LANDMARK BANCORP INC
Form 10-Q
August 05, 2016

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 June 30, 2016

OR

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

For the transition period from ________ to ________

Commission File Number 0-33203

LANDMARK BANCORP, INC.

(Exact name of registrant as specified in its charter)

Delaware	**43-1930755**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

701 Poyntz Avenue, Manhattan, Kansas 66502

(Address of principal executive offices) (Zip code)

(785) 565-2000
(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 x No ¨

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

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

Large accelerated filer ¨ Accelerated filer ¨ Non-accelerated filer ¨ Smaller reporting company x
(Do not check if a smaller reporting company)

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock as of the latest practicable date: as of August 4, 2016, the issuer had outstanding 3,638,060 shares of its common stock, $.01 par value per share.

LANDMARK BANCORP, INC.

Form 10-Q Quarterly Report

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PART I – FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

LANDMARK BANCORP, INC. AND SUBSIDIARY

CONSOLIDATED BALANCE SHEETS

(Dollars in thousands, except per share amounts)	June 30,	December 31,
	2016	2015
	(Unaudited)	
Assets		
Cash and cash equivalents	$ 14,317	$ 13,569
Investment securities available-for-sale, at fair value	366,550	353,438
Bank Stocks, at cost	4,622	4,497
Loans, net of allowance for loans losses of $5,652 and $5,922	430,064	419,923
Loans held for sale, net	10,057	14,465
Premises and equipment, net	20,760	20,958
Bank owned life insurance	18,078	18,164
Goodwill	17,532	17,532
Other intangible assets, net	4,148	4,304
Real estate owned, net	718	1,000
Accrued interest and other assets	9,476	10,526
Total assets	$ 896,322	$ 878,376
Liabilities and Stockholders' Equity		
Liabilities:		
Deposits:		
Non-interest-bearing demand	$ 151,049	$ 143,616
Money market and checking	328,816	346,106
Savings	87,106	81,062
Time	148,650	143,943
Total deposits	715,621	714,727
Federal Home Loan Bank borrowings	48,000	37,600
Subordinated debentures	21,184	21,084
Other borrowings	11,527	11,974
Accrued interest, taxes, and other liabilities	10,623	12,421
Total liabilities	806,955	797,806

Commitments and contingencies		
Stockholders' equity:		
Preferred stock, $0.01 par value per share, 200,000 shares authorized; none issued	-	-
Common stock, $0.01 par value per share, 7,500,000 shares authorized; 3,620,669 and 3,531,036 shares issued and outstanding at June 30, 2016 and December 31, 2015, respectively	36	35
Additional paid-in capital	46,763	45,372
Retained earnings	36,073	32,988
Accumulated other comprehensive income	6,495	2,175
Total stockholders' equity	89,367	80,570
Total liabilities and stockholders' equity	$ 896,322	$ 878,376

See accompanying notes to consolidated financial statements.

LANDMARK BANCORP, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF EARNINGS

(Unaudited)

(Dollars in thousands, except per share amounts)	Three months ended June 30,		Six months ended June 30,	
	2016	2015	2016	2015
Interest income:				
Loans:				
Taxable	$ 5,285	$ 5,436	$ 10,420	$ 10,556
Tax-exempt	60	75	127	143
Investment securities:				
Taxable	1,171	1,146	2,335	2,343
Tax-exempt	856	736	1,664	1,414
Total interest income	7,372	7,393	14,546	14,456
Interest expense:				
Deposits	287	272	564	550
Borrowings	523	497	1,016	988
Total interest expense	810	769	1,580	1,538
Net interest income	6,562	6,624	12,966	12,918
Provision for loan losses	300	200	350	(800)
Net interest income after provision for loan losses	6,262	6,424	12,616	13,718
Non-interest income:				
Fees and service charges	1,847	1,813	3,576	3,495
Gains on sales of loans, net	1,405	2,251	3,199	4,194
Bank owned life insurance	145	123	265	245
Gains (losses) on sales of investment securities, net	285	-	297	(254)
Other	266	495	505	765
Total non-interest income	3,948	4,682	7,842	8,445
Non-interest expense:				
Compensation and benefits	3,777	3,845	7,578	7,566
Occupancy and equipment	1,055	1,059	2,111	2,130
Amortization of intangibles	331	346	668	681
Data processing	346	342	657	689
Professional fees	282	259	501	493
Advertising	166	125	332	249
Federal deposit insurance premiums	110	105	220	224
Foreclosure and real estate owned expense	51	20	116	45
Other	1,093	1,342	2,190	2,477
Total non-interest expense	7,211	7,443	14,373	14,554
Earnings before income taxes	2,999	3,663	6,085	7,609
Income tax expense	754	1,047	1,563	2,216

Net earnings	$ 2,245	$ 2,616	$4,522	$5,393
Earnings per share:				
Basic (1)	$ 0.62	$ 0.75	$1.26	$1.54
Diluted (1)	$ 0.61	$ 0.72	$1.24	$1.50
Dividends per share (1)	$ 0.20	$ 0.18	$0.40	$0.36

(1) Per share amounts for the periods ended June 30, 2015 have been adjusted to give effect to the 5% stock dividend paid during December 2015.

See accompanying notes to consolidated financial statements.

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LANDMARK BANCORP, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited)

(Dollars in thousands)	Three months ended June 30,		Six months ended June 30,	
	2016	2015	2016	2015
Net earnings	$ 2,245	$ 2,616	$ 4,522	$ 5,393
Net unrealized holding gains (losses) on available-for-sale securities	3,771	(3,235)	7,161	(1,322)
Reclassification adjustment for net (gains) losses included in earnings	(285)	-	(297)	254
Net unrealized gains (losses)	3,486	(3,235)	6,864	(1,068)
Income tax effect on net (gains) losses included in earnings	105	-	110	(94)
Income tax effect on net unrealized holding (gains) losses	(1,396)	1,201	(2,654)	493
Other comprehensive income (loss)	2,195	(2,034)	4,320	(669)
Total comprehensive income	$ 4,440	$ 582	$ 8,842	$ 4,724

See accompanying notes to consolidated financial statements.

LANDMARK BANCORP, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

(Unaudited)

(Dollars in thousands, except per share amounts)	Common stock	Additional paid-in capital	Retained earnings	Accumulated other comprehensive income (loss)	Total
Balance at January 1, 2015	$ 33	$ 40,473	$ 29,321	$ 1,818	$ 71,645
Net earnings	-	-	5,393	-	5,393
Other comprehensive loss	-	-	-	(669)	(669)
Dividends paid ($0.36 per share)	-	-	(1,268)	-	(1,268)
Stock-based compensation	-	16	-	-	16
Exercise of stock options, 4,181 shares, including excess tax benefit of $5	-	79	-	-	79
Balance at June 30, 2015	$ 33	$ 40,568	$ 33,446	$ 1,149	$ 75,196
Balance at January 1, 2016	$ 35	$ 45,372	$ 32,988	$ 2,175	$ 80,570
Net earnings	-	-	4,522	-	4,522
Other comprehensive income	-	-	-	4,320	4,320
Dividends paid ($0.40 per share)	-	-	(1,437)	-	(1,437)
Exercise of stock options, 89,633 shares, including excess tax benefit of $197	1	1,391	-	-	1,392
Balance at June 30, 2016	$ 36	$ 46,763	$ 36,073	$ 6,495	$ 89,367

See accompanying notes to consolidated financial statements.

LANDMARK BANCORP, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(Dollars in thousands)	Six months ended June 30, 2016	2015
Cash flows from operating activities:		
Net earnings	$4,522	$5,393
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Provision for loan losses	350	(800)
Amortization of investment security premiums, net	818	767
Amortization of purchase accounting adjustment on loans	(57)	(362)
Amortization of purchase accounting adjustment on subordinated debentures	100	100
Amortization of intangibles	668	681
Depreciation	581	577
Increase in cash surrender value of bank owned life insurance	(265)	(245)
Stock-based compensation	-	16
Deferred income taxes	229	215
Net (gains) losses on sales of investment securities	(297)	254
Impairment of affordable housing investment	-	163
Net loss (gain) on sales of premises, equipment and real estate owned	72	(236)
Net gains on sales of loans	(3,199)	(4,194)
Proceeds from sales of loans	121,551	148,064
Origination of loans held for sale	(113,944)	(151,326)
Changes in assets and liabilities:		
Accrued interest and other assets	(1,536)	(1,534)
Accrued expenses, taxes, and other liabilities	(2,538)	(1,237)
Net cash provided by (used in) operating activities	7,055	(3,704)
Cash flows from investing activities:		
Net increase in loans	(10,932)	(3,659)
Maturities and prepayments of investment securities	23,429	34,411
Purchases of investment securities	(43,815)	(62,094)
Proceeds from sales of investment securities	13,617	19,069
Redemption of bank stocks	3,009	4,769
Purchase of bank stocks	(3,134)	(5,951)
Proceeds from sales of premises and equipment and foreclosed assets	749	219
Proceeds from bank owned life insurance	351	-
Purchases of premises and equipment, net	(386)	(509)
Net cash used in investing activities	(17,112)	(13,745)
Cash flows from financing activities:		
Net increase (decrease) in deposits	897	(5,005)
Federal Home Loan Bank advance borrowings	156,291	131,251

Federal Home Loan Bank advance repayments	(145,891)	(103,945)
Proceeds from other borrowings	-	1,400
Repayments on other borrowings	(447)	(2,688)
Proceeds from exercise of stock options, including excess tax benefit	1,392	79
Payment of dividends	(1,437)	(1,268)
Net cash provided by financing activities	10,805	19,824
Net increase in cash and cash equivalents	748	2,375
Cash and cash equivalents at beginning of period	13,569	12,760
Cash and cash equivalents at end of period	$14,317	$15,135

(Continued)

LANDMARK BANCORP, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS, CONTINUED

(Unaudited)

(Dollars in thousands)	Six months ended June 30,	
	2016	2015
Supplemental disclosure of cash flow information:		
Cash payments for income taxes	$ 500	$ 1,890
Cash paid for interest	1,599	1,551
Supplemental schedule of noncash investing and financing activities:		
Transfer of loans to real estate owned	536	24
Investment securities purchases not yet settled	-	(2,817)

See accompanying notes to consolidated financial statements.

LANDMARK BANCORP, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Interim Financial Statements

The unaudited consolidated financial statements of Landmark Bancorp, Inc. (the “Company”) and subsidiary have been prepared in accordance with the instructions to Form 10-Q. Accordingly, they do not include all the information and footnotes required by generally accepted accounting principles ("GAAP") for complete financial statements and should be read in conjunction with the Company’s most recent annual report on Form 10-K, containing the latest audited consolidated financial statements and notes thereto. The consolidated financial statements in this report have not been audited by an independent registered public accounting firm, but in the opinion of management, all adjustments, consisting of normal recurring accruals, considered necessary for a fair presentation of financial statements have been reflected herein. The results of the six months ended June 30, 2016 are not necessarily indicative of the results expected for the year ending December 31, 2016 or for any other period. The Company has evaluated subsequent events for recognition and disclosure up to the date the financial statements were issued.

2. Investments

A summary of investment securities available-for-sale is as follows:

	As of June 30, 2016			
(Dollars in thousands)	Amortized cost	Gross unrealized gains	Gross unrealized losses	Estimated fair value
U. S. treasury securities	$ 6,011	$ 38	$ -	$ 6,049
U. S. federal agency obligations	27,721	269	(5)	27,985
Municipal obligations, tax exempt	150,554	5,203	(22)	155,735
Municipal obligations, taxable	71,998	2,268	-	74,266
Agency mortgage-backed securities	89,731	1,781	(11)	91,501
Common stocks	562	752	-	1,314
Certificates of deposit	9,700	-	-	9,700
Total	$ 356,277	$ 10,311	$ (38)	$ 366,550

	As of December 31, 2015			
	Amortized	Gross unrealized	Gross unrealized	Estimated

(Dollars in thousands)	cost	gains	losses	fair value
U. S. treasury securities	$6,517	$ 1	$ (1)	$6,517
U. S. federal agency obligations	30,064	43	(187)	29,920
Municipal obligations, tax exempt	135,341	2,671	(71)	137,941
Municipal obligations, taxable	81,999	472	(581)	81,890
Agency mortgage-backed securities	85,829	391	(235)	85,985
Common stocks	580	906	-	1,486
Certificates of deposit	9,699	-	-	9,699
Total	$350,029	$ 4,484	$ (1,075)	$353,438

The tables above show that some of the securities in the available-for-sale investment portfolio had unrealized losses, or were temporarily impaired, as of June 30, 2016 and December 31, 2015. This temporary impairment represents the estimated amount of loss that would be realized if the securities were sold on the valuation date. Securities which were temporarily impaired are shown below, along with the length of time in a continuous unrealized loss position.

