

BankFinancial CORP  
Form 10-Q  
May 07, 2012  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
WASHINGTON, D.C. 20549

**FORM 10-Q**

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

For the Quarterly Period ended March 31, 2012

or

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

For transition period from to

Commission File Number 0-51331

**BANKFINANCIAL CORPORATION**

(Exact Name of Registrant as Specified in Charter)

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**Maryland**  
(State or Other Jurisdiction)

**75-3199276**  
(I.R.S. Employer

of Incorporation)

Identification No.)

**15W060 North Frontage Road, Burr Ridge, Illinois**  
(Address of Principal Executive Offices)

**60527**  
(Zip Code)

**Registrant's telephone number, including area code: (800) 894-6900**

**Not Applicable**

(Former name or former address, if changed since last report)

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

Indicate by check mark whether the registrant 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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No .

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer, or a smaller reporting company. See 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

Indicate the number of shares outstanding of each of the Issuer's classes of common stock as of the latest practicable date. 21,072,966 shares of Common Stock, par value \$0.01 per share, were issued and outstanding as of May 4, 2012

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**BANKFINANCIAL CORPORATION**

Form 10-Q Quarterly Report

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**Table of Contents****BANKFINANCIAL CORPORATION****CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION**

March 31, 2012 and December 31, 2011

(In thousands, except share and per share data) (Unaudited)

|                                                                                                                                 | March 31,<br>2012 | December 31,<br>2011 |
|---------------------------------------------------------------------------------------------------------------------------------|-------------------|----------------------|
| <b>ASSETS</b>                                                                                                                   |                   |                      |
| Cash and due from other financial institutions                                                                                  | \$ 24,037         | \$ 24,247            |
| Interest-bearing deposits in other financial institutions                                                                       | 154,043           | 96,457               |
| Cash and cash equivalents                                                                                                       | 178,080           | 120,704              |
| Securities, at fair value                                                                                                       | 81,241            | 92,832               |
| Loans held-for-sale                                                                                                             | 521               | 1,918                |
| Loans receivable, net of allowance for loan losses:                                                                             |                   |                      |
| March 31, 2012, \$31,638 and December 31, 2011, \$31,726                                                                        | 1,177,719         | 1,227,391            |
| Other real estate owned                                                                                                         | 20,189            | 22,480               |
| Stock in Federal Home Loan Bank, at cost                                                                                        | 11,336            | 16,346               |
| Premises and equipment, net                                                                                                     | 39,044            | 39,155               |
| Accrued interest receivable                                                                                                     | 4,911             | 5,573                |
| Core deposit intangible                                                                                                         | 3,508             | 3,671                |
| Bank owned life insurance                                                                                                       | 21,333            | 21,207               |
| FDIC prepaid expense                                                                                                            | 4,027             | 4,351                |
| Income tax receivable                                                                                                           | 1,353             | 1,809                |
| Other assets                                                                                                                    | 5,875             | 6,138                |
| Total assets                                                                                                                    | \$ 1,549,137      | \$ 1,563,575         |
| <b>LIABILITIES AND STOCKHOLDERS EQUITY</b>                                                                                      |                   |                      |
| Liabilities:                                                                                                                    |                   |                      |
| Deposits                                                                                                                        |                   |                      |
| Noninterest-bearing                                                                                                             | 144,182           | 142,084              |
| Interest-bearing                                                                                                                | 1,176,398         | 1,190,468            |
| Total deposits                                                                                                                  | 1,320,580         | 1,332,552            |
| Borrowings                                                                                                                      | 9,995             | 9,322                |
| Advance payments by borrowers taxes and insurance                                                                               | 8,136             | 10,976               |
| Accrued interest payable and other liabilities                                                                                  | 8,315             | 10,868               |
| Total liabilities                                                                                                               | 1,347,026         | 1,363,718            |
| Commitments and contingent liabilities                                                                                          |                   |                      |
| <b>Stockholders equity:</b>                                                                                                     |                   |                      |
| Preferred Stock, \$0.01 par value, 25,000,000 shares authorized, none issued or outstanding                                     |                   |                      |
| Common Stock, \$0.01 par value, 100,000,000 shares authorized; 21,072,966 shares issued at March 31, 2012 and December 31, 2011 | 211               | 211                  |
| Additional paid-in capital                                                                                                      | 193,740           | 193,801              |
| Retained earnings                                                                                                               | 20,072            | 17,946               |
| Unearned Employee Stock Ownership Plan shares                                                                                   | (12,968)          | (13,212)             |
| Accumulated other comprehensive income                                                                                          | 1,056             | 1,111                |

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|                                            |              |              |
|--------------------------------------------|--------------|--------------|
| Total stockholders' equity                 | 202,111      | 199,857      |
| Total liabilities and stockholders' equity | \$ 1,549,137 | \$ 1,563,575 |

See accompanying notes to consolidated financial statements.

**Table of Contents****BANKFINANCIAL CORPORATION****CONSOLIDATED STATEMENTS OF OPERATIONS**

Three months ended March 31, 2012 and 2011

(In thousands, except per share data) (Unaudited)

|                                                            | 2012          | 2011          |
|------------------------------------------------------------|---------------|---------------|
| Interest and dividend income                               |               |               |
| Loans, including fees                                      | \$ 16,112     | \$ 14,410     |
| Securities                                                 | 442           | 822           |
| Other                                                      | 80            | 116           |
| <b>Total interest income</b>                               | <b>16,634</b> | <b>15,348</b> |
| Interest expense                                           |               |               |
| Deposits                                                   | 1,214         | 1,900         |
| Borrowings                                                 | 26            | 96            |
| <b>Total interest expense</b>                              | <b>1,240</b>  | <b>1,996</b>  |
| <b>Net interest income</b>                                 | <b>15,394</b> | <b>13,352</b> |
| Provision for loan losses                                  | 996           | 2,424         |
| <b>Net interest income after provision for loan losses</b> | <b>14,398</b> | <b>10,928</b> |
| Noninterest income                                         |               |               |
| Deposit service charges and fees                           | 557           | 614           |
| Other fee income                                           | 385           | 382           |
| Insurance commissions and annuities income                 | 122           | 169           |
| Gain on sale of loans, net                                 | 267           | 19            |
| Loss on disposition of premises and equipment, net         |               | (10)          |
| Loan servicing fees                                        | 128           | 132           |
| Amortization and impairment of servicing assets            | (82)          | (54)          |
| Earnings on bank owned life insurance                      | 126           | 158           |
| Trust                                                      | 184           | 76            |
| Other                                                      | 145           | 85            |
| <b>Total noninterest income</b>                            | <b>1,832</b>  | <b>1,571</b>  |
| Noninterest expense                                        |               |               |
| Compensation and benefits                                  | 6,659         | 6,600         |
| Office occupancy and equipment                             | 1,743         | 1,868         |
| Advertising and public relations                           | 94            | 237           |
| Information technology                                     | 1,261         | 948           |
| Supplies, telephone, and postage                           | 430           | 375           |
| Amortization of intangibles                                | 163           | 382           |
| Nonperforming asset management                             | 1,191         | 455           |
| Operations of other real estate owned                      | 601           | 453           |
| FDIC insurance premiums                                    | 348           | 567           |
| Acquisition costs                                          |               | 1,531         |
| Other                                                      | 946           | 839           |
| <b>Total noninterest expense</b>                           | <b>13,436</b> | <b>14,255</b> |

