assurance, however, that, in the event of an adverse change in interest rates, the Company's efforts to limit interest rate risk will be successful.

*Net Portfolio Value.* The Company uses a Net Portfolio Value ( NPV ) approach to the quantification of interest rate risk. This approach calculates the difference between the present value of expected cash flows from assets and the present value of expected cash flows from

liabilities, as well as cash flows from any off-balance sheet contracts. Management of the Company's assets and liabilities is performed within the context of the marketplace, but also within limits established by the Board of Directors on the amount of change in NPV that is acceptable given certain interest rate changes.

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Presented below (including discontinued operations), as of March 31, 2009 and September 30, 2008, is an analysis of the Company's interest rate risk as measured by changes in NPV for an instantaneous and sustained parallel shift in the yield curve, in 100 basis point increments, up and down 200 basis points. At March 31, 2009, the Company was similarly exposed to an adjustment in market value in an increasing interest rate environment compared to September 30, 2008. Down 100 basis points and down 200 basis points are not presented for March 31, 2009 due to the extremely low rate environment. At both March 31, 2009 and September 30, 2008, the Company's interest rate risk profile was within the limits set by the Board of Directors. As of March 31, 2009, MetaBank's interest rate risk profile was within the limits set forth by the Office of Thrift Supervision.

| Change in Interest Rates<br>(Basis Points) | Board Limit<br>% Change | At March 31, 2009      |          | At September 30, 2008 |          |
|--------------------------------------------|-------------------------|------------------------|----------|-----------------------|----------|
|                                            |                         | \$ Change              | % Change | \$ Change             | % Change |
|                                            |                         | (Dollars in thousands) |          |                       |          |
| +200 bp                                    | (20)%                   | \$ (6,001)             | (14)%    | \$ (10,035)           | (14)%    |
| +100 bp                                    | (10)                    | (5,628)                | (7)      | (4,739)               | (7)      |
| 0 bp (Base Case)                           |                         |                        |          |                       |          |
| -100 bp                                    | (10)                    |                        |          | 2,447                 | 4        |
| -200 bp                                    | (20)                    |                        |          | 668                   | 1        |

Certain shortcomings are inherent in the method of analysis presented in the preceding table. For example, although certain assets and liabilities may have similar maturities or periods to repricing, they may react in different degrees to changes in market interest rates. Also, the interest rates on certain types of assets and liabilities may fluctuate in advance of changes in market interest rates, while interest rates on other types may lag behind changes in market rates. Additionally, certain assets, such as adjustable-rate mortgage loans, have features that restrict changes in interest rates on a short-term basis and over the life of the asset. Furthermore, although management has estimated changes in the levels of prepayments and early withdrawal in these rate environments, such levels would likely deviate from those assumed in calculating the table. Finally, the ability of some borrowers to service their debt may decrease in the event of an interest rate increase.

In addition to the NPV approach, the Company also reviews gap reports, which measure the differences in assets and liabilities repricing in given time periods, and net income simulations to assess its interest rate risk profile. Management reviews its interest rate risk profile on a quarterly basis.

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Part I. Financial Information

Item 4T. Controls and Procedures

**CONTROLS AND PROCEDURES**

Any control system, no matter how well designed and operated, can provide only reasonable (not absolute) assurance that its objectives will be met. Furthermore, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, have been detected.

**DISCLOSURE CONTROLS AND PROCEDURES**

The Company's management, with the participation of the Company's Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the Company's disclosure controls and procedures, as such term is defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934 (Exchange Act) as of the end of the period covered by the report.

Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that, as of March 31, 2009, the Company's disclosure controls and procedures were effective to provide reasonable assurance that (i) the information required to be disclosed by us in this Report was recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and (ii) information required to be disclosed by us in our reports that we file or submit under the Exchange Act is accumulated and communicated to our management, including our principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

**INTERNAL CONTROL OVER FINANCIAL REPORTING**

With the participation of the Company's management, including its Chief Executive Officer and Chief Financial Officer, the Company also conducted an evaluation of the Company's internal control over financial reporting to determine whether any changes occurred during the Company's fiscal quarter ended March 31, 2009, that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting. Based on such evaluation, management concluded that, as of the end of the period covered by this report, there have not been any changes in the Company's internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the fiscal quarter to which this report relates that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

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**META FINANCIAL GROUP, INC.**

**PART II - OTHER INFORMATION**

**FORM 10-Q**

Item 1. Legal Proceedings See Legal Proceedings of Note 5 to the Notes to Condensed Consolidated Financial Statements, which is incorporated herein by reference.

Item 1A. Risk Factors - In addition to the other information set forth in this report, you should carefully consider the factors discussed in Part I, Item 1A. Risk Factors in our Annual Report on Form 10-K for the year ended September 30, 2008 as well as in our Quarterly Report on Form 10-Q for the period ended December 31, 2008. Additional risks and uncertainties not currently known to us or that we currently deem immaterial may also materially and adversely affect us.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds - None

Item 3. Defaults Upon Senior Securities None

Item 4. Submission of Matters to a Vote of Security Holders

At the Company's Annual Meeting of Shareholders held on January 26, 2009 (the Annual Meeting), the shareholders elected the three individuals nominated to serve as directors until 2012 or until their respective successors are elected and qualified, as set forth in Proposal I in the Company's Proxy Statement relating to the Annual Meeting. The three individuals elected, and the number of votes cast for, or withheld, with respect to each of them, is as follows:

|                    |                |                        |
|--------------------|----------------|------------------------|
| James S. Haahr     | For: 2,189,908 | Vote Withheld: 206,648 |
| Jeanne Partlow     | For: 2,144,393 | Vote Withheld: 252,163 |
| Frederick V. Moore | For: 2,199,843 | Vote Withheld: 196,713 |

The following directors continue to serve on the Board of Directors following the Annual Meeting: J. Tyler Haahr, E. Wayne Cooley, E. Thurman Gaskill, Bradley C. Hanson and Rodney G. Muilenburg.

Item 5. Other Information - None

Item 6. Exhibits

(a) Exhibits:

31.1 Section 302 certification of Chief Executive Officer.  
31.2 Section 302 certification of Chief Financial Officer.  
32.1 Section 906 certification of Chief Executive Officer.  
32.2 Section 906 certification of Chief Financial Officer.

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**META FINANCIAL GROUP, INC.**

**SIGNATURES**

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

**META FINANCIAL GROUP, INC.**

Date: May 14, 2009

By: /s/ J. Tyler Haahr  
J. Tyler Haahr, President, and Chief Executive Officer

Date: May 14, 2009

By: /s/ David W. Leedom  
David W. Leedom, Senior Vice President and Chief Financial Officer