		As of June 30, 2016					
(Dollars in thousands)		Less than 12 months		12 months or longer		Total	
	No. of securities	Fair value	Unrealized losses	Fair value	Unrealized losses	Fair value	Unrealized losses
U.S. federal agency obligations	1	$-	$ -	$ 3,200	$ (5)	$3,200	$ (5)
Municipal obligations, tax exempt	20	4,313	(20)	626	(2)	4,939	(22)
Agency mortgage-backed securities	12	645	(1)	1,907	(10)	2,552	(11)
Total	33	$4,958	$ (21)	$ 5,733	$ (17)	$10,691	$ (38)

		As of December 31, 2015					
(Dollars in thousands)		Less than 12 months		12 months or longer		Total	
	No. of securities	Fair value	Unrealized losses	Fair value	Unrealized losses	Fair value	Unrealized losses
U.S. treasury securities	2	$3,542	$ (1)	$ -	$ -	$3,542	$ (1)
U. S. federal agency obligations	18	23,015	(163)	1,976	(24)	24,991	(187)
Municipal obligations, tax exempt	47	11,328	(53)	2,132	(18)	13,460	(71)
Municipal obligations, taxable	105	38,605	(494)	5,068	(87)	43,673	(581)
Agency mortgage-backed securities	40	29,814	(166)	2,925	(69)	32,739	(235)
Total	212	$106,304	$ (877)	$ 12,101	$ (198)	$118,405	$ (1,075)

The Company's U.S. federal agency portfolio consists of securities issued by the government-sponsored agencies of Federal Home Loan Mortgage Corporation ("FHLMC"), Federal National Mortgage Association ("FNMA") and Federal Home Loan Bank ("FHLB"). The receipt of principal and interest on U.S. federal agency obligations is guaranteed by the respective government-sponsored agency guarantor, such that the Company believes that its U.S. federal agency obligations do not expose the Company to credit-related losses. Based on these factors, along with the Company's intent to not sell the securities and its belief that it was more likely than not that the Company will not be required to sell the securities before recovery of their cost basis, the Company believed that the U.S. federal agency obligations identified in the tables above were temporarily impaired as of the date of the respective table.

The Company's portfolio of municipal obligations consists of both tax-exempt and taxable general obligations securities issued by various municipalities. As of June 30, 2016, the Company did not intend to sell and it was more likely than not that the Company will not be required to sell its municipal obligations in an unrealized loss position until the recovery of their costs. Due to the issuers' continued satisfaction of the securities' obligations in accordance with their contractual terms and the expectation that they will continue to do so, the evaluation of the fundamentals of

the issuers' financial condition and other objective evidence, the Company believed that the municipal obligations identified in the tables above were temporarily impaired as of the date of the respective table.

The Company's agency mortgage-backed securities portfolio consists of securities underwritten to the standards of and guaranteed by the government-sponsored agencies of FHLMC, FNMA and the Government National Mortgage Association ("GNMA"). The receipt of principal, at par, and interest on agency mortgage-backed securities is guaranteed by the respective government-sponsored agency guarantor, such that the Company believed that its agency mortgage-backed securities did not expose the Company to credit-related losses. Based on these factors, along with the Company's intent to not sell the securities and the Company's belief that it was more likely than not that the Company will not be required to sell the securities before recovery of their cost basis, the Company believed that the agency mortgage-backed securities identified in the tables above were temporarily impaired as of the date of the respective table.

The table below of the amortized cost and estimated fair value of investment securities includes scheduled principal payments and estimated prepayments, based on observable market inputs, for agency mortgage-backed securities. Actual maturities will differ from contractual maturities because borrowers have the right to prepay obligations with or without prepayment penalties. The amortized cost and fair value of investment securities at June 30, 2016 are as follows:

(Dollars in thousands)	Amortized cost	Estimated fair value
Due in less than one year	$ 17,508	$ 17,598
Due after one year but within five years	180,166	182,762
Due after five years but within ten years	88,657	92,255
Due after ten years	69,384	72,621
Common stocks	562	1,314
Total	$ 356,277	$ 366,550

Sales proceeds and gross realized gains and losses on sales of available-for-sale securities are as follows:

(Dollars in thousands)	Three months ended June 30,		Six months ended June 30,	
	2016	2015	2016	2015
Sales proceeds	$ 11,801	$ -	$ 13,617	$ 19,069
Realized gains	$ 296	$ -	$ 312	$ 24
Realized losses	(11)	-	(15)	(278)
Net realized losses	$ 285	$ -	$ 297	$ (254)

Securities with carrying values of $201.8 million and $171.6 million were pledged to secure public funds on deposit, repurchase agreements and as collateral for borrowings at June 30, 2016 and December 31, 2015, respectively. Except for U.S. federal agency obligations, no investment in a single issuer exceeded 10% of consolidated stockholders' equity.

3. Loans and Allowance for Loan Losses

Loans consisted of the following as of the dates indicated below:

	June 30,	December 31,

(Dollars in thousands)	2016	2015
One-to-four family residential real estate	$130,753	$ 131,930
Construction and land	18,381	15,043
Commercial real estate	119,147	118,983
Commercial loans	62,120	61,300
Agriculture loans	78,817	71,030
Municipal loans	7,263	7,635
Consumer loans	19,203	19,895
Total gross loans	435,684	425,816
Net deferred loan costs and loans in process	32	29
Allowance for loan losses	(5,652)	(5,922)
Loans, net	$430,064	$ 419,923

The following tables provide information on the Company's activity in the allowance for loan losses by loan class:

(Dollars in thousands)	Three and six months ended June 30, 2016 One-to-four family residential real estate	Construction and land	Commercial real estate	Commercial loans	Agriculture loans	Municipal loans	Consumer loans	Total
Allowance for loan losses:								
Balance at April 1, 2016	$864	$ 82	$ 1,831	$ 1,384	$ 1,483	$ 24	$ 201	$5,869
Charge-offs	-	-	-	(306)	(83)	-	(148)	(537)
Recoveries	3	-	-	1	-	6	10	20
Provision for loan losses	(283)	7	(55)	314	200	(7)	124	300
Balance at June 30, 2016	584	89	1,776	1,393	1,600	23	187	5,652
Balance at January 1, 2016	$925	$ 77	$ 1,740	$ 1,530	$ 1,428	$ 23	$ 199	$5,922
Charge-offs	-	-	-	(306)	(83)	-	(285)	(674)
Recoveries	5	-	-	20	-	6	23	54
Provision for loan losses	(346)	12	36	149	255	(6)	250	350
Balance at June 30, 2016	584	89	1,776	1,393	1,600	23	187	5,652

(Dollars in thousands)	Three and six months ended June 30, 2015 One-to-four family residential real estate	Construction and land	Commercial real estate	Commercial loans	Agriculture loans	Municipal loans	Consumer loans	Total
Allowance for loan losses:								
Balance at April 1, 2015	$1,386	$ 103	$ 1,600	$ 1,515	$ 1,104	$ 25	$ 172	$5,905
Charge-offs	(9)	-	-	(10)	-	-	(88)	(107)
Recoveries	3	4	2	2	-	-	8	19
Provision for loan losses	(55)	(9)	(63)	249	(2)	(4)	84	200
Balance at June 30, 2015	1,325	99	1,539	1,756	1,102	21	176	6,018
Balance at January 1, 2015	$755	$ 762	$ 1,832	$ 836	$ 915	$ 51	$ 169	$5,320
Charge-offs	(9)	-	-	(10)	-	(88)	(142)	(249)
Recoveries	5	1,719	2	3	-	-	18	1,747
Provision for loan losses	574	(2,382)	(295)	927	187	58	131	(800)
Balance at June 30, 2015	1,325	99	1,539	1,756	1,102	21	176	6,018

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The following tables provide information on the Company's activity in the allowance for loan losses by loan class and allowance methodology:

(Dollars in thousands)	As of June 30, 2016 One-to-four family residential real estate	Construction and land	Commercial real estate	Commercial loans	Agriculture loans	Municipal loans	Consumer loans	Total
Allowance for loan losses:								
Individually evaluated for loss	19	-	-	13	206	-	7	245
Collectively evaluated for loss	565	89	1,776	1,380	1,394	23	180	5,407
Total	584	89	1,776	1,393	1,600	23	187	5,652
Loan balances:								
Individually evaluated for loss	1,106	2,061	2,417	127	879	393	102	7,085
Collectively evaluated for loss	129,647	16,320	116,730	61,993	77,938	6,870	19,101	428,599
Total	$ 130,753	$ 18,381	$ 119,147	$ 62,120	$ 78,817	$ 7,263	$ 19,203	$ 435,684

(Dollars in thousands)	As of December 31, 2015 One-to-four family residential real estate	Construction and land	Commercial real estate	Commercial loans	Agriculture loans	Municipal loans	Consumer loans	Total
Allowance for loan losses:								
Individually evaluated for loss	78	-	-	-	-	-	10	88
Collectively evaluated for loss	847	77	1,740	1,530	1,428	23	189	5,834
Total	925	77	1,740	1,530	1,428	23	199	5,922
Loan balances:								
Individually evaluated for loss	752	2,220	2,429	620	189	591	36	6,837
Collectively evaluated for loss	131,178	12,823	116,554	60,680	70,841	7,044	19,859	418,979
Total	$ 131,930	$ 15,043	$ 118,983	$ 61,300	$ 71,030	$ 7,635	$ 19,895	$ 425,816

The Company recorded net loan charge-offs of $620,000 during the first six months of 2016 compared to net loan recoveries of $1.5 million during the first six months of 2015. The net loan charge-offs during the first six months of 2016 were primarily related to the liquidation of the assets securing a previously identified and impaired commercial loan. The charge-off associated with this commercial loan exceeded the related allowance recorded at March 31, 2016, which contributed to provision for loan losses during the second quarter of 2016. The net loan recoveries during 2015 were primarily associated with the recovery of $1.7 million on a $4.3 million construction loan which was fully charged-off during 2010 and 2011. As of June 30, 2016, the Company has recovered approximately $2.4 million of the loan and continues to pursue collection of the remaining amount.

The Company's impaired loans increased from $6.8 million at December 31, 2015 to $7.1 million at June 30, 2016. The difference between the unpaid contractual principal and the impaired loan balance is a result of charge-offs recorded against impaired loans. The difference in the Company's non-accrual loan balances and impaired loan balances at June 30, 2016 and December 31, 2015, was related to troubled debt restructurings ("TDR") that are current and accruing interest, but still classified as impaired. Interest income recognized on a cash basis was immaterial during the six months ended June 30, 2016 and 2015. The following tables present information on impaired loans:

(Dollars in thousands)	As of June 30, 2016						
	Unpaid contractual principal	Impaired loan balance	Impaired loans without an allowance	Impaired loans with an allowance	Related allowance recorded	Year-to-date average loan balance	Year-to-date interest income recognized
One-to-four family residential real estate	$1,106	$ 1,106	$ 502	$ 604	$ 19	$ 1,117	$ 4
Construction and land	3,796	2,061	2,061	-	-	2,137	38
Commercial real estate	2,417	2,417	2,417	-	-	2,426	253
Commercial loans	127	127	75	52	13	148	1
Agriculture loans	879	879	225	654	206	918	1
Municipal loans	393	393	393	-	-	514	8
Consumer loans	102	102	86	16	7	106	-
Total impaired loans	$8,820	$ 7,085	$ 5,759	$ 1,326	$ 245	$ 7,366	$ 305

(Dollars in thousands)	As of December 31, 2015						
	Unpaid contractual principal	Impaired loan balance	Impaired loans without an allowance	Impaired loans with an allowance	Related allowance recorded	Year-to-date average loan balance	Year-to-date interest income recognized
One-to-four family residential real estate	$752	$ 752	$ 408	$ 344	$ 78	$ 1,041	$ -
Construction and land	3,955	2,220	2,220	-	-	2,389	88
Commercial real estate	2,429	2,429	2,429	-	-	2,484	175
Commercial loans	637	620	620	-	-	634	3
Agriculture loans	189	189	189	-	-	188	3
Municipal loans	591	591	591	-	-	631	19
Consumer loans	36	36	10	26	10	41	-
Total impaired loans	$8,589	$ 6,837	$ 6,467	$ 370	$ 88	$ 7,408	$ 288