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|                                                              |            |            |
|--------------------------------------------------------------|------------|------------|
| <b>Income (loss) before income taxes</b>                     | 2,794      | (1,756)    |
| Income tax expense (benefit)                                 | 457        | (979)      |
| <b>Net income (loss)</b>                                     | \$ 2,337   | \$ (777)   |
| Basic income (loss) per common share                         | \$ 0.12    | \$ (0.04)  |
| Diluted income (loss) per common share                       | \$ 0.12    | \$ (0.04)  |
| Weighted average common shares outstanding                   | 19,835,273 | 19,689,723 |
| Diluted weighted average common shares outstanding           | 19,836,080 | 19,689,723 |
| See accompanying notes to consolidated financial statements. |            |            |

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**BANKFINANCIAL CORPORATION**

**CONSOLIDATED STATEMENTS COMPREHENSIVE INCOME (LOSS)**

Three months ended March 31, 2012 and 2011

(In thousands, except per share data) (Unaudited)

|                                                                | <b>2012</b>     | <b>2011</b>       |
|----------------------------------------------------------------|-----------------|-------------------|
| <b>Net income (loss)</b>                                       | <b>\$ 2,337</b> | <b>\$ (777)</b>   |
| Unrealized holding loss arising during the period              | (55)            | (906)             |
| Tax effect                                                     |                 | 345               |
| Change in other comprehensive income (loss), net of tax effect | (55)            | (561)             |
| <b>Comprehensive income (loss)</b>                             | <b>\$ 2,282</b> | <b>\$ (1,338)</b> |

See accompanying notes to consolidated financial statements.



Table of Contents**BANKFINANCIAL CORPORATION****CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS EQUITY**

Three months ended March 31, 2012 and 2011

(In thousands, except per share data) (Unaudited)

|                                                            | Common<br>Stock | Additional<br>Paid-in<br>Capital | Retained<br>Earnings | Unearned<br>Employee<br>Stock<br>Plan<br>Shares | Accumulated<br>Other<br>Comprehen-<br>sive Income | Total      |
|------------------------------------------------------------|-----------------|----------------------------------|----------------------|-------------------------------------------------|---------------------------------------------------|------------|
| <b>Balance at January 1, 2011</b>                          | \$ 211          | \$ 194,186                       | \$ 71,278            | \$ (14,190)                                     | \$ 1,800                                          | \$ 253,285 |
| Net loss                                                   |                 |                                  | (777)                |                                                 |                                                   | (777)      |
| Change in other comprehensive income, net of tax effects   |                 |                                  |                      |                                                 | (561)                                             | (561)      |
| Nonvested stock awards-stock-based compensation expense    |                 | 18                               |                      |                                                 |                                                   | 18         |
| Cash dividends declared on common stock (\$0.07 per share) |                 |                                  | (1,475)              |                                                 |                                                   | (1,475)    |
| ESOP shares earned                                         |                 | (19)                             |                      | 241                                             |                                                   | 222        |
| <b>Balance at March 31, 2011</b>                           | \$ 211          | \$ 194,185                       | \$ 69,026            | \$ (13,949)                                     | \$ 1,239                                          | \$ 250,712 |
| <b>Balance at January 1, 2012</b>                          | \$ 211          | \$ 193,801                       | \$ 17,946            | \$ (13,212)                                     | \$ 1,111                                          | \$ 199,857 |
| Net income                                                 |                 |                                  | 2,337                |                                                 |                                                   | 2,337      |
| Change in other comprehensive income, net of tax effects   |                 |                                  |                      |                                                 | (55)                                              | (55)       |
| Nonvested stock awards-stock-based compensation expense    |                 | 21                               |                      |                                                 |                                                   | 21         |
| Cash dividends declared on common stock (\$0.01 per share) |                 |                                  | (211)                |                                                 |                                                   | (211)      |
| ESOP shares earned                                         |                 | (82)                             |                      | 244                                             |                                                   | 162        |
| <b>Balance at March 31, 2012</b>                           | \$ 211          | \$ 193,740                       | \$ 20,072            | \$ (12,968)                                     | \$ 1,056                                          | \$ 202,111 |

See accompanying notes to consolidated financial statements.

**Table of Contents****BANKFINANCIAL CORPORATION****CONSOLIDATED STATEMENTS OF CASH FLOWS**

Three months ended March 31, 2012 and 2011

(In thousands) (Unaudited)

|                                                                            | 2012      | 2011      |
|----------------------------------------------------------------------------|-----------|-----------|
| <b>Cash flows from operating activities</b>                                |           |           |
| Net income (loss)                                                          | \$ 2,337  | \$ (777)  |
| Adjustments to reconcile to net loss to net cash from operating activities |           |           |
| Provision for loan losses                                                  | 996       | 2,424     |
| ESOP shares earned                                                         | 162       | 222       |
| Stock based compensation expense                                           | 21        | 18        |
| Depreciation and amortization                                              | 1,154     | 1,087     |
| Amortization of premiums and discounts on securities and loans             | (943)     | 170       |
| Amortization of core deposit and other intangible assets                   | 163       | 381       |
| Amortization and impairment of servicing assets                            | 82        | 54        |
| Net change in net deferred loan origination costs                          | 60        | 186       |
| Net gain on sale of other real estate owned                                | (139)     | (52)      |
| Net gain on sale of loans                                                  | (267)     | (19)      |
| Net loss disposition of premises and equipment                             |           | 10        |
| Loans originated for sale                                                  | (6,127)   | (3,154)   |
| Proceeds from sale of loans                                                | 7,791     | 5,889     |
| Net change in:                                                             |           |           |
| Deferred income tax                                                        |           | (980)     |
| Accrued interest receivable                                                | 662       | (397)     |
| Earnings on bank owned life insurance                                      | (126)     | (158)     |
| Other assets                                                               | 992       | 448       |
| Accrued interest payable and other liabilities                             | (2,553)   | (186)     |
| Net cash from operating activities                                         | 4,265     | 5,166     |
| <b>Cash flows from investing activities</b>                                |           |           |
| Securities                                                                 |           |           |
| Proceeds from maturities                                                   | 6,455     | 8,140     |
| Proceeds from principal repayments                                         | 6,209     | 7,892     |
| Purchases of securities                                                    | (1,153)   | (7,113)   |
| Loans receivable                                                           |           |           |
| Principal payments on loans receivable                                     | 156,725   | 172,229   |
| Purchases of loans                                                         |           | (149,409) |
| Originated for investment                                                  | (108,142) | (158,149) |
| Proceeds of redemption of Federal Reserve Bank stock                       |           | 155       |
| Proceeds of redemption of Federal Home Loan Bank of Chicago stock          | 5,010     |           |
| Proceeds from sale of other real estate owned                              | 2,984     | 1,023     |
| Purchase of premises and equipment, net                                    | (685)     | (152)     |
| Cash acquired in acquisition                                               |           | 61,619    |
| Net cash from investing activities                                         | 67,403    | (63,765)  |

(continued)

**Table of Contents****BANKFINANCIAL CORPORATION****CONSOLIDATED STATEMENTS OF CASH FLOWS**

Three months ended March 31, 2012 and 2011

(In thousands) (Unaudited)

|                                                                              | 2012              | 2011              |
|------------------------------------------------------------------------------|-------------------|-------------------|
| <b>Cash flows from financing activities</b>                                  |                   |                   |
| Net change in deposits                                                       | \$ (11,914)       | \$ (26,752)       |
| Net change in advance payments by borrowers for taxes and insurance          | (2,840)           | (1,468)           |
| Net change in borrowings                                                     | 673               | (8,261)           |
| Cash dividends paid on common stock                                          | (211)             | (1,475)           |
| Net cash from financing activities                                           | (14,292)          | (37,956)          |
| Net change in cash and cash equivalents                                      | 57,376            | (96,555)          |
| Beginning cash and cash equivalents                                          | 120,704           | 220,810           |
| <b>Ending cash and cash equivalents</b>                                      | <b>\$ 178,080</b> | <b>\$ 124,255</b> |
| <b>Supplemental disclosures of cash flow information:</b>                    |                   |                   |
| Interest paid                                                                | \$ 1,263          | \$ 1,801          |
| Income taxes paid                                                            |                   |                   |
| Loans transferred to other real estate owned                                 | 1,127             | 1,699             |
| <b>Supplemental disclosures of noncash investing activities Acquisition:</b> |                   |                   |
| Noncash assets acquired:                                                     |                   |                   |
| Securities                                                                   |                   | \$ 10,177         |
| Loans receivable                                                             |                   | 118,147           |
| Other real estate owned                                                      |                   | 6,965             |
| Stock in Federal Home Loan Bank and Federal Reserve Bank                     |                   | 903               |
| Goodwill                                                                     |                   | 1,296             |
| Premises and equipment, net                                                  |                   | 7,442             |
| Accrued interest receivable                                                  |                   | 355               |
| Core deposit intangible                                                      |                   | 2,660             |
| FDIC prepaid expense                                                         |                   | 774               |
| Income tax receivable                                                        |                   | 774               |
| Deferred taxes, net                                                          |                   | 2,662             |
| Other assets                                                                 |                   | 42                |
| Total noncash items acquired                                                 |                   | 152,197           |
| Liabilities assumed:                                                         |                   |                   |
| Deposits                                                                     |                   | 212,939           |
| Advance payments by borrowers taxes and insurance                            |                   | 34                |
| Accrued interest payable and other liabilities                               |                   | 843               |
| Total liabilities assumed                                                    |                   | 213,816           |
| Cash and cash equivalents acquired                                           |                   | \$ 61,619         |

See accompanying notes to consolidated financial statements.



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**BANKFINANCIAL CORPORATION**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

(Table amounts in thousands, except share and per share data)

**NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Basis of Presentation:** BankFinancial Corporation, a Maryland corporation headquartered in Burr Ridge, Illinois, is the owner of all of the issued and outstanding capital stock of BankFinancial, F.S.B. (the Bank).

**Principles of Consolidation:** The interim unaudited consolidated financial statements include the accounts of and transactions of BankFinancial Corporation, the Maryland corporation, the Bank, and the Bank's wholly-owned subsidiaries, Financial Assurance Services, Inc. and BF Asset Recovery Corporation (collectively, the Company) and reflect all normal and recurring adjustments that are, in the opinion of management, considered necessary for a fair presentation of the financial condition and results of operations for the periods presented. All significant intercompany accounts and transactions have been eliminated. The results of operations for the three-month period ended March 31, 2012, are not necessarily indicative of the results of operations that may be expected for the year ending December 31, 2012.

Certain information and note disclosures normally included in financial statements prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission.

**Use of Estimates:** To prepare financial statements in conformity with GAAP, management makes estimates and assumptions based on available information. These estimates and assumptions affect the amounts reported in the financial statements and the disclosures provided, and future results could differ. The allowance for loan losses, mortgage servicing rights, deferred tax assets, stock-based compensation, impairment of securities and fair value of financial instruments are particularly subject to change and the effect of such change could be material to the financial statements.

**Reclassifications:** Certain reclassifications have been made in the prior period's financial statements to conform them to the current period's presentation.

These unaudited consolidated financial statements should be read in conjunction with the Company's Annual Report on Form 10-K for the year ended December 31, 2011, as filed with the Securities and Exchange Commission.

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(Table amounts in thousands, except share and per share data)

**NOTE 2 INCOME (LOSS) PER SHARE**

Amounts reported in income (loss) per share reflect income (loss) available to common stockholders for the period divided by the weighted average number of shares of common stock outstanding during the period, exclusive of unearned ESOP shares and unvested restricted stock shares. Stock options and restricted stock are regarded as potential common stock and are considered in the diluted earnings per share calculations to the extent that they would have a dilutive effect if converted to common stock.

|                                                                                                | <b>Three months ended March 31,</b> |                  |
|------------------------------------------------------------------------------------------------|-------------------------------------|------------------|
|                                                                                                | <b>2012</b>                         | <b>2011</b>      |
| Net income (loss) available to common stockholders                                             | \$ 2,337                            | \$ (777)         |
| Average common shares outstanding                                                              | 21,072,966                          | 21,072,966       |
| Less:                                                                                          |                                     |                  |
| Unearned ESOP shares                                                                           | (1,233,359)                         | (1,374,576)      |
| Unvested restricted stock shares                                                               | (4,334)                             | (8,667)          |
| Weighted average common shares outstanding                                                     | 19,835,273                          | 19,689,723       |
| <b>Basic income (loss) per common share</b>                                                    | <b>\$ 0.12</b>                      | <b>\$ (0.04)</b> |
| Weighted average common shares outstanding                                                     | 19,835,273                          | 19,689,723       |
| Net effect of dilutive stock options and unvested restricted stock                             | 807                                 |                  |
| Weighted average dilutive common shares outstanding                                            | 19,836,080                          | 19,689,723       |
| <b>Diluted income (loss) per common share</b>                                                  | <b>\$ 0.12</b>                      | <b>\$ (0.04)</b> |
| Number of anti-dilutive stock options excluded from the diluted earnings per share calculation | 2,055,553                           | 2,287,553        |
| Weighted average exercise price of anti-dilutive option shares                                 | \$ 16.53                            | \$ 16.52         |