The Company’s key credit quality indicator is a loan’s performance status, defined as accruing or non-accruing. Performing loans are considered to have a lower risk of loss. Non-accrual loans are those which the Company believes have a higher risk of loss. The accrual of interest on non-performing loans is discontinued at the time the loan is ninety days delinquent, unless the credit is well secured and in process of collection. Loans are placed on non-accrual or are charged off at an earlier date if collection of principal or interest is considered doubtful. There were no loans ninety days delinquent and accruing interest at December 31, 2015. The following tables present information on the Company’s past due and non-accrual loans by loan class:

(Dollars in thousands)	As of June 30, 2016						
	30-59 days delinquent and accruing	60-89 days delinquent and accruing	90 days or more delinquent and accruing	Total past due loans accruing	Non-accrual loans	Total past due and non-accrual loans	Total loans not past due
One-to-four family residential real estate	$ 140	$ 512	$ -	$ 652	$ 916	$ 1,568	$ 129,185
Construction and land	5	-	-	5	607	612	17,769
Commercial real estate	10	237	-	247	39	286	118,861
Commercial loans	-	-	-	-	96	96	62,024
Agriculture loans	174	30	218	422	834	1,256	77,561
Municipal loans	-	-	-	-	-	-	7,263
Consumer loans	82	23	-	105	102	207	18,996
Total	$ 411	$ 802	$ 218	$ 1,431	$ 2,594	$ 4,025	$ 431,659
Percent of gross loans	0.09 %	0.18 %	0.05 %	0.32 %	0.60 %	0.92 %	99.08 %

(Dollars in thousands)	As of December 31, 2015						
	30-59 days delinquent and accruing	60-89 days delinquent and accruing	90 days or more delinquent and accruing	Total past due loans accruing	Non-accrual loans	Total past due and non-accrual loans	Total loans not past due
One-to-four family residential real estate	$ 70	$ 712	$ -	$ 782	$ 749	$ 1,531	$ 130,399
Construction and land	4	-	-	4	614	618	14,425
Commercial real estate	240	-	-	240	47	287	118,696
Commercial loans	90	40	-	130	583	713	60,587
Agriculture loans	174	5	-	179	139	318	70,712
Municipal loans	-	-	-	-	-	-	7,635
Consumer loans	65	2	-	67	36	103	19,792
Total	$ 643	$ 759	$ -	$ 1,402	$ 2,168	$ 3,570	$ 422,246
Percent of gross loans	0.15 %	0.18 %	0.00 %	0.33 %	0.51 %	0.84 %	99.16 %

Under the original terms of the Company's non-accrual loans, interest earned on such loans for the six months ended June 30, 2016 and 2015, would have increased interest income by $44,000 and $237,000, respectively. No interest income related to non-accrual loans was included in interest income for the six months ended June 30, 2016 and 2015.

The Company also categorizes loans into risk categories based on relevant information about the ability of the borrowers to service their debt such as current financial information, historical payment experience, credit documentation, public information and current economic trends, among other factors. The Company analyzes loans

individually by classifying the loans as to credit risk. This analysis is performed on a quarterly basis. Non-classified loans generally include those loans that are expected to be repaid in accordance with contractual loan terms. Classified loans are those that are assigned a special mention, substandard or doubtful risk rating using the following definitions:

Special Mention: Loans are currently protected by the current net worth and paying capacity of the obligor or of the collateral pledged but such protection is potentially weak. These loans constitute an undue and unwarranted credit risk, but not to the point of justifying a classification of substandard. The credit risk may be relatively minor, yet constitutes an unwarranted risk in light of the circumstances surrounding a specific asset.

Substandard: Loans are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged. Loans have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. Loans are characterized by the distinct possibility that the Company will sustain some loss if the deficiencies are not corrected.

Doubtful: Loans classified doubtful have all the weaknesses inherent in those classified as substandard, with the added characteristic that weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable and improbable.

The following table provides information on the Company's risk categories by loan class:

(Dollars in thousands)	As of June 30, 2016		As of December 31, 2015	
	Nonclassified	Classified	Nonclassified	Classified
One-to-four family residential real estate	$ 129,286	$ 1,467	$ 130,575	$ 1,355
Construction and land	17,638	743	14,429	614
Commercial real estate	109,454	9,693	111,016	7,967
Commercial loans	58,875	3,245	58,862	2,438
Agriculture loans	72,179	6,638	68,186	2,844
Municipal loans	7,263	-	7,635	-
Consumer loans	19,084	119	19,839	56
Total	413,779	21,905	410,542	15,274

At June 30, 2016, the Company had ten loan relationships consisting of fourteen outstanding loans that were classified as TDRs. During the second quarter of 2016, the Company classified a $8,000 commercial loan as a TDR after modifying the payments to interest only. Also during the second quarter of 2016, the Company classified a $188,000 one-to-four family residential real estate loan as a TDR after agreeing to a loan modification which adjusted the payment schedule. Since all of the loans were adequately secured, no charge-offs or provisions for loan losses were recorded against the principal as of June 30, 2016. No loan modifications were classified as TDRs during the first quarter 2016. During the second quarter of 2015, the Company classified a commercial loan relationship consisting of $2.7 million in real estate and land loans as a TDR after agreeing to a bankruptcy plan with the borrower. The bankruptcy plan restarted the amortization period of the loans which extended the maturities of the loans. During the first quarter of 2015, the Company classified a $44,000 agriculture loan relationship consisting of two loans as a TDR after extending the maturity of the loans. During the first six months of 2016, a $56,000 one-to-four family residential real estate loan and a $25,000 agriculture loan, which were both classified as TDRs during 2015 were paid off.

The Company evaluates each TDR individually and returns the loan to accrual status when a payment history is established after the restructuring and future payments are reasonably assured. There were no loans modified as TDRs for which there was a payment default within 12 months of modification as of June 30, 2016 and 2015. At June 30, 2016, there was a commitment of $84,000 to lend additional funds on one construction and land loan classified as a TDR. The Company had no allowance recorded against loans classified as TDRs at June 30, 2016 or December 31, 2015.

The following table presents information on loans that are classified as TDRs:

(Dollars in thousands)	As of June 30, 2016	As of December 31, 2015

	Number of loans	Non-accrual balance	Accruing balance	Number of loans	Non-accrual balance	Accruing balance
One-to-four family residential real estate	2	$ -	$ 190	2	$ 55	$ 3
Construction and land	4	594	1,454	4	600	1,606
Commercial real estate	3	-	2,378	3	-	2,382
Commercial loans	2	-	31	1	-	37
Agriculture	1	-	45	2	-	50
Municipal loans	2	-	393	2	-	591
Total troubled debt restructurings	14	$ 594	$ 4,491	14	$ 655	$ 4,669

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4. Goodwill and Other Intangible Assets

The Company tests goodwill for impairment annually or more frequently if circumstances warrant. The Company's annual step one impairment test as of December 31, 2015 concluded that its goodwill was not impaired. The Company concluded there were no triggering events during the first six months of 2016 that required an interim goodwill impairment test.

Lease intangible assets are amortized over the life of the lease. Core deposit intangible assets are amortized over the estimated useful life of ten years on an accelerated basis. A summary of the other intangible assets that continue to be subject to amortization is as follows:

(Dollars in thousands)	As of June 30, 2016		
	Gross carrying amount	Accumulated amortization	Net carrying amount
Core deposit intangible assets	$2,067	$ (1,000)	$ 1,067
Lease intangible asset	350	(120)	230
Mortgage servicing rights	5,580	(2,729)	2,851
Total other intangible assets	$7,997	$ (3,849)	$ 4,148

(Dollars in thousands)	As of December 31, 2015		
	Gross carrying amount	Accumulated amortization	Net carrying amount
Core deposit intangible assets	$2,067	$ (855)	$ 1,212
Lease intangible asset	350	(98)	252
Mortgage servicing rights	5,322	(2,482)	2,840
Total other intangible assets	$7,739	$ (3,435)	$ 4,304

The following sets forth estimated amortization expense for core deposit and lease intangible assets for the remainder of 2016 and in successive years ending December 31:

(Dollars in thousands)	Amortization expense
Remainder of 2016	$ 160
2017	289
2018	252
2019	214
2020	177
Thereafter	205

Total	$ 1,297

Mortgage loans serviced for others are not reported as assets. The following table provides information on the principal balances of mortgage loans serviced for others:

(Dollars in thousands)	June 30, 2016	December 31, 2015
FHLMC	$467,663	$ 444,714
FHLB	12,685	14,039

Custodial escrow balances maintained in connection with serviced loans were $4.5 million and $3.5 million at June 30, 2016 and December 31, 2015, respectively. Gross service fee income related to such loans was $304,000 and $268,000 for the three months ended June 30, 2016 and 2015, respectively, and is included in fees and service charges in the consolidated statements of earnings. Gross service fee income related to such loans was $604,000 and $523,000 for the six months ended June 30, 2016 and 2015, respectively.

Activity for mortgage servicing rights and the related valuation allowance follows:

(Dollars in thousands)	Three months ended June 30,		Six months ended June 30,	
	2016	2015	2016	2015
Mortgage servicing rights:				
Balance at beginning of period	$ 2,808	$ 2,557	$ 2,840	$ 2,477
Additions	291	408	512	710
Amortization	(248)	(236)	(501)	(458)
Balance at end of period	$ 2,851	$ 2,729	$ 2,851	$ 2,729

The fair value of mortgage servicing rights was $4.1 million and $4.6 million at June 30, 2016 and December 31, 2015, respectively. Fair value at June 30, 2016 was determined using discount rates ranging from 9.50% to 9.52%; prepayment speeds ranging from 6.14% to 14.98%, depending on the stratification of the specific mortgage servicing right; and a weighted average default rate of 2.16%. Fair value at December 31, 2015 was determined using discount rates ranging from 9.50% to 10.00%; prepayment speeds ranging from 5.15% to 33.78%, depending on the stratification of the specific mortgage servicing right; and a weighted average default rate of 2.25%.

The Company had a mortgage repurchase reserve of $361,000 and $351,000 at June 30, 2016 and December 31, 2015, respectively, which represents the Company's best estimate of probable losses that the Company will incur related to the repurchase of one-to-four family residential real estate loans previously sold or to reimburse investors for credit losses incurred on loans previously sold where a breach of the contractual representations and warranties occurred. The Company did not incur any losses charged against the reserve or make any provisions to the reserve during the first six months of 2016 and 2015. The Company recovered $3,000 of losses during the three months ended June 30, 2016 and $10,000 of losses against the mortgage repurchase reserve during the six months ended June 30, 2016. As of June 30, 2016, the Company did not have any outstanding mortgage repurchase requests.

5. Earnings per Share

Basic earnings per share have been computed based upon the weighted average number of common shares outstanding during each period. Diluted earnings per share include the effect of all potential common shares outstanding during each period. The shares used in the calculation of basic and diluted earnings per share are shown below:

(Dollars in thousands, except per share amounts)	Three months ended June 30		Six months ended June 30	
	2016	2015	2016	2015
Net earnings	$2,245	$2,616	$4,522	$5,393

Weighted average common shares outstanding - basic (1)	3,613,671	3,504,295	3,585,235	3,503,495
Assumed exercise of stock options (1)	76,324	109,128	75,064	103,749
Weighted average common shares outstanding - diluted (1)	3,689,995	3,613,423	3,660,299	3,607,244
Net earnings per share (1):				
Basic	$0.62	$0.75	$1.26	$1.54
Diluted	$0.61	$0.72	$1.24	$1.50

(1) Share and per share values for the periods ended June 30, 2015 have been adjusted to give effect to the 5% stock dividend paid during December 2015.

The diluted earnings per share computations for the three and six months ended June 30, 2016 and 2015 include all unexercised stock options because no stock options were anti-dilutive during such periods.

6. Repurchase Agreements

The Company has overnight repurchase agreements with certain deposit customers whereby the Company uses investment securities as collateral for non-insured funds. These balances are accounted for as collateralized financing and included in other borrowings on the balance sheet. The following is a summary of the balances of and collateral for the Company's repurchase agreements:

	As of June 30, 2016				
	Overnight and Continuous	Up to 30 days	30-90 days	Greater than 90 days	Total
Repurchase agreements:					
U.S. federal agency obligations	$5,063	$ -	$ -	$ -	$5,063
Agency mortgage-backed securities	6,464	-	-	-	6,464
Total	$11,527	$ -	$ -	$ -	$11,527

	As of December 31, 2015				
	Overnight and Continuous	Up to 30 days	30-90 days	Greater than 90 days	Total
Repurchase agreements:					
U.S. federal agency obligations	$5,810	$ -	$ -	$ -	$5,810
Agency mortgage-backed securities	6,164	-	-	-	6,164
Total	$11,974	$ -	$ -	$ -	$11,974

Repurchase agreements are comprised of non-insured customer funds, totaling $11.5 million at June 30, 2016, and $12.0 million at December 31, 2015, which were secured by $17.3 million and $15.7 million of the Company's investment portfolio at the same dates, respectively.