**Table of Contents****BANKFINANCIAL CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

(Table amounts in thousands, except share and per share data)

**NOTE 3 SECURITIES**

The following table summarizes the amortized cost and fair value of securities and the corresponding gross unrealized gains and losses recognized in accumulated other comprehensive income (loss) are as follows:

|                                                 | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Fair<br>Value |
|-------------------------------------------------|-------------------|------------------------------|-------------------------------|---------------|
| <b><u>March 31, 2012</u></b>                    |                   |                              |                               |               |
| Certificates of deposit                         | \$ 24,401         | \$                           | \$                            | \$ 24,401     |
| Municipal securities                            | 515               | 32                           |                               | 547           |
| Equity mutual fund                              | 500               | 23                           |                               | 523           |
| Mortgage-backed securities residential          | 33,449            | 1,449                        |                               | 34,898        |
| Collateralized mortgage obligations residential | 20,590            | 255                          | (19)                          | 20,826        |
| SBA-guaranteed loan participation certificates  | 46                |                              |                               | 46            |
|                                                 | \$ 79,501         | \$ 1,759                     | \$ (19)                       | \$ 81,241     |
| <b><u>December 31, 2011</u></b>                 |                   |                              |                               |               |
| Certificates of deposit                         | \$ 30,448         | \$                           | \$                            | \$ 30,448     |
| Municipal securities                            | 515               | 36                           |                               | 551           |
| Equity mutual fund                              | 500               | 24                           |                               | 524           |
| Mortgage-backed securities residential          | 34,691            | 1,385                        |                               | 36,076        |
| Collateralized mortgage obligations residential | 24,837            | 372                          | (23)                          | 25,186        |
| SBA-guaranteed loan participation certificates  | 47                |                              |                               | 47            |
|                                                 | \$ 91,038         | \$ 1,817                     | \$ (23)                       | \$ 92,832     |

The amortized cost and fair values of securities at March 31, 2012 by contractual maturity are shown below. Securities not due at a single maturity date are shown separately. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

|                                                 | March 31, 2012    |               |
|-------------------------------------------------|-------------------|---------------|
|                                                 | Amortized<br>Cost | Fair<br>Value |
| Within one year                                 | \$ 24,566         | \$ 24,570     |
| One to five years                               | 350               | 378           |
|                                                 | 24,916            | 24,948        |
| Equity mutual fund                              | 500               | 523           |
| Mortgage-backed securities residential          | 33,449            | 34,898        |
| Collateralized mortgage obligations residential | 20,590            | 20,826        |
| SBA-guaranteed loan participation certificates  | 46                | 46            |

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|       |           |           |
|-------|-----------|-----------|
| Total | \$ 79,501 | \$ 81,241 |
|-------|-----------|-----------|



**Table of Contents****BANKFINANCIAL CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

(Table amounts in thousands, except share and per share data)

**NOTE 3 SECURITIES (continued)**

Securities with unrealized losses at March 31, 2012 and December 31, 2011 that were not recognized in income are as follows:

|                                                 | Less than 12 Months<br>Fair<br>Value | Unrealized<br>Loss | 12 Months or More<br>Fair<br>Value | Unrealized<br>Loss | Total<br>Fair<br>Value | Total<br>Unrealized<br>Loss |
|-------------------------------------------------|--------------------------------------|--------------------|------------------------------------|--------------------|------------------------|-----------------------------|
| <b><u>March 31, 2012</u></b>                    |                                      |                    |                                    |                    |                        |                             |
| Collateralized mortgage obligations residential | \$                                   | \$                 | \$ 2,123                           | \$ 19              | \$ 2,123               | \$ 19                       |
| <b><u>December 31, 2011</u></b>                 |                                      |                    |                                    |                    |                        |                             |
| Collateralized mortgage obligations residential | \$                                   | \$                 | \$ 2,134                           | \$ 23              | \$ 2,134               | \$ 23                       |

The Company evaluates marketable investment securities with significant declines in fair value on a quarterly basis to determine whether they should be considered other-than-temporarily impaired under current accounting guidance, which generally provides that if a marketable security is in an unrealized loss position, whether due to general market conditions or industry or issuer-specific factors, the holder of the securities must assess whether the impairment is other-than-temporary.

Collateralized mortgage obligations that the Company holds in its investment portfolio remained in an unrealized loss position at March 31, 2012, but the unrealized losses were not considered significant under the Company's impairment testing methodology. In addition, the Company does not intend to sell this security, and it is likely that the Company will not be required to sell the security before its anticipated recovery occurs.

There were no sales of securities for the quarters ended March 31, 2012 and 2011.

**NOTE 4 LOANS RECEIVABLE**

Loans receivable are as follows:

|                                                  | March 31,<br>2012 | December 31,<br>2011 |
|--------------------------------------------------|-------------------|----------------------|
| One-to-four family residential real estate loans | \$ 262,263        | \$ 272,032           |
| Multi-family mortgage loans                      | 410,341           | 423,615              |
| Nonresidential real estate loans                 | 308,094           | 311,641              |
| Construction and land loans                      | 19,283            | 19,852               |
| Commercial loans                                 | 81,998            | 93,932               |
| Commercial leases                                | 124,319           | 134,990              |
| Consumer loans                                   | 2,211             | 2,147                |
| Total loans                                      | 1,208,509         | 1,258,209            |

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|                                     |              |              |
|-------------------------------------|--------------|--------------|
| Net deferred loan origination costs | 848          | 908          |
| Allowance for loan losses           | (31,638)     | (31,726)     |
| Loans, net                          | \$ 1,177,719 | \$ 1,227,391 |

**Table of Contents****BANKFINANCIAL CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

(Table amounts in thousands, except share and per share data)

**NOTE 4 LOANS RECEIVABLE (continued)**

The following tables present the balance in the allowance for loan losses and the loans receivable by portfolio segment and based on impairment method:

|                                                  | Allowance for loan losses                      |                                |                                                |                  | Loan Balances                               |                                |                                                |                     |
|--------------------------------------------------|------------------------------------------------|--------------------------------|------------------------------------------------|------------------|---------------------------------------------|--------------------------------|------------------------------------------------|---------------------|
|                                                  | Individually<br>evaluated<br>for<br>impairment | Purchased<br>impaired<br>loans | Collectively<br>evaluated<br>for<br>impairment | Total            | Individually<br>evaluated for<br>impairment | Purchased<br>impaired<br>loans | Collectively<br>evaluated<br>for<br>impairment | Total               |
| <b>March 31, 2012</b>                            |                                                |                                |                                                |                  |                                             |                                |                                                |                     |
| One-to-four family residential real estate loans | \$ 1,557                                       | \$ 303                         | \$ 4,186                                       | \$ 6,046         | \$ 14,400                                   | \$ 3,670                       | \$ 244,193                                     | \$ 262,263          |
| Multi-family mortgage loans                      | 1,529                                          |                                | 4,008                                          | 5,537            | 18,918                                      | 1,454                          | 389,969                                        | 410,341             |
| Nonresidential real estate loans                 | 7,763                                          | 6                              | 5,565                                          | 13,334           | 33,905                                      | 3,308                          | 270,881                                        | 308,094             |
| Construction and land loans                      | 1,023                                          |                                | 770                                            | 1,793            | 3,268                                       | 4,859                          | 11,156                                         | 19,283              |
| Commercial loans                                 | 2,653                                          | 28                             | 1,626                                          | 4,307            | 3,714                                       | 841                            | 77,443                                         | 81,998              |
| Commercial leases                                | 22                                             |                                | 533                                            | 555              | 22                                          |                                | 124,297                                        | 124,319             |
| Consumer loans                                   | 8                                              |                                | 58                                             | 66               | 8                                           |                                | 2,203                                          | 2,211               |
| <b>Total</b>                                     | <b>\$ 14,555</b>                               | <b>\$ 337</b>                  | <b>\$ 16,746</b>                               | <b>\$ 31,638</b> | <b>\$ 74,235</b>                            | <b>\$ 14,132</b>               | <b>\$ 1,120,142</b>                            | <b>1,208,509</b>    |
| Net deferred loan origination costs              |                                                |                                |                                                |                  |                                             |                                |                                                | 848                 |
| Allowance for loan losses                        |                                                |                                |                                                |                  |                                             |                                |                                                | (31,638)            |
| <b>Loans, net</b>                                |                                                |                                |                                                |                  |                                             |                                |                                                | <b>\$ 1,177,719</b> |

|                                                  | Allowance for loan losses                   |                                                |                  |                                             | Loan Balances               |                                                |                  |  |
|--------------------------------------------------|---------------------------------------------|------------------------------------------------|------------------|---------------------------------------------|-----------------------------|------------------------------------------------|------------------|--|
|                                                  | Individually<br>evaluated for<br>impairment | Collectively<br>evaluated<br>for<br>impairment | Total            | Individually<br>evaluated for<br>impairment | Purchased<br>impaired loans | Collectively<br>evaluated<br>for<br>impairment | Total            |  |
| <b>December 31, 2011</b>                         |                                             |                                                |                  |                                             |                             |                                                |                  |  |
| One-to-four family residential real estate loans | \$ 1,883                                    | \$ 4,220                                       | \$ 6,103         | \$ 14,181                                   | \$ 3,941                    | \$ 253,910                                     | \$ 272,032       |  |
| Multi-family mortgage loans                      | 1,881                                       | 4,201                                          | 6,082            | 20,380                                      | 1,418                       | 401,817                                        | 423,615          |  |
| Nonresidential real estate loans                 | 8,126                                       | 5,630                                          | 13,756           | 32,669                                      | 3,375                       | 275,597                                        | 311,641          |  |
| Construction and land loans                      | 959                                         | 725                                            | 1,684            | 3,263                                       | 4,788                       | 11,801                                         | 19,852           |  |
| Commercial loans                                 | 2,079                                       | 1,460                                          | 3,539            | 3,160                                       | 1,078                       | 89,694                                         | 93,932           |  |
| Commercial leases                                | 22                                          | 482                                            | 504              | 22                                          |                             | 134,968                                        | 134,990          |  |
| Consumer loans                                   | 3                                           | 55                                             | 58               | 3                                           |                             | 2,144                                          | 2,147            |  |
| <b>Total</b>                                     | <b>\$ 14,953</b>                            | <b>\$ 16,773</b>                               | <b>\$ 31,726</b> | <b>\$ 73,678</b>                            | <b>\$ 14,600</b>            | <b>\$ 1,169,931</b>                            | <b>1,258,209</b> |  |
| Net deferred loan origination costs              |                                             |                                                |                  |                                             |                             |                                                | 908              |  |

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|                           |              |
|---------------------------|--------------|
| Allowance for loan losses | (31,726)     |
| Loans, net                | \$ 1,227,391 |

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(Table amounts in thousands, except share and per share data)

**NOTE 4 LOANS RECEIVABLE (continued)**

Activity in the allowance for loan losses is as follows:

|                                                  | <b>For the Three Months Ended<br/>March 31,</b> |             |
|--------------------------------------------------|-------------------------------------------------|-------------|
|                                                  | <b>2012</b>                                     | <b>2011</b> |
| Beginning balance                                | \$ 31,726                                       | \$ 22,180   |
| Loans charged offs:                              |                                                 |             |
| One-to-four family residential real estate loans | (672)                                           | (1,628)     |
| Multi-family mortgage loans                      | (554)                                           | (237)       |
| Nonresidential real estate loans                 | (433)                                           |             |
| Construction and land loans                      | (47)                                            | (378)       |
| Commercial loans                                 | (138)                                           |             |
| Commercial leases                                |                                                 |             |
| Consumer loans                                   | (12)                                            | (16)        |
|                                                  | (1,856)                                         | (2,259)     |
| Recoveries:                                      |                                                 |             |
| One-to-four family residential real estate loans | 111                                             | 2           |
| Multi-family mortgage loans                      | 384                                             | 89          |
| Nonresidential real estate loans                 | 31                                              | 58          |
| Construction and land loans                      | 184                                             |             |
| Commercial loans                                 | 57                                              | 10          |
| Commercial leases                                |                                                 |             |
| Consumer loans                                   | 5                                               |             |
|                                                  | 772                                             | 159         |
| Net charge-off                                   | (1,084)                                         | (2,100)     |
| Provision for loan losses                        | 996                                             | 2,424       |
| Ending balance                                   | \$ 31,638                                       | \$ 22,504   |

**Impaired loans**

|                                                   | <b>March 31,<br/>2012</b> | <b>December 31,<br/>2011</b> |
|---------------------------------------------------|---------------------------|------------------------------|
| Loans with allocated allowance for loan losses    | \$ 46,892                 | \$ 45,649                    |
| Loans with no allocated allowance for loan losses | 27,343                    | 28,029                       |

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|                          |           |           |
|--------------------------|-----------|-----------|
|                          | 74,235    | 73,678    |
| Purchased impaired loans | 14,132    | 14,600    |
| Total impaired loans     | \$ 88,367 | \$ 88,278 |