The investment securities are held by a third-party financial institution in the customer's custodial account. The Company is required to maintain adequate collateral for each repurchase agreement. Changes in the fair value of the investment securities impact the amount of collateral required. If the Company were to default, the investment securities would be used to settle the repurchase agreement with the deposit customer.

7. Fair Value of Financial Instruments and Fair Value Measurements

Fair value is the exchange price that would be received for an asset or paid to transfer a liability (exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. There are three levels of inputs that may be used to measure fair values:

Level 1 – Quoted prices (unadjusted) for identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.

Level 2 – Significant other observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

Level 3 – Significant unobservable inputs that reflect a company's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

Fair value estimates of the Company's financial instruments as of June 30, 2016 and December 31, 2015, including methods and assumptions utilized, are set forth below:

(Dollars in thousands)	As of June 30, 2016				
	Carrying amount	Level 1	Level 2	Level 3	Total
Financial assets:					
Cash and cash equivalents	$14,317	$14,317	$-	$-	$14,317
Investment securities available-for-sale	366,550	7,363	359,187	-	366,550
Bank stocks, at cost	4,622	n/a	n/a	n/a	n/a
Loans, net	430,064	-	-	431,483	431,483
Loans held for sale, net	10,057	-	10,062	-	10,062
Derivative financial instruments	615	-	615	-	615
Accrued interest receivable	3,927	22	1,979	1,926	3,927
Financial liabilities:					
Non-maturity deposits	$(566,971)	$(566,971)	$-	$-	(566,971)
Time deposits	(148,650)	-	(148,116)	-	(148,116)
FHLB borrowings	(48,000)	-	(49,247)	-	(49,247)
Subordinated debentures	(21,184)	-	(18,812)	-	(18,812)
Other borrowings	(11,527)	-	(11,527)	-	(11,527)
Accrued interest payable	(271)	-	(271)	-	(271)

	As of December 31, 2015				
	Carrying amount	Level 1	Level 2	Level 3	Total
Financial assets:					
Cash and cash equivalents	$13,569	$13,569	$-	$-	$13,569
Investment securities available-for-sale	353,438	8,003	345,435	-	353,438
Bank stocks, at cost	4,497	n/a	n/a	n/a	n/a
Loans, net	419,923	-	-	420,061	420,061
Derivative financial instruments	797	-	797	-	797
Accrued interest receivable	4,002	22	2,117	1,863	4,002
Financial liabilities:					
Non-maturity deposits	$(570,784)	$(570,784)	$-	$-	$(570,784)
Time deposits	(143,943)	-	(142,924)	-	(142,924)
FHLB borrowings	(37,600)	-	(38,215)	-	(38,215)
Subordinated debentures	(2,184)	-	(19,051)	-	(19,051)
Other borrowings	(11,974)	-	(11,974)	-	(11,974)
Accrued interest payable	(287)	-	(287)	-	(287)

Methods and Assumptions Utilized

The carrying amount of cash and cash equivalents is considered to approximate fair value.

The Company's investment securities classified as available-for-sale include U.S. treasury securities, U.S. federal agency securities, municipal obligations, agency mortgage-backed securities, certificates of deposits and common stocks. Quoted exchange prices are available for the Company's U.S treasury securities and common stock investments, which are classified as Level 1. U.S. federal agency securities and agency mortgage-backed obligations are priced utilizing industry-standard models that consider various assumptions, including time value, yield curves, volatility factors, prepayment speeds, default rates, loss severity, current market and contractual prices for the underlying financial instruments, as well as other relevant economic measures. Substantially all of these assumptions are observable in the marketplace, can be derived from observable data, or are supported by observable levels at which transactions are executed in the marketplace. These measurements are classified as Level 2. Municipal securities are valued using a type of matrix, or grid, pricing in which securities are benchmarked against U.S. treasury rates based on credit rating. These model and matrix measurements are classified as Level 2 in the fair value hierarchy.

It is not practical to determine the fair value of bank stocks due to restrictions placed on the transferability of FHLB and FRB stock.

The estimated fair value of the Company's loan portfolio is based on the segregation of loans by collateral type, interest terms, and maturities. The fair value is estimated based on discounting scheduled and estimated cash flows through maturity using an appropriate risk-adjusted yield curve to approximate current interest rates for each category. No adjustment was made to the interest rates for changes in credit risk of performing loans where there are no known credit concerns. Management segregates loans in appropriate risk categories. Management believes that the risk factor embedded in the interest rates along with the allowance for loan losses applicable to the performing loan portfolio results in a fair valuation of such loans. The fair values of impaired loans are generally based on market prices for similar assets determined through independent appraisals or discounted values of independent appraisals and brokers' opinions of value. This method of estimating fair value does not incorporate the exit-price concept of fair value prescribed by ASC Topic 820 and is classified as Level 3.

Mortgage loans originated and intended for sale in the secondary market are carried at the lower of cost or estimated fair value, determined on an aggregate basis. The mortgage loan valuations are based on quoted secondary market prices for similar loans and are classified as Level 2.

The carrying amounts of accrued interest receivable and payable are considered to approximate fair value.

The estimated fair value of deposits with no stated maturity, such as non-interest-bearing demand deposits, savings, money market accounts, and checking accounts, is equal to the amount payable on demand. The fair value of interest-bearing time deposits is based on the discounted value of contractual cash flows of such deposits. The discount rate is tied to the FHLB yield curve plus an appropriate servicing spread. Fair value measurements based on discounted cash flows are classified as Level 2. These fair values do not incorporate the value of core deposit intangibles which may be associated with the deposit base.

The fair value of advances from the FHLB, subordinated debentures, and other borrowings is estimated using current yield curves for similar borrowings adjusted for the Company's current credit spread and classified as Level 2.

The Company's derivative financial instruments consist of interest rate lock commitments and corresponding forward sales contracts on mortgage loans held for sale. The fair values of these derivatives are based on quoted prices for similar loans in the secondary market. The market prices are adjusted by a factor, based on the Company's historical data and management's judgment about future economic trends, which considers the likelihood that a commitment will ultimately result in a closed loan. These instruments are classified as Level 2. The amounts are included in other assets

or other liabilities on the consolidated balance sheets and gains on sale of loans, net in the consolidated statements of earnings.

Off-Balance-Sheet Financial Instruments

The fair value of letters of credit and commitments to extend credit is based on the fees currently charged to enter into similar agreements. The aggregate of these fees is not material.

Transfers

The Company did not transfer any assets or liabilities among levels during the six months ended June 30, 2016 or during the year ended December 31, 2015.

Valuation Methods for Instruments Measured at Fair Value on a Recurring Basis

The following table represents the Company's financial instruments that are measured at fair value on a recurring basis at June 30, 2016 and December 31, 2015, allocated to the appropriate fair value hierarchy:

(Dollars in thousands)		As of June 30, 2016		
		Fair value hierarchy		
	Total	Level 1	Level 2	Level 3
Assets:				
Available-for-sale investment securities				
U. S. treasury securities	$6,049	$6,049	$-	$ -
U. S. federal agency obligations	27,985	-	27,985	-
Municipal obligations, tax exempt	155,735	-	155,735	-
Municipal obligations, taxable	74,266	-	74,266	-
Agency mortgage-backed securities	91,501	-	91,501	-
Common stocks	1,314	1,314	-	-
Certificates of deposit	9,700	-	9,700	-
Derivative financial instruments	$615	$-	$615	$ -

(Dollars in thousands)		As of December 31, 2015		
		Fair value hierarchy		
	Total	Level 1	Level 2	Level 3
Assets:				
Available-for-sale investment securities				
U. S. treasury securities	$6,517	$ 6,517	$ -	$ -
U. S. federal agency obligations	29,920	-	29,920	-
Municipal obligations, tax exempt	137,941	-	137,941	-
Municipal obligations, taxable	81,890	-	81,890	-
Agency mortgage-backed securities	85,985	-	85,985	-
Common stocks	1,486	1,486	-	-
Certificates of deposit	9,699	-	9,699	-
Derivative financial instruments	797	-	797	-

Changes in the fair value of available-for-sale securities are included in other comprehensive income to the extent the changes are not considered other-than-temporary impairments. Other-than-temporary impairment tests are performed on a quarterly basis and any decline in the fair value of an individual security below its cost that is deemed to be other-than-temporary results in a write-down of that security's cost basis.

Valuation Methods for Instruments Measured at Fair Value on a Non-recurring Basis

The Company does not value its loan portfolio at fair value. Collateral-dependent impaired loans are generally carried at the lower of cost or fair value of the collateral, less estimated selling costs. Collateral values are determined based on appraisals performed by qualified licensed appraisers hired by the Company and then further adjusted if warranted based on relevant facts and circumstances. The appraisals may utilize a single valuation approach or a combination of approaches including the comparable sales and income approach. Adjustments are routinely made in the appraisal process by the appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are typically significant and result in a Level 3 classification of the inputs for determining fair value. Impaired loans are reviewed and evaluated at least quarterly for additional impairment and adjusted accordingly, based on the same factors identified above. The carrying value of the Company’s impaired loans was $7.1 million and $6.8 million, with an allocated allowance of $245,000 and $88,000, at June 30, 2016 and December 31, 2015, respectively.

The following table represents the Company’s financial instruments that are measured at fair value on a non-recurring basis as of June 30, 2016 and December 31, 2015 allocated to the appropriate fair value hierarchy:

(Dollars in thousands)

		As of June 30, 2016 Fair value hierarchy			Total gains/
	Total	Level 1	Level 2	Level 3	(losses)
Assets:					
Impaired loans:					
One-to-four family residential real estate	$585	$ -	$ -	$ 585	$ 3
Commercial loans	39	-	-	39	(13)
Agriculture loans	448	-	-	448	(206)
Consumer loans	9	-	-	9	2

		As of December 31, 2015 Fair value hierarchy			Total (losses)/
	Total	Level 1	Level 2	Level 3	gains
Assets:					
Impaired loans:					
One-to-four family residential real estate	$266	$ -	$ -	$ 266	$ (137)
Consumer loans	16	-	-	16	6
Loans held for sale	14,465	-	14,465	-	(10)

The following table presents quantitative information about Level 3 fair value measurements for impaired loans measured at fair value on a non-recurring basis as of June 30, 2016 and December 31, 2015.

(Dollars in thousands)

	Fair value	Valuation technique	Unobservable inputs	Ran
As of June 30, 2016				
Impaired loans:				
One-to-four family residential real estate	$ 585	Sales comparison	Adjustment to appraised value	6%
Commercial loans	39	Sales comparison	Adjustment to appraised value	15
Agriculture loans	448	Sales comparison	Adjustment to appraised value	20
Consumer loans	9	Sales comparison	Adjustment to appraised value	0
As of December 31, 2015				
Impaired loans:	Hotels [1]			
Occupancy	**83 %**	91 %		**80 %**
Available Room Nights (in thousands)	**2,193**	2,143		**220**

Per Room Guest Spending	**$ 223**	$	214	**$**	**301**

(1) Per room guest spending consists of the average daily hotel room rate as well as guest spending on food, beverage and merchandise at the hotels. Hotel statistics include rentals of Disney Vacation Club units.

Increased revenues at our international operations reflected the sale of a real estate property and higher guest spending, hotel occupancy and attendance at Disneyland Paris along with increased attendance, guest spending and hotel occupancy at Hong Kong Disneyland Resort. These increases were partially offset by a decrease at Disneyland Paris reflecting the unfavorable impact of foreign currency translation as a result of the strengthening of the U.S. dollar against the Euro.

At our domestic operations, decreased revenues reflected lower attendance and hotel occupancy at our parks and resorts and fewer passenger cruise days at Disney Cruise Line, partially offset by higher guest spending at our parks and resorts. Decreased attendance in part reflected an unfavorable impact due to a shift in the timing of the Easter holiday period relative to our fiscal periods. Higher guest spending was primarily due to higher average ticket prices.

Costs and Expenses

Costs and expenses, which consist primarily of labor, depreciation, costs of merchandise, food and beverage sold, marketing and sales expense, repairs and maintenance and entertainment, increased 6%, or $124 million, to $2.4 billion. Higher costs were driven by increases at the domestic parks and resorts and Disney Cruise Line. The increase at our domestic parks and resorts reflected labor cost inflation, higher pension and post-retirement medical expenses and costs for new guest offerings, including *World of Color* at Disneyland Resort, partially offset by lower volume-related costs. The increase at Disney Cruise Line was due to increased operating costs to support the fleet expansion and higher fuel costs. Costs and expenses at Disneyland Paris were flat as costs associated with the sale of a real estate property were essentially offset by the favorable impact of foreign currency translation as a result of the strengthening of the U.S. dollar against the Euro.