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(Table amounts in thousands, except share and per share data)

**NOTE 4 LOANS RECEIVABLE (continued)**

The following table includes the unpaid principal balances and recorded investment for impaired loans, by class, with the associated allowance amount, if applicable. In addition, the table includes the average recorded investments in the impaired loans and the related amount of interest recognized for the duration of the impairment within the period reported.

|                                                                     | <b>Loan<br/>Balance</b> | <b>Recorded<br/>Investment</b> | <b>Allowance<br/>for Loan<br/>Losses<br/>Allocated</b> | <b>Average<br/>Investment<br/>in Impaired<br/>Loans</b> | <b>Interest<br/>Income<br/>Recognized</b> |
|---------------------------------------------------------------------|-------------------------|--------------------------------|--------------------------------------------------------|---------------------------------------------------------|-------------------------------------------|
| <b>March 31, 2012</b>                                               |                         |                                |                                                        |                                                         |                                           |
| With no related allowance recorded:                                 |                         |                                |                                                        |                                                         |                                           |
| One-to-four family residential real estate loans                    | \$ 2,647                | \$ 2,670                       | \$                                                     | \$ 2,215                                                | \$ 30                                     |
| One-to-four family residential real estate loans non-owner occupied | 6,550                   | 6,598                          | \$                                                     | 6,223                                                   | 47                                        |
| Multi-family mortgage loans                                         | 8,490                   | 8,753                          |                                                        | 8,803                                                   | 64                                        |
| Wholesale commercial lending                                        | 3,302                   | 3,307                          |                                                        | 3,303                                                   | 30                                        |
| Nonresidential real estate loans                                    | 6,140                   | 6,409                          |                                                        | 6,893                                                   | 41                                        |
| Commercial loans secured                                            | 214                     | 215                            |                                                        | 226                                                     | 5                                         |
|                                                                     | 27,343                  | 27,952                         |                                                        | 27,663                                                  | 217                                       |
| With an allowance recorded:                                         |                         |                                |                                                        |                                                         |                                           |
| One-to-four family residential real estate loans                    | 3,078                   | 3,223                          | 773                                                    | 3,701                                                   | 9                                         |
| One-to-four family residential real estate loans non-owner occupied | 2,125                   | 2,250                          | 784                                                    | 1,922                                                   | 6                                         |
| Multi-family mortgage loans                                         | 7,126                   | 7,578                          | 1,529                                                  | 7,887                                                   | 20                                        |
| Nonresidential real estate loans                                    | 27,765                  | 28,844                         | 7,763                                                  | 26,027                                                  | 66                                        |
| Land loans                                                          | 3,268                   | 3,384                          | 1,023                                                  | 3,266                                                   |                                           |
| Commercial loans secured                                            | 2,864                   | 3,176                          | 2,044                                                  | 2,864                                                   |                                           |
| Commercial loans unsecured                                          | 636                     | 681                            | 609                                                    | 198                                                     |                                           |
| Non-rated commercial leases                                         | 22                      | 22                             | 22                                                     | 22                                                      |                                           |
| Consumer loans                                                      | 8                       | 9                              | 8                                                      | 4                                                       |                                           |
|                                                                     | 46,892                  | 49,167                         | 14,555                                                 | 45,891                                                  | 101                                       |
| <b>Total</b>                                                        | <b>\$ 74,235</b>        | <b>\$ 77,119</b>               | <b>\$ 14,555</b>                                       | <b>\$ 73,554</b>                                        | <b>\$ 318</b>                             |

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(Table amounts in thousands, except share and per share data)

**NOTE 4 LOANS RECEIVABLE (continued)**

|                                                                     | Loan<br>Balance | Recorded<br>Investment | Allowance<br>for Loan<br>Losses<br>Allocated | Average<br>Investment<br>in Impaired<br>Loans | Interest<br>Income<br>Recognized |
|---------------------------------------------------------------------|-----------------|------------------------|----------------------------------------------|-----------------------------------------------|----------------------------------|
| <b>December 31, 2011</b>                                            |                 |                        |                                              |                                               |                                  |
| With no related allowance recorded:                                 |                 |                        |                                              |                                               |                                  |
| One-to-four family residential real estate loans                    | \$ 2,329        | \$ 2,347               | \$                                           | \$ 623                                        | \$ 24                            |
| One-to-four family residential real estate loans non-owner occupied | 5,945           | 5,868                  | \$                                           | 2,499                                         | 266                              |
| Multi-family mortgage loans                                         | 8,910           | 9,113                  |                                              | 5,567                                         | 378                              |
| Wholesale commercial lending                                        | 3,304           | 3,300                  |                                              | 338                                           | 35                               |
| Nonresidential real estate loans                                    | 7,304           | 7,468                  |                                              | 5,977                                         | 275                              |
| Construction loans                                                  |                 |                        |                                              | 77                                            |                                  |
| Land loans                                                          |                 |                        |                                              | 70                                            |                                  |
| Commercial loans secured                                            | 237             | 244                    |                                              | 448                                           | 45                               |
| Commercial loans unsecured                                          |                 |                        |                                              |                                               | 41                               |
| Commercial loans other                                              |                 |                        |                                              | 44                                            | 15                               |
|                                                                     | 28,029          | 28,340                 |                                              | 15,643                                        | 1,079                            |
| With an allowance recorded:                                         |                 |                        |                                              |                                               |                                  |
| One-to-four family residential real estate loans                    | 3,970           | 4,145                  | 1,055                                        | 1,406                                         | 2                                |
| One-to-four family residential real estate loans non-owner occupied | 1,937           | 2,051                  | 828                                          | 2,962                                         |                                  |
| Multi-family mortgage loans                                         | 8,166           | 8,594                  | 1,881                                        | 4,307                                         | 5                                |
| Wholesale commercial lending                                        |                 |                        |                                              | 4,066                                         |                                  |
| Nonresidential real estate loans                                    | 25,365          | 26,157                 | 8,126                                        | 12,134                                        | 75                               |
| Construction loans                                                  |                 |                        |                                              | 1,392                                         |                                  |
| Land loans                                                          | 3,263           | 3,315                  | 959                                          | 2,128                                         | 82                               |
| Commercial loans secured                                            | 2,869           | 3,144                  | 2,048                                        | 3,253                                         |                                  |
| Commercial loans unsecured                                          | 54              | 63                     | 31                                           | 150                                           |                                  |
| Commercial loans other                                              |                 |                        |                                              | 22                                            |                                  |
| Non-rated commercial leases                                         | 22              | 22                     | 22                                           | 98                                            |                                  |
| Consumer loans                                                      | 3               | 3                      | 3                                            |                                               |                                  |
|                                                                     | 45,649          | 47,494                 | 14,953                                       | 31,918                                        | 164                              |
| Total                                                               | \$ 73,678       | \$ 75,834              | \$ 14,953                                    | \$ 47,561                                     | \$ 1,243                         |



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(Table amounts in thousands, except share and per share data)

**NOTE 4 LOANS RECEIVABLE (continued)****Purchased Impaired Loans**

As a result of its acquisition of Downers Grove National Bank, the Company holds purchased loans for which there was evidence of deterioration of credit quality since origination and for which it was probable that all contractually required payments would not be collected as of the date of the acquisition. The carrying amount of these purchased impaired loans is as follows:

|                                                                                           | <b>March 31,<br/>2012</b> | <b>December 31,<br/>2011</b> |
|-------------------------------------------------------------------------------------------|---------------------------|------------------------------|
| One to four family residential real estate loans                                          | \$ 3,670                  | \$ 3,941                     |
| Multi-family mortgage loans                                                               | 1,454                     | 1,418                        |
| Nonresidential real estate loans                                                          | 3,308                     | 3,375                        |
| Construction loans                                                                        | 834                       | 813                          |
| Land loans                                                                                | 4,025                     | 3,975                        |
| Commercial loans                                                                          | 841                       | 1,078                        |
| <b>Outstanding balance</b>                                                                | <b>\$ 14,132</b>          | <b>\$ 14,600</b>             |
| Carrying amount, net of allowance: \$337,000 at March 31, 2012, none at December 31, 2011 | \$ 13,795                 | \$ 14,600                    |

Accretable yield, or income expected to be collected, related to purchased impaired loans is as follows:

|                       | <b>For the Three Months Ended<br/>March 31,</b> |                 |
|-----------------------|-------------------------------------------------|-----------------|
|                       | <b>2012</b>                                     | <b>2011</b>     |
| Beginning balance     | \$ 2,270                                        | \$ 3,410        |
| New loans purchased   |                                                 | 3,410           |
| Accretion of income   | 480                                             |                 |
| <b>Ending balance</b> | <b>\$ 1,790</b>                                 | <b>\$ 3,410</b> |

For the above purchased impaired loans, the Company increased the allowance for loan losses by \$337,000 during the three months ended March 31, 2012. No allowance for loan losses was recorded for these loans for the three months ended March 31, 2011.

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(Table amounts in thousands, except share and per share data)

**NOTE 4 LOANS RECEIVABLE (continued)**

Purchased impaired loans for which it was probable at the date of acquisition that all contractually required payments would not be collected are as follows:

|                                                                | <b>March 31,<br/>2012</b> | <b>December 31,<br/>2011</b> |
|----------------------------------------------------------------|---------------------------|------------------------------|
| Contractually required payments receivable of loans purchased: |                           |                              |
| One-to-four family residential real estate loans               | \$ 5,449                  | \$ 5,886                     |
| Multi-family mortgage loans                                    | 3,456                     | 3,456                        |
| Nonresidential real estate loans                               | 5,362                     | 5,395                        |
| Construction loans                                             | 1,314                     | 1,314                        |
| Land loans                                                     | 7,982                     | 8,152                        |
| Commercial loans                                               | 7,580                     | 7,672                        |
| Consumer loans                                                 | 32                        | 33                           |
|                                                                | <b>\$ 31,175</b>          | <b>\$ 31,908</b>             |
| Cash flows expected to be collected at acquisition             |                           | \$ 18,779                    |
| Fair value of purchased impaired loans at acquisition          |                           | 15,369                       |

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(Table amounts in thousands, except share and per share data)

**NOTE 4 LOANS RECEIVABLE (continued)****Nonaccrual loans**

The following table presents the recorded investment in nonaccrual and loans past due over 90 days and still on accrual by class of loans, excluding purchased impaired loans:

|                                                                     | Unpaid<br>Principal<br>Balance | Recorded<br>Investment | Loans Past<br>Due Over 90<br>Days, still<br>accruing |
|---------------------------------------------------------------------|--------------------------------|------------------------|------------------------------------------------------|
| <b><u>March 31, 2012</u></b>                                        |                                |                        |                                                      |
| One-to-four family residential real estate loans                    | \$ 6,425                       | \$ 6,721               | \$ 30                                                |
| One-to-four family residential real estate loans non owner occupied | 5,177                          | 5,356                  | 33                                                   |
| Multi-family mortgage loans                                         | 13,264                         | 13,879                 | 666                                                  |
| Nonresidential real estate loans                                    | 32,892                         | 33,929                 | 99                                                   |
| Land loans                                                          | 3,263                          | 3,384                  |                                                      |
| Commercial loans secured                                            | 2,880                          | 3,176                  |                                                      |
| Commercial loans unsecured                                          | 647                            | 693                    |                                                      |
| Non-rated commercial leases                                         | 22                             | 22                     |                                                      |
| Consumer loans                                                      | 8                              | 9                      |                                                      |
|                                                                     | \$ 64,578                      | \$ 67,169              | \$ 828                                               |
| <b><u>December 31, 2011</u></b>                                     |                                |                        |                                                      |
| One-to-four family residential real estate loans                    | \$ 6,199                       | \$ 6,488               | \$ 40                                                |
| One-to-four family residential real estate loans non owner occupied | 4,510                          | 4,647                  |                                                      |
| Multi-family mortgage loans                                         | 14,983                         | 15,495                 |                                                      |
| Nonresidential real estate loans                                    | 30,396                         | 31,104                 | 125                                                  |
| Land loans                                                          | 3,263                          | 3,315                  | 185                                                  |
| Commercial loans secured                                            | 2,885                          | 3,144                  |                                                      |
| Commercial loans unsecured                                          | 55                             | 63                     |                                                      |
| Non-rated commercial leases                                         | 22                             | 22                     |                                                      |
| Consumer loans                                                      | 3                              | 3                      |                                                      |
|                                                                     | \$ 62,316                      | \$ 64,281              | \$ 350                                               |

Nonaccrual loans and impaired loans are defined differently. Some loans may be included in both categories, and some may only be included in one category. Nonaccrual loans include both smaller balance homogeneous loans that are collectively evaluated for impairment and individually classified impaired loans.

The Company's reserve for uncollected loan interest was \$3.3 million and \$2.7 million at March 31, 2012 and December 31, 2011, respectively. Except for purchased impaired loans, when a loan is on non-accrual status and the ultimate collectability of the total principal of an impaired loan is in doubt, all payments are applied to principal under the cost recovery method. Alternatively, when a loan is on non-accrual status but

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there is doubt concerning only the ultimate collectability of interest, contractual interest is credited to interest income only when received, under the cash basis method pursuant to the provisions of FASB ASC 310-10, as applicable. In all cases, the average balances are calculated based on the month-end balances of the financing receivables within the period reported pursuant to the provisions of FASB ASC 310-10, as applicable.