Segment Operating Income

Segment operating income decreased 8% to $477 million primarily due to decreases at the domestic parks and Disney Cruise Line, partially offset by improvements at the international operations.

MANAGEMENT S DISCUSSION AND ANALYSIS OF

FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)

Restructuring and impairment charges

The Company recorded charges totaling $2 million in the prior-year quarter for severance and related costs which were reported in Restructuring and impairment charges in the Consolidated Statements of Income.

Studio Entertainment

Revenues

Revenues for the quarter increased 30%, or $378 million, to $1.6 billion primarily due to increases of $362 million in worldwide theatrical distribution, including our participation in *Iron Man 2*, and $47 million in worldwide television distribution.

The revenue growth in worldwide theatrical distribution was primarily due to the strong performance of *Toy Story 3, Alice in Wonderland* and *Iron Man 2*. The prior-year quarter included *Up, Hannah Montana: The Movie* and *The Proposal*. The increase in worldwide television distribution was driven by the timing of titles available in international markets.

Costs and Expenses

Costs and expenses, which consist primarily of production cost amortization, distribution and marketing expenses, product costs and participation costs, increased 19%, or $243 million, primarily due to an increase in worldwide theatrical distribution and higher film cost write-downs, partially offset by a decrease in domestic home entertainment.

The increase in worldwide theatrical distribution was primarily due to higher production cost amortization, driven by *Prince of Persia: The Sands of Time* and *Iron Man 2,* and higher participation costs driven by *Alice in Wonderland*.

Lower costs and expenses in domestic home entertainment were primarily due to a lower production cost amortization rate and lower distribution and marketing expense resulting from cost reduction initiatives. Key releases included *Alice in Wonderland* in the current quarter versus *Bedtime Stories*, *Bolt* and *Confessions of a Shopaholic* in the prior-year quarter.

Segment Operating Income

Segment operating income increased $135 million to $123 million due to the strong worldwide theatrical performance of *Toy Story 3*, *Alice in Wonderland* and *Iron Man 2* and increases at domestic home entertainment and worldwide television distribution, partially offset by higher film cost write-downs.

Restructuring and impairment charges

The Company recorded charges totaling $5 million in the current quarter for severance and related costs which were reported in Restructuring and impairment charges in the Consolidated Statements of Income.

Consumer Products

Revenues

Revenues for the quarter increased 19%, or $96 million, to $606 million, driven by increases of $43 million at Publishing, $32 million at Retail, and $18 million at Merchandise Licensing.

MANAGEMENT S DISCUSSION AND ANALYSIS OF

FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)

The increase at Publishing was driven by the acquisition of Marvel and the success of *The Red Pyramid* and *Percy Jackson* titles. Higher revenues at Retail were due to the acquisition of The Disney Store Japan (see discussion of The Disney Store Japan acquisition below). Merchandise Licensing revenue growth was driven by the strong performance of *Toy Story* and sales of Marvel merchandise, partially offset by a higher revenue share with the Studio Entertainment segment. The increase in revenue share with the Studio Entertainment segment in the current quarter was primarily due to growth from *Toy Story* merchandise.

Costs and Expenses

Costs and expenses, which consist primarily of cost of sales, salaries and benefits, marketing, and occupancy, increased 18%, or $75 million, primarily due to increases at Publishing, Retail, and Merchandise Licensing. The increase at Publishing was primarily due to cost of sales associated with Marvel products. At Retail, higher operating costs were due to the acquisition of The Disney Store Japan, partially offset by decreased cost of sales at The Disney Store North America reflecting global procurement efficiencies. The increase at Merchandise Licensing was primarily due to operating costs and intangible asset amortization associated with Marvel.

Operating Income

Segment operating income increased 22%, or $21 million, to $117 million, primarily due to improvement at Retail driven by The Disney Store North America and growth at Publishing.

Restructuring and impairment charges

The Company recorded charges totaling $1 million in the prior-year quarter for severance and related costs which were reported in Restructuring and impairment charges in the Consolidated Statements of Income.

The Disney Store Japan Acquisition

On March 31, 2010, the Company acquired all of the outstanding shares of Retail Networks Company Limited (The Disney Store Japan) in exchange for a $17 million note. At the time of the acquisition, The Disney Store Japan had a cash balance of $13 million. In connection with the acquisition in the second quarter of the current year, the Company recognized a $22 million non-cash gain from the deemed termination of the existing licensing arrangement. The gain is reported in Other income in the fiscal 2010 Condensed Consolidated Statement of Income.

Interactive Media

Revenues

Interactive Media revenues for the quarter increased 74%, or $84 million, to $197 million primarily due to increases of $64 million at Disney Interactive Studios and $10 million at Disney Online driven by increased Club Penguin subscription revenues.

At Disney Interactive Studios, the revenue growth was primarily due to higher sales of self-published video games in the current quarter. Significant current quarter releases included *Toy Story 3* and *Split Second* while the prior-year quarter included *Hannah Montana.*

Costs and Expenses

Costs and expenses, which consist primarily of video game and internet product development costs, cost of sales, distribution and marketing expenses, general and administrative costs, and technology infrastructure costs, increased 39%, or $74 million, to $262 million driven by increases at Disney Interactive Studios and Disney Online.

MANAGEMENT S DISCUSSION AND ANALYSIS OF

FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)

The increase at Disney Interactive Studios was primarily due to higher sales and marketing expenses driven by more new releases in the current quarter primarily *Toy Story 3* and *Split Second*, higher cost of sales driven by increased unit sales, and higher product development costs. These increases were partially offset by lower per unit video game cost of sales for catalog titles that had previously been written down to net realizable value. Higher costs and expenses at Disney Online were primarily due to increased cost of sales at Club Penguin and higher product development costs.

Operating Loss

Segment operating loss decreased 13% to $65 million due to an improvement at Disney Interactive Studios.

BUSINESS SEGMENT RESULTS Nine Month Results

Media Networks

Revenues

Media Networks revenues increased 11%, or $1.3 billion, to $12.7 billion, consisting of a 16% increase, or $1.1 billion, at the Cable Networks and a 3% increase, or $137 million, at Broadcasting.

Increased Cable Networks revenues were primarily due to growth of $915 million from Affiliate Fees and $260 million from advertising revenues. The increase in Affiliate Fees was primarily due to increases at ESPN resulting from earlier recognition of previously deferred revenues related to annual programming commitments, higher contractual rates and subscriber growth, including growth from the launch of a new network in the United Kingdom and, to a lesser extent, at the worldwide Disney Channels due to rate increases domestically and subscriber growth internationally. During the nine months, ESPN deferred a net $166 million of revenue compared to a net $532 million in the prior-year period. Higher advertising revenue was due to an increase at ESPN driven by higher sold inventory.

Increased Broadcasting revenues were primarily due to higher revenues from ABC Studios productions driven by increased international sales led by *Castle*, *Lost* and *Ghost Whisperer*, higher third party network license fees for *Criminal Minds* and increased advertising revenue. Higher advertising revenue reflected an increase at the owned television stations and higher sports advertising revenues due to the college Bowl Championship Series (BCS) national championship game, which was not broadcast by ABC in the prior year, partially offset by lower primetime advertising revenues at the ABC Television Network. The decrease in primetime advertising revenue was driven by lower ratings, partially offset by higher rates.

Costs and Expenses

Costs and expenses increased 7%, or $573 million, to $9.2 billion, consisting of a 9% increase, or $443 million, at the Cable Networks and a 3% increase, or $131 million, at Broadcasting. The increase at Cable Networks was driven by higher rights and production costs at ESPN due to programming costs for the new network in the United Kingdom, increased contractual costs for college basketball, college football and NFL programming, and soccer programming rights for the World Cup. The increase at Broadcasting reflected higher production cost amortization driven by increased sales of ABC Studios productions and an increase in programming costs at the ABC Television Network, including costs for the BCS national championship game. These increases were partially offset by the absence of a bad debt charge which was recorded in the prior year in connection with the bankruptcy of a syndication customer.

MANAGEMENT S DISCUSSION AND ANALYSIS OF

FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)

Segment Operating Income

Segment operating income increased 19% to $3.9 billion due to increases of $627 million at Cable Networks and $8 million at Broadcasting. The increase at the Cable Networks was primarily due to an increase at ESPN. The increase at Broadcasting was primarily due the absence of a bad debt charge which was recorded in the prior year in connection with the bankruptcy of a syndication customer and higher advertising revenue at the owned television stations, partially offset by decreased primetime advertising revenue at the ABC Television Network.

Restructuring and impairment charges

The Company recorded charges totaling $78 million and $226 million for the current and prior year nine-month periods, respectively. The charges in the current nine-month period were for severance and related costs and the closure of five ESPN Zone locations, while the charges in the prior-year nine-month period were primarily due to $108 million of radio FCC license impairments and $46 million of impairment related to our investment in UTV Group. These charges were reported in Restructuring and impairment charges in the Consolidated Statements of Income.

Parks and Resorts

Revenues

Parks and Resorts revenues increased 2%, or $119 million, to $7.9 billion due to an increase at our international operations. Revenues at our domestic operations were essentially flat.

The following table presents attendance, per capita theme park guest spending, and hotel statistics for our domestic properties:

	East Coast Nine months Ended		West Coast Nine months Ended		Total Domestic Nine months Ended	
	July 3, 2010	June 27, 2009	**July 3, 2010**	June 27, 2009	**July 3, 2010**	June 27, 2009
Parks						
(Increase/decrease)						
Attendance	**(1) %**	(2) %	**4 %**	2 %	**1 %**	(1) %
Per Capita Guest Spending	**1 %**	(3) %	**3 %**	(7) %	**2 %**	(4) %
Hotels [(1)]						
Occupancy	**82 %**	89 %	**75 %**	79%	**81 %**	88 %
Available Room Nights (in thousands)	**6,555**	6,390	**659**	599	**7,214**	6,989
Per Room Guest Spending	**$ 222**	$ 211	**$ 302**	$ 320	**$ 229**	$ 219

(1) Per room guest spending consists of the average daily hotel room rate as well as guest spending on food, beverage and merchandise at the hotels. Hotel statistics include rentals of Disney Vacation Club units.

Increased revenues at our international operations reflected the sale of a real estate property, the favorable impact of foreign currency translation as a result of the weakening of the U.S. dollar against the Euro and increased guest spending at Disneyland Paris along with increased guest spending and attendance at Hong Kong Disneyland Resort. These increases were partially offset by decreased attendance and occupied room nights at Disneyland Paris. Increased guest spending at Disneyland Paris and Hong Kong Disneyland Resort was driven by higher average ticket prices.

At our domestic operations, increased revenues from higher guest spending and attendance at our parks and resorts were largely offset by decreased occupied room nights at our resorts, and higher promotional activities and fewer passenger cruise days at Disney Cruise Line. Higher guest spending was primarily due to higher average ticket prices and daily hotel room rates, partially offset by lower merchandise spending.

MANAGEMENT S DISCUSSION AND ANALYSIS OF

FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)

Costs and Expenses

Costs and expenses increased 3%, or $191 million, to $6.9 billion. Higher costs were driven by increases at the domestic parks and resorts, Disneyland Paris and Disney Cruise Line. The increase at our domestic parks and resorts reflected higher pension and post-retirement medical expenses, labor cost inflation, and costs for new guest offerings, including *World of Color* at Disneyland Resort. These increases were partially offset by savings from cost mitigation activities and lower volume-related expenses. The increase at Disney Cruise Line was due to higher marketing costs to support the fleet expansion. The increase at Disneyland Paris reflected the unfavorable impact of foreign currency translation as a result of the weakening of the U.S. dollar against the Euro and costs associated with the sale of a real estate property. The increase at Disney Cruise Line was due to higher operating costs to support the fleet expansion.

Segment Operating Income

Segment operating income decreased 7% to $1.0 billion driven by decreases at the domestic parks and Disney Cruise Line, partially offset by improved results at the international operations.

Restructuring and impairment charges

The Company recorded charges totaling $54 million in the prior-year nine-month period for severance and related costs which were reported in Restructuring and impairment charges in the Consolidated Statements of Income.

Studio Entertainment

Revenues

Revenues increased 10%, or $469 million, to $5.1 billion driven by an increase of $651 million in worldwide theatrical distribution, including our participation in *Iron Man 2*, partially offset by a decrease of $163 million in worldwide home entertainment.

The revenue growth in worldwide theatrical distribution was primarily due to the strong performance of current period titles. Significant current period titles included *Alice in Wonderland* and *Iron Man 2* in domestic and international markets and *Toy Story 3* domestically while the prior-year period included *Up* domestically.

The decrease in worldwide home entertainment was primarily due to lower net effective sales prices and decreased television series DVD unit sales internationally and a decline in unit sales of new releases domestically. Key current period titles included *Up, Snow White* Diamond Release and *Tinker Bell And The Lost Treasure* while the prior-year period included *WALL-E, The Chronicles of Narnia: Prince Caspian* and *High School Musical 3: Senior Year.*

Costs and Expenses

Costs and expenses were essentially flat at $4.5 billion as a decrease in worldwide home entertainment was offset by an increase in worldwide theatrical distribution and higher film cost write-downs.

Lower costs and expenses in worldwide home entertainment were primarily due to decreased distribution and marketing expenses resulting from cost reduction initiatives and lower unit sales. The increase in worldwide theatrical distribution was primarily due to higher production cost amortization driven by stronger performing titles including *Alice in Wonderland* and *Iron Man 2,* and higher participation costs driven by *Alice in Wonderland* in the current period.

MANAGEMENT S DISCUSSION AND ANALYSIS OF

FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)

Segment Operating Income

Segment operating income increased $401 million to $589 million due to higher results in worldwide theatrical distribution and domestic home entertainment.

Restructuring and impairment charges

The Company recorded charges totaling $127 million for the current nine months and $2 million in the prior year nine-month period. The current-year nine month charges were primarily related to the write-off of capitalized costs related to abandoned film projects, the closure of a production facility and, severance and related costs which are reported in Restructuring and impairment charges in the Consolidated Statements of Income.

Consumer Products

Revenues

Revenues for the nine months increased 9%, or $169 million, to $1.9 billion, primarily due to increases of $79 million at Publishing, $66 million at Retail, and $12 million at Merchandise Licensing.

The increase at Publishing was driven by the acquisition of Marvel and sales of *Percy Jackson* titles. Higher revenues at Retail were driven by the acquisition of the Disney Store Japan and higher comparable store sales at the Disney Store North America. Merchandise Licensing revenue growth was driven by the strong performance of *Toy Story* merchandise and revenues from Marvel properties, partially offset by a higher revenue share with the Studio Entertainment segment and lower performance of *High School Musical* and *Hannah Montana* merchandise.

Costs and Expenses

Costs and expenses increased 10%, or $134 million primarily due to higher cost of sales at Publishing driven by Marvel and an increase at Retail due to the acquisition of the Disney Store Japan and unfavorable foreign currency impacts in Europe.

Segment Operating Income

Segment operating income increased 8%, or $35 million, to $493 million, primarily due to increases at Retail and Publishing.

Restructuring and impairment charges

The Company recorded charges totaling $2 million in the current nine months and $9 million in the prior-year nine-month period for severance and related costs which were reported in Restructuring and impairment charges in the Consolidated Statements of Income.

Interactive Media

Revenues

Interactive Media revenues for the nine months increased 3%, or $18 million, to $573 million reflecting an increase of $41 million at Disney Online, partially offset by a decrease of $34 million at Disney Interactive Studios.

The increase at Disney Online was driven by higher Club Penguin subscription revenues and increased advertising sales. At Disney Interactive Studios, the decrease was primarily due to a sales mix shift from new video game releases to catalog titles which have a lower sales price. Significant releases for the current nine months included *Toy Story 3*, *Split Second* and *Sing It 2*, while the prior year included *High School Musical 3*, *Sing It*, *Bolt* and *Club Penguin*.

MANAGEMENT S DISCUSSION AND ANALYSIS OF

FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)

Costs and Expenses

Costs and expenses decreased 5%, or $36 million, to $703 million driven by a decrease at Disney Interactive Studios, partially offset by an increase at Disney Online driven by higher product development costs.

The decrease at Disney Interactive Studios was primarily due to lower cost of sales driven by a higher sales mix of lower cost catalog titles and an overall decrease in sales volume. Additionally, certain prior year titles had higher per unit costs due to bundled accessories.

Operating Loss

Segment operating loss decreased 28% to $130 million due to an improvement at Disney Interactive Studios.

Restructuring and impairment charges

The Company recorded charges totaling $29 million in the prior-year nine-month period primarily for goodwill impairment which was reported in Restructuring and impairment charges in the Consolidated Statements of Income.

OTHER FINANCIAL INFORMATION

Corporate and Unallocated Shared Expenses

Corporate and unallocated shared expenses are as follows:

	Quarter Ended		% Change	**Nine months Ended**		% Change
(in millions)	**July 3, 2010**	June 27, 2009	Better/ (Worse)	**July 3, 2010**	June 27, 2009	Better/ (Worse)
Corporate and unallocated shared expenses	**$ 119**	$ 96	(24) %	**$ 282**	$ 268	(5) %

The increase in corporate and unallocated shared expenses for the quarter was driven by higher compensation related costs.

Net Interest Expense

Net interest expense is as follows:

	Quarter Ended		% Change	**Nine months Ended**		% Change
(in millions)	**July 3, 2010**	June 27, 2009	Better/ (Worse)	**July 3, 2010**	June 27, 2009	Better/ (Worse)
Interest expense	**$ (103)**	$ (134)	23 %	**$ (368)**	$ (452)	19 %
Interest and investment income	**14**	59	(76) %	**46**	110	(58) %
Net interest expense	**$ (89)**	$ (75)	(19) %	**$ (322)**	$ (342)	6 %

The decrease in interest expense for the quarter was primarily due to lower average debt balances. For the nine months, the decrease in interest expense reflected lower average debt balances and lower effective interest rates, partially offset by expense related to the early redemption of a film financing borrowing.

MANAGEMENT S DISCUSSION AND ANALYSIS OF

FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)

The decrease in interest and investment income for the quarter and nine months was primarily due to a gain on the sale of an investment in the prior-year third quarter. The nine months also decreased due to lower effective interest rates.

Income Taxes

The effective income tax rate is as follows:

	Quarter Ended		Change	**Nine months Ended**		Change
	July 3, 2010	June 27, 2009	Better/ (Worse)	**July 3, 2010**	June 27, 2009	Better/ (Worse)
Effective Income Tax Rate	**35.6 %**	37.8 %	2.2 ppt	**35.5 %**	36.6 %	1.1 ppt

The decrease in the effective income tax rate for the current-year quarter was driven by favorable adjustments related to certain prior-year income tax matters.

For the nine months, the decrease in the effective income tax rate was primarily due to favorable adjustments related to certain prior-year income tax matters, partially offset by a $72 million charge related to the health care reform legislation enacted in March 2010. Under this legislation the Company s deductions for retiree prescription drug benefits will be reduced by the amount of Medicare Part D drug subsidies received beginning in fiscal year 2014. Under applicable accounting rules, the Company is required to reduce in the period of enactment its existing deferred tax asset, which was established for the future deductibility of retiree prescription drug benefit costs, to reflect the lost deductions.

Noncontrolling Interests

Net income attributable to noncontrolling interests is as follows:

(in millions)	**Quarter Ended**		% Change	**Nine months Ended**		% Change
	July 3, 2010	June 27, 2009	Better/ (Worse)	**July 3, 2010**	June 27, 2009	Better/ (Worse)
Net income attributable to noncontrolling interests	**$ 174**	$ 77	(>100) %	**$ 219**	$ 123	(78) %

The increase in net income attributable to noncontrolling interests for both the quarter and nine months was primarily due to higher operating results at ESPN. The net income attributable to noncontrolling interests is determined based on income after royalties, financing costs and income taxes.

MANAGEMENT S DISCUSSION AND ANALYSIS OF

FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)

FINANCIAL CONDITION

The change in cash and cash equivalents is as follows:

	Nine months Ended		
(in millions)	**July 3, 2010**	June 27, 2009	Change Better/(Worse)
Cash provided by operations	**$ 4,372**	$ 3,581	$ 791
Cash used in investing activities	**(3,463)**	(1,110)	(2,353)
Cash used in financing activities	**(1,375)**	(2,344)	969
(Decrease)/increase in cash and cash equivalents	**$ (466)**	$ 127	$ (593)

Operating Activities

The increase in cash provided by operations was driven by higher segment operating results.

Film and Television Costs

The Company s Studio Entertainment and Media Networks segments incur costs to acquire and produce film and television programming. Film and television production costs include all internally produced content such as live action and animated feature films, animated direct-to-video programming, television series, television specials, theatrical stage plays or other similar product. Programming costs include film or television product licensed for a specific period from third parties for airing on the Company s broadcast and cable networks and television stations. Programming assets are generally recorded when the programming becomes available to us with a corresponding increase in programming liabilities. Accordingly, we analyze our programming assets net of the related liability.

The Company s film and television production and programming activity for the nine months ended July 3, 2010 and June 27, 2009 are as follows:

	Nine months Ended	
(in millions)	**July 3, 2010**	June 27, 2009
Beginning balances:		
Production and programming assets	**$ 5,756**	$ 5,935
Programming liabilities	**(1,040)**	(1,108)
	4,716	4,827
Spending:		
Film and television production	**2,518**	2,562
Broadcast programming	**3,375**	2,905
	5,893	5,467
Amortization:		
Film and television production	**(2,710)**	(2,414)

Broadcast programming	**(3,214)**	(2,773)
	(5,924)	(5,187)
Change in film and television production and programming costs	**(31)**	280
Other non-cash activity	**108**	(129)
Ending balances:		
Production and programming assets	**5,556**	5,872
Programming liabilities	**(763)**	(894)
	$ 4,793	$ 4,978

MANAGEMENT S DISCUSSION AND ANALYSIS OF

FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)

Investing Activities

Cash used by investing activities during the nine months ended July 3, 2010 of $3.5 billion included $2.3 billion for the cash portion of the Marvel Entertainment, Inc. acquisition (see Note 3 to the Condensed Consolidated Financial Statements for further details) and $1.3 billion of investments in parks, resorts and other property, partially offset by proceeds totaling $170 million from the sales of investments in pay television services in Europe and the sale of the rights and assets related to the Power Rangers property.

During the nine months ended July 3, 2010 and June 27, 2009, investments in parks, resorts and other properties were as follows:

	Nine months Ended	
(in millions)	**July 3, 2010**	June 27, 2009
Media Networks		
Cable Networks	**$ 60**	$ 98
Broadcasting	**52**	87
Total Media Networks	**112**	185
Parks and Resorts		
Domestic	**851**	674
International	**148**	75
Total Parks and Resorts	**999**	749
Studio Entertainment	**65**	110
Consumer Products	**41**	22
Interactive Media	**13**	15
Corporate	**83**	46
Total investment in parks, resorts and other property	**$ 1,313**	$ 1,127

The increase in capital expenditures for the nine months reflected higher construction progress payments on two new cruise ships, the expansion at Disney s California Adventure and Hong Kong Disneyland, and the construction of a Disney Vacation Club Resort in Hawaii, partially offset by the construction of broadcast and film production facilities in the prior-year nine month period.

Financing Activities

Cash used by financing activities during the nine months ended July 3, 2010 of $1.4 billion reflected repurchases of common stock and dividend payments, partially offset by proceeds from stock option exercises and net borrowings. The decrease in cash used in financing activities from the prior-year nine-month period was driven by higher proceeds from stock option exercises and net borrowings in the current nine months compared to a net reduction in borrowings and the purchase of additional interests in Jetix Europe N.V. (Jetix) in the prior-year period. These decreases were partially offset by higher repurchases of common stock.

MANAGEMENT S DISCUSSION AND ANALYSIS OF

FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)

During the nine months ended July 3, 2010, the Company s borrowing activity was as follows:

	October 3, 2009	Additions	Payments	Other Activity	**July 3, 2010**
Commercial paper borrowings	$	$ 794	$	$	**$ 794**
U.S. medium-term notes	7,618		(50)	3	**7,571**
European medium-term notes	347		(88)	5	**264**
Other foreign currency denominated debt	904			22	**926**
Film financing	350		(350)		
Other	614			15	**629**
Euro Disney borrowings[(1)]	2,344		(91)	(307)	**1,946**
Hong Kong Disneyland borrowings	524			(27)	**497**
Total	$ 12,701	$ 794	$ (579)	$ (289)	**$ 12,627**

[(1)] The other activity is primarily the impact of foreign currency translation as a result of the strengthening of the U.S. dollar against the Euro.
The Company s bank facilities as of July 3, 2010 were as follows:

(in millions)	Committed Capacity	Capacity Used	Unused Capacity
Bank facilities expiring February 2011	$ 2,225	$ 235	$ 1,990
Bank facilities expiring February 2013	2,250		2,250
Total	$ 4,475	$ 235	$ 4,240

These bank facilities allow for borrowings at LIBOR-based rates plus a spread, which depends on the Company s public debt rating and can range from 0.18% to 4.50%. As of July 3, 2010, the Company had not borrowed under these bank facilities. The Company also has the ability to issue up to $800 million of letters of credit under the facility expiring in February 2011, which if utilized, reduces available borrowings under this facility. As of July 3, 2010, $235 million of letters of credit had been issued under this facility.

The Company may use commercial paper borrowings up to the amount of its unused bank facilities, in conjunction with term debt issuance and operating cash flow, to retire or refinance other borrowings before or as they come due.

On December 2, 2009, the Company declared a $653 million dividend ($0.35 per share) related to fiscal 2009 for shareholders of record on December 14, 2009, which was paid on January 19, 2010. On December 3, 2008, the Company declared a $648 million dividend ($0.35 per share) related to fiscal 2008 for shareholders of record on December 15, 2008, which was paid on January 20, 2009.

During the nine months ended July 3, 2010, the Company repurchased 45 million shares of its common stock for approximately $1.5 billion. As of July 3, 2010, the Company had remaining authorization in place to repurchase approximately 134 million additional shares. The repurchase program does not have an expiration date.

We believe that the Company s financial condition is strong and that its cash balances, other liquid assets, operating cash flows, access to debt and equity capital markets and borrowing capacity, taken together, provide adequate resources to fund ongoing operating requirements and

future capital expenditures related to the expansion of existing businesses and development of new projects. However, the Company s operating cash flow and access to the capital markets can be impacted by

MANAGEMENT S DISCUSSION AND ANALYSIS OF

FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)

macroeconomic factors outside of its control. In addition to macroeconomic factors, the Company s borrowing costs can be impacted by short and long-term debt ratings assigned by independent rating agencies, which are based, in significant part, on the Company s performance as measured by certain credit metrics such as interest coverage and leverage ratios. As of July 3, 2010, Moody s Investors Service s long and short-term debt ratings for the Company were A2 and P-1, respectively, with stable outlook; Standard & Poor s long and short-term debt ratings for the Company were A and A-1, respectively, with negative outlook; and Fitch s long and short-term debt ratings for the Company were A and F-1, respectively, with stable outlook. The Company s bank facilities contain only one financial covenant, relating to interest coverage, which the Company met on July 3, 2010, by a significant margin. The Company s bank facilities also specifically exclude certain entities, such as Euro Disney and Hong Kong Disneyland, from any representations, covenants or events of default.

Euro Disney has annual covenants under its debt agreements that limit its investment and financing activities and require it to meet certain financial performance covenants. Euro Disney was in compliance with these covenants for fiscal 2009.

COMMITMENTS AND CONTINGENCIES

Legal Matters

As disclosed in Note 11 to the Condensed Consolidated Financial Statements, the Company has exposure for certain legal matters.

Guarantees

See Note 11 to the Condensed Consolidated Financial Statements for information regarding the Company s guarantees.

Tax Matters

As disclosed in Note 10 to the Consolidated Financial Statements in the 2009 Annual Report on Form 10-K as amended on Form 8-K dated February 18, 2010, the Company has exposure for certain tax matters.

Contractual Commitments

Refer to Note 15 in the Consolidated Financial Statements in the 2009 Annual Report on Form 10-K as amended on Form 8-K dated February 18, 2010 for information regarding the Company s contractual commitments.

OTHER MATTERS

Accounting Policies and Estimates

We believe that the application of the following accounting policies, which are important to our financial position and results of operations, require significant judgments and estimates on the part of management. For a summary of our significant accounting policies, including the accounting policies discussed below, see Note 2 to the Consolidated Financial Statements in the 2009 Annual Report on Form 10-K as amended on Form 8-K dated February 18, 2010.

Film and Television Revenues and Costs

We expense film and television production, participation and residual costs over the applicable product life cycle based upon the ratio of the current period s revenues to the estimated remaining total revenues (Ultimate Revenues) for each production. If our estimate of Ultimate Revenues decreases, amortization of film and television costs may be accelerated. Conversely, if estimates of Ultimate Revenues increase, film and television cost amortization may be slowed. For film productions, Ultimate Revenues include revenues from all sources that will be earned within ten years from the date

MANAGEMENT S DISCUSSION AND ANALYSIS OF

FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)

of the initial theatrical release. For television series, we include revenues that will be earned within ten years from delivery of the first episode, or if still in production, five years from delivery of the most recent episode, if later.

With respect to films intended for theatrical release, the most sensitive factor affecting our estimate of Ultimate Revenues (and therefore affecting future film cost amortization and/or impairment) is domestic theatrical performance. Revenues derived from other markets subsequent to the domestic theatrical release (e.g. the home video or international theatrical markets) have historically been highly correlated with domestic theatrical performance. Domestic theatrical performance varies primarily based upon the public interest and demand for a particular film, the popularity of competing films at the time of release and the level of marketing effort. Upon a film s release and determination of domestic theatrical performance, the Company s estimates of revenues from succeeding windows and markets are revised based on historical relationships and an analysis of current market trends. The most sensitive factor affecting our estimate of Ultimate Revenues for released films is the extent of home entertainment sales achieved. Home entertainment sales vary based on the number and quality of competing home video products as well as the manner in which retailers market and price our products.

With respect to television series or other television productions intended for broadcast, the most sensitive factor affecting estimates of Ultimate Revenues is the program s rating and the strength of the advertising market. Program ratings, which are an indication of market acceptance, directly affect the Company s ability to generate advertising revenues during the airing of the program. In addition, television series with greater market acceptance are more likely to generate incremental revenues through the eventual sale of the program rights in the syndication, international and home entertainment markets. Alternatively, poor ratings may result in a television series cancellation, which would require the immediate write-off of any unamortized production costs. A significant decline in the advertising market would also negatively impact our estimates.

We expense the cost of television broadcast rights for acquired movies, series and other programs based on the number of times the program is expected to be aired or on a straight-line basis over the useful life, as appropriate. Amortization of those television programming assets being amortized on a number of airings basis may be accelerated if we reduce the estimated future airings and slowed if we increase the estimated future airings. The number of future airings of a particular program is impacted primarily by the program s ratings in previous airings, expected advertising rates, and availability and quality of alternative programming. Accordingly, planned usage is reviewed periodically and revised if necessary. Rights costs for multi-year sports programming arrangements are amortized during the applicable seasons based on the estimated relative value of each year in the arrangement. The estimated values of each year are based on our projection of revenues over the contract period which include advertising revenue and an allocation of affiliate revenue. If the annual contractual payments related to each season approximate each season s relative value, we expense the related contractual payment during the applicable season. If planned usage patterns or estimated relative values by year were to change significantly, amortization of our sports rights costs may be accelerated or slowed.

Costs of film and television productions are subject to regular recoverability assessments which compare the estimated fair values with the unamortized costs. The net realizable value of the television broadcast program licenses and rights are reviewed using a daypart methodology. A daypart is defined as an aggregation of programs broadcast during a particular time of day or programs of a similar type. The Company s dayparts are: early morning, daytime, late night, primetime, news, children, and sports (includes network and cable). The net realizable values of other cable programming assets are reviewed on an aggregated basis for each cable channel. Individual programs are written-off when there are no plans to air or sublicense the program. Estimated values are based upon assumptions about future demand and market conditions. If actual demand or market conditions are less favorable than our projections, film, television and programming cost write-downs may be required.

MANAGEMENT S DISCUSSION AND ANALYSIS OF

FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)

Revenue Recognition

The Company has revenue recognition policies for its various operating segments that are appropriate to the circumstances of each business. See Note 2 to the Consolidated Financial Statements in the 2009 Annual Report on Form 10-K as amended on Form 8-K dated February 18, 2010 for a summary of these revenue recognition policies.

We reduce home entertainment and software product revenues for estimated future returns of merchandise and for customer programs and sales incentives. These estimates are based upon historical return experience, current economic trends and projections of customer demand for and acceptance of our products. If we underestimate the level of returns and concessions in a particular period, we may record less revenue in later periods when returns exceed the estimated amount. Conversely, if we overestimate the level of returns and concessions for a period, we may have additional revenue in later periods when returns and concessions are less than estimated.

Revenues from advance theme park ticket sales are recognized when the tickets are used. For non-expiring, multi-day tickets, we recognize revenue over a three-year time period based on estimated usage, which is derived from historical usage patterns. If actual usage is different than our estimated usage, revenues may not be recognized in the periods the related services are rendered. In addition, a change in usage patterns would impact the timing of revenue recognition.

Pension and Postretirement Medical Plan Actuarial Assumptions

The Company s pension and postretirement medical benefit obligations and related costs are calculated using a number of actuarial assumptions. Two critical assumptions, the discount rate and the expected return on plan assets, are important elements of expense and/or liability measurement which we evaluate annually. Refer to the 2009 Annual Report on Form 10-K as amended on Form 8-K dated February 18, 2010 for estimated impacts of changes in these assumptions. Other assumptions include the healthcare cost trend rate and employee demographic factors such as retirement patterns, mortality, turnover and rate of compensation increase.

The discount rate enables us to state expected future cash payments for benefits as a present value on the measurement date. A lower discount rate increases the present value of benefit obligations and increases pension expense. The guideline for setting this rate is high-quality long-term corporate bond rates that are currently available. The Company s discount rate is determined by considering the average of pension yield curves constructed of a large population of high quality corporate bonds. The resulting discount rate reflects the matching of plan liability cash flows to the yield curves.

To determine the expected long-term rate of return on the plan assets, we consider the current and expected asset allocation, as well as historical and expected returns on each plan asset class. A lower expected rate of return on pension plan assets will increase pension expense.

Goodwill, Intangible Assets, Long-Lived Assets and Investments

The Company is required to test goodwill and other indefinite-lived intangible assets for impairment on an annual basis and between annual tests if current events or circumstances require an interim impairment assessment. Goodwill is allocated to various reporting units, which are generally an operating segment or one reporting level below the operating segment. The Company compares the fair value of each reporting unit to its carrying amount to determine if there is potential goodwill impairment. If the fair value of a reporting unit is less than its carrying value, an impairment loss is recorded to the extent that the fair value of the goodwill within the reporting unit is less than the carrying value of its goodwill.

MANAGEMENT S DISCUSSION AND ANALYSIS OF

FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)

To determine the fair value of our reporting units, we generally use a present value technique (discounted cash flow) corroborated by market multiples when available and as appropriate. We apply what we believe to be the most appropriate valuation methodology for each of our reporting units. The discounted cash flow analyses are sensitive to our estimates of future revenue growth and margins for these businesses. We include in the projected cash flows an estimate of the revenue we believe the reporting unit would receive if the intellectual property developed by the reporting unit that is being used by other reporting units was licensed to an unrelated third party at its fair market value. These amounts are not necessarily the same as those included in segment operating results. We believe our estimates of fair value are consistent with how a marketplace participant would value our reporting units.

In times of adverse economic conditions in the global economy, the Company s long-term cash flow projections are subject to a greater degree of uncertainty than usual. If we had established different reporting units or utilized different valuation methodologies or assumptions, the impairment test results could differ, and we could be required to record impairment charges. Because of the way the accounting rules work, a relatively modest reduction in our estimate of the fair value of our Broadcasting reporting unit could result in a significant goodwill impairment charge.

The Company is required to compare the fair values of other indefinite-lived intangible assets to their carrying amounts. If the carrying amount of an indefinite-lived intangible asset exceeds its fair value, an impairment loss is recognized. Fair values of other indefinite-lived intangible assets are determined based on discounted cash flows or appraised values, as appropriate.

The Company has cost and equity investments. The fair value of these investments is dependent on the performance of the investee companies, as well as volatility inherent in the external markets for these investments. In assessing the potential impairment for these investments, we consider these factors, as well as the forecasted financial performance of our investees and market values, where available. If these forecasts are not met or market values indicate an other-than-temporary decline in value, impairment charges may be required.

Allowance for Doubtful Accounts

We evaluate our allowance for doubtful accounts and estimate collectibility of accounts receivable based on our analysis of historical bad debt experience in conjunction with our assessment of the financial condition of individual companies with which we do business. In times of domestic or global economic turmoil, our estimates and judgments with respect to the collectibility of our receivables are subject to greater uncertainty than in more stable periods. If our estimate of uncollectible accounts is too low, costs and expenses may increase in future periods, and if it is too high, cost and expenses may decrease in future periods.

MANAGEMENT S DISCUSSION AND ANALYSIS OF

FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)

Contingencies and Litigation

We are currently involved in certain legal proceedings and, as required, have accrued estimates of the probable and estimable losses for the resolution of these claims. These estimates have been developed in consultation with outside counsel and are based upon an analysis of potential results, assuming a combination of litigation and settlement strategies. It is possible, however, that future results of operations for any particular quarterly or annual period could be materially affected by changes in our assumptions or the effectiveness of our strategies related to these proceedings. See Note 11 to the Condensed Consolidated Financial Statements for information on litigation exposure.

Income Tax Audits

As a matter of course, the Company is regularly audited by federal, state and foreign tax authorities. From time to time, these audits result in proposed assessments. Our determinations regarding the recognition of income tax liabilities and benefits are made in consultation with outside tax and legal counsel where appropriate and are based upon the technical merits of our tax positions in consideration of applicable tax statutes and related interpretations and precedents and upon the expected outcome of proceedings (or negotiations) with taxing and legal authorities. The tax liabilities or benefits ultimately realized by the Company may differ from those recognized in our financial statements based on a number of factors, including the Company s decision to settle rather than litigate a matter, relevant legal precedents related to similar matters and the Company s success in supporting its filing positions with taxing authorities.

Stock Option Compensation Expense

Compensation expense for stock options is estimated on the date of grant using a binomial valuation model. The weighted average assumptions used in the binomial valuation model during the nine months ended July 3, 2010 were 32% for the expected volatility, 1.4 for the expected exercise multiple (the multiple of exercise price to grant price at which exercises are expected to occur on average) and 3% for the expected termination rate. Although the initial fair value of stock options is not adjusted after the grant date, changes in the Company s assumptions may change the estimated fair value of and therefore, the expense related to future stock option grants. The assumptions that cause the greatest variation in fair value in the binomial valuation model are the assumed volatility and expected exercise multiple. Increases or decreases in either the assumed volatility or expected exercise multiple will cause the binomial option value to increase or decrease, respectively.

The volatility assumption considers both historical and implied volatility and may be impacted by the Company s performance as well as changes in economic and market conditions. The expected exercise multiple may be influenced by the Company s future stock performance, stock price volatility and employee turnover rate. Refer to the 2009 Annual Report on Form 10-K as amended on Form 8-K dated February 18, 2010 for estimated impacts of changes in these assumptions.

New Accounting Pronouncements

See Note 12 to the Condensed Consolidated Financial Statements for information regarding new accounting pronouncements.

MARKET RISK

The Company is exposed to the impact of interest rate changes, foreign currency fluctuations, commodity fluctuations and changes in the market values of its investments.

Policies and Procedures

In the normal course of business, we employ established policies and procedures to manage the Company s exposure to changes in interest rates, foreign currencies, commodities, and the fair market value of certain investments in debt and equity securities using a variety of financial instruments.

MANAGEMENT S DISCUSSION AND ANALYSIS OF

FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)

Our objectives in managing exposure to interest rate changes are to limit the impact of interest rate volatility on earnings and cash flows and to lower overall borrowing costs. To achieve these objectives, we primarily use interest rate swaps to manage net exposure to interest rate changes related to the Company s portfolio of borrowings. By policy, the Company targets fixed-rate debt as a percentage of its net debt between minimum and maximum percentages.

Our objective in managing exposure to foreign currency fluctuations is to reduce volatility of earnings and cash flow in order to allow management to focus on core business issues and challenges. Accordingly, the Company enters into various contracts that change in value as foreign exchange rates change to protect the U.S. dollar equivalent value of its existing foreign currency assets, liabilities, commitments and forecasted foreign currency revenues. The Company utilizes option strategies and forward contracts that provide for the sale of foreign currencies to hedge probable, but not firmly committed, transactions. The Company also uses forward contracts to hedge foreign currency assets and liabilities. The principal foreign currencies hedged are the Euro, British pound, Japanese yen and Canadian dollar. Cross-currency swaps are used to effectively convert foreign currency denominated borrowings to U.S. dollar denominated borrowings. By policy, the Company maintains hedge coverage between minimum and maximum percentages of its forecasted foreign exchange exposures generally for periods not to exceed five years. The gains and losses on these contracts offset changes in the U.S. dollar equivalent value of the related exposures.

Our objectives in managing exposure to commodity fluctuations are to use commodity derivatives to reduce volatility of earnings and cash flows arising from commodity price changes. The amounts hedged using commodity swap contracts are based on forecasted levels of consumption of certain commodities, such as fuel oil and gasoline.

It is the Company s policy to enter into foreign currency and interest rate derivative transactions and other financial instruments only to the extent considered necessary to meet its objectives as stated above. The Company does not enter into these transactions or any other hedging transactions for speculative purposes.

Item 3. Quantitative and Qualitative Disclosures about Market Risk. See Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures We have established disclosure controls and procedures to ensure that the information required to be disclosed by the Company in the reports that it files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms and that such information is accumulated and made known to the officers who certify the Company s financial reports and to other members of senior management and the Board of Directors as appropriate to allow timely decisions regarding required disclosure.

Based on their evaluation as of July 3, 2010, the principal executive officer and principal financial officer of the Company have concluded that the Company s disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) are effective.

There have been no changes in our internal controls over financial reporting during the third quarter of fiscal 2010 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. Legal Proceedings

Since our Form 10-Q filing for the quarter ended April 3, 2010, developments identified below occurred in the following legal proceedings.

Milne and Disney Enterprises, Inc. v. Stephen Slesinger, Inc. On November 5, 2002, the granddaughter of the author of the Winnie the Pooh books and Disney Enterprises, Inc. (DEI), a Company subsidiary, filed an action against Stephen Slesinger, Inc. (SSI) in the United States District Court for the Central District of California seeking a declaratory judgment that a notice served upon SSI terminating a prior grant to it of certain Winnie the Pooh rights was proper and that a later grant of those rights to DEI was valid. SSI filed counterclaims seeking, among other relief, a declaration that the attempted termination and grant to DEI were unenforceable, and that DEI remained obligated to pay SSI royalties for certain exploitations of Winnie the Pooh under the terms of a 1983 agreement executed by SSI. SSI s counterclaims for declaratory relief were dismissed as moot by the court s decisions that the termination notice, as well as another termination notice served by the heir of the illustrator of the Winnie the Pooh books, were invalid. SSI filed amended answers and asserted additional counterclaims against the Company for breach of contract, fraud, unfair business practices, and copyright and trademark infringement. On May 19, 2009, the court granted the Company s motion for summary judgment on the breach of contract and fraud counterclaims, and on September 25, 2009, the court granted the Company s motion for summary judgment on SSI s remaining claims. SSI appealed to the United States Court of Appeals for the Ninth Circuit, but on June 28, 2010, voluntarily dismissed the appeal.

Celador International Ltd. v. The Walt Disney Company. On May 19, 2004, an affiliate of the creator and licensor of the television program, *Who Wants to be a Millionaire*, filed an action against the Company and certain of its subsidiaries, including American Broadcasting Companies, Inc. and Buena Vista Television, LLC, alleging it was damaged by defendants improperly engaging in certain intra-company transactions and charging merchandise distribution expenses, resulting in an underpayment to the plaintiff. On July 7, 2010, the jury returned a verdict for breach of contract against certain subsidiaries of the Company, awarding plaintiff damages of $269.4 million. The plaintiff has advised the Company that it intends to seek an award of prejudgment interest on the verdict amount. Although we cannot predict the ultimate outcome of this lawsuit, the Company believes the jury s verdict is in error and intends to vigorously pursue its position in post-trial motions and, if those motions are unsuccessful, on appeal.

The Company, together with, in some instances, certain of its directors and officers is a defendant or codefendant in various other legal actions involving copyright, breach of contract and various other claims incident to the conduct of its businesses. Management does not expect the Company to suffer material liability by reason of these actions.

ITEM 1A. Risk Factors

The Private Securities Litigation Reform Act of 1995 (the Act) provides a safe harbor for forward-looking statements made by or on behalf of the Company. We may from time to time make written or oral statements that are forward-looking, including statements contained in this report and other filings with the Securities and Exchange Commission and in reports to our shareholders. All forward-looking statements are made on the basis of management s views and assumptions regarding future events and business performance as of the time the statements are made and the Company does not undertake any obligation to update its disclosure relating to forward looking matters. Actual results may differ materially from those expressed or implied. Such differences may result from actions taken by the Company, including restructuring or strategic initiatives (including capital investments or asset acquisitions or dispositions), as well as from developments beyond the Company s control, including: changes in domestic and global economic conditions, competitive conditions and consumer preferences; adverse weather conditions or natural disasters; health concerns; international, political or military developments; and technological developments. Such developments may affect travel and leisure businesses generally and may, among other things, affect the performance of the Company s theatrical and home entertainment releases, the advertising market for broadcast and cable television programming, expenses of providing medical and pension benefits, demand for our products and performance of some or all company businesses either directly or through their impact on those who distribute our products. Additional factors are discussed in the 2009 Annual Report on Form 10-K under the Item 1A, Risk Factors.

Our results may be adversely affected if long-term programming or carriage contracts are not renewed on sufficiently favorable terms.

We enter into long-term contracts for both the acquisition and the distribution of media programming and products, including contracts for the acquisition of programming rights for sporting events and other programs, and contracts for the distribution of our programming to MVSPs. As these contracts expire, we must renew or renegotiate the contracts, and one such contract for the distribution of programming expires prior to the end of the current fiscal year. If we are unable to renew any such contract on acceptable terms, we may lose programming rights or distribution rights. Even if these contracts are renewed, the cost of obtaining programming rights may increase (or increase at faster rates than our historical experience) or the revenue from distribution of programs may be reduced (or increase at slower rates than our historical experience). With respect to the acquisition of programming rights, particularly sports programming rights, the impact of these long-term contracts on our results over the term of the contracts depends on a number of factors, including the strength of advertising markets, effectiveness of marketing efforts and the size of viewer audiences. There can be no assurance that revenues from programming based on these rights will exceed the cost of the rights plus the other costs of producing and distributing the programming.

PART II. OTHER INFORMATION (continued)

ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds

The following table provides information about Company purchases of equity securities that are registered by the Company pursuant to Section 12 of the Exchange Act during the quarter ended July 3, 2010**:**

Period	Total Number of Shares Purchased [1]	Weighted Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs[2]
April 4, 2010 May 3, 2010	2,233,076	$ 35.75	2,167,000	171 million
May 4, 2010 June 3, 2010	21,764,872	33.52	21,654,096	169 million
June 4, 2010 July 3, 2010	13,237,946	33.90	13,145,600	147 million
Total	37,235,894	33.79	36,966,696	134 million

[1] 269,198 shares were purchased on the open market to provide shares to participants in the Walt Disney Investment Plan (WDIP) and Employee Stock Purchase Plan (ESPP). These purchases were not made pursuant to a publicly announced repurchase plan or program.

[2] Under a share repurchase program implemented effective June 10, 1998, the Company is authorized to repurchase shares of its common stock. On May 1, 2007, following share repurchases made through May 1, 2007, the Company s Board of Directors increased the repurchase authorization to a total of 400 million shares as of that date. The repurchase program does not have an expiration date.

ITEM 6. Exhibits

See Index of Exhibits.

SIGNATURE

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.

THE WALT DISNEY COMPANY
(Registrant)

By: /s/ JAMES A. RASULO
James A. Rasulo,

Senior Executive Vice President and

Chief Financial Officer

August 10, 2010

Burbank, California

INDEX OF EXHIBITS

Number and Description of Exhibit (Numbers Coincide with Item 601 of Regulation S-K)		Document Incorporated by Reference from a Previous Filing or Filed Herewith, as Indicated below
10.1	Disney Savings and Investment Plan As Amended and Restated Effective January 1, 2010	Filed herewith
31(a)	Rule 13a-14(a) Certification of Chief Executive Officer of the Company in accordance with Section 302 of the Sarbanes-Oxley Act of 2002	Filed herewith
31(b)	Rule 13a-14(a) Certification of Chief Financial Officer of the Company in accordance with Section 302 of the Sarbanes-Oxley Act of 2002	Filed herewith
32(a)	Section 1350 Certification of Chief Executive Officer of the Company in accordance with Section 906 of the Sarbanes-Oxley Act of 2002*	Furnished
32(b)	Section 1350 Certification of Chief Financial Officer of the Company in accordance with Section 906 of the Sarbanes-Oxley Act of 2002*	Furnished
101	The following materials from the Company s Quarterly Report on Form 10-Q for the quarter ended July 3, 2010 formatted in Extensible Business Reporting Language (XBRL): (i) the Condensed Consolidated Statements of Income, (ii) the Condensed Consolidated Balance Sheets, (iii) the Condensed Consolidated Statements of Cash Flows, (iv) the Condensed Consolidated Statements of Equity and (v) related notes	Furnished

* A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.