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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

(Table amounts in thousands, except share and per share data)

**NOTE 4 LOANS RECEIVABLE (continued)**

Generally, the Company utilizes the 90 days delinquent, still accruing category of loan classification when: (1) the loan is repaid in full shortly after the period end date; (2) the loan is well secured and there are no asserted or pending legal barriers to its collection; or (3) the borrower has remitted all scheduled payments and is otherwise in substantial compliance with the terms of the loan, but the processing of payments actually received or the renewal of a loan has not occurred for administrative reasons.

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(Table amounts in thousands, except share and per share data)

**NOTE 4 LOANS RECEIVABLE (continued)****Past Due Loans**

The following tables present the aging of the recorded investment in past due loans by class of loans, excluding purchased impaired loans:

|                                                                        | 30-59 Days<br>Past Due   | 60-89 Days<br>Past Due  | 90 Days<br>or<br>Greater<br>Past Due | Total Past<br>Due | Loans Not<br>Past Due | Total        |
|------------------------------------------------------------------------|--------------------------|-------------------------|--------------------------------------|-------------------|-----------------------|--------------|
| <b>March 31, 2012</b>                                                  |                          |                         |                                      |                   |                       |              |
| One-to-four family residential real estate loans                       | \$ 1,896                 | \$ 539                  | \$ 6,059                             | \$ 8,494          | \$ 174,870            | \$ 183,364   |
| One-to-four family residential real estate loans<br>non-owner occupied | 2,339                    | 248                     | 3,439                                | 6,026             | 69,434                | 75,460       |
| Multi-family mortgage loans                                            | 8,945                    |                         | 11,919                               | 20,864            | 322,208               | 343,072      |
| Wholesale commercial lending                                           | 1,366                    |                         |                                      | 1,366             | 63,675                | 65,041       |
| Nonresidential real estate loans                                       | 14,415                   | 168                     | 20,953                               | 35,536            | 268,954               | 304,490      |
| Construction loans                                                     |                          |                         |                                      |                   | 1,379                 | 1,379        |
| Land loans                                                             | 4,818                    |                         | 3,384                                | 8,202             | 4,972                 | 13,174       |
| Commercial loans:                                                      |                          |                         |                                      |                   |                       |              |
| Secured                                                                | 11                       | 110                     | 3,167                                | 3,288             | 24,377                | 27,665       |
| Unsecured                                                              | 2,758                    | 46                      | 654                                  | 3,458             | 6,676                 | 10,134       |
| Municipal loans                                                        |                          |                         |                                      |                   | 5,887                 | 5,887        |
| Warehouse lines                                                        | 41                       |                         |                                      | 41                | 9,367                 | 9,408        |
| Health care                                                            |                          |                         |                                      |                   | 20,705                | 20,705       |
| Other                                                                  |                          |                         |                                      |                   | 7,981                 | 7,981        |
| Commercial leases:                                                     |                          |                         |                                      |                   |                       |              |
| Investment rated commercial leases                                     | 504                      |                         |                                      | 504               | 78,956                | 79,460       |
| Below investment grade                                                 | 195                      |                         |                                      | 195               | 7,163                 | 7,358        |
| Non-rated                                                              | 542                      |                         | 22                                   | 564               | 32,057                | 32,621       |
| Lease pools                                                            |                          |                         |                                      |                   | 5,732                 | 5,732        |
| Consumer loans                                                         |                          |                         | 5                                    | 5                 | 2,217                 | 2,222        |
| Total                                                                  | \$ 37,830 <sup>(1)</sup> | \$ 1,111 <sup>(1)</sup> | \$ 49,602                            | \$ 88,543         | \$ 1,106,610          | \$ 1,195,153 |

(1) 26% of the combined 30-89 days past due loans have matured and are in the process of analysis and renewal.

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(Table amounts in thousands, except share and per share data)

**NOTE 4 LOANS RECEIVABLE (continued)**

The following table presents the aging of the recorded investment in past due purchased impaired loans by class of loans:

|                                                                     | 30-59 Days<br>Past Due | 60-89 Days<br>Past Due | 90 Days or<br>Greater<br>Past Due | Total Past<br>Due | Loans Not<br>Past Due | Total     |
|---------------------------------------------------------------------|------------------------|------------------------|-----------------------------------|-------------------|-----------------------|-----------|
| <b><u>March 31, 2012</u></b>                                        |                        |                        |                                   |                   |                       |           |
| One-to-four family residential real estate loans non-owner occupied | \$                     | \$                     | \$ 2,948                          | \$ 2,948          | \$ 723                | \$ 3,671  |
| Multi-family mortgage loans                                         |                        |                        | 1,454                             | 1,454             |                       | 1,454     |
| Nonresidential real estate loans                                    |                        |                        | 1,184                             | 1,184             | 2,123                 | 3,307     |
| Construction loans                                                  |                        |                        | 834                               | 834               |                       | 834       |
| Land loans                                                          |                        |                        | 3,650                             | 3,650             | 367                   | 4,017     |
| Commercial loans secured                                            |                        |                        | 680                               | 680               | 161                   | 841       |
| Total                                                               | \$                     | \$                     | \$ 10,750                         | \$ 10,750         | \$ 3,374              | \$ 14,124 |

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(Table amounts in thousands, except share and per share data)

**NOTE 4 LOANS RECEIVABLE (continued)**

The following tables present the aging of the recorded investment in past due loans by class of loans, excluding purchased impaired loans:

|                                                                        | 30-59 Days<br>Past Due   | 60-89 Days<br>Past Due   | 90 Days<br>or<br>Greater<br>Past Due | Total Past<br>Due | Loans Not<br>Past Due | Total        |
|------------------------------------------------------------------------|--------------------------|--------------------------|--------------------------------------|-------------------|-----------------------|--------------|
| <b>December 31, 2011</b>                                               |                          |                          |                                      |                   |                       |              |
| One-to-four family residential real estate loans                       | \$ 2,259                 | \$ 605                   | \$ 5,925                             | \$ 8,789          | \$ 182,895            | \$ 191,684   |
| One-to-four family residential real estate loans<br>non-owner occupied | 2,307                    | 122                      | 3,005                                | 5,434             | 71,114                | 76,548       |
| Multi-family mortgage loans                                            | 6,002                    | 4,176                    | 13,237                               | 23,415            | 327,488               | 350,903      |
| Wholesale commercial lending                                           | 785                      |                          |                                      | 785               | 67,723                | 68,508       |
| Nonresidential real estate loans                                       | 3,387                    | 6,183                    | 17,971                               | 27,541            | 279,628               | 307,169      |
| Construction loans                                                     |                          | 520                      |                                      | 520               | 1,336                 | 1,856        |
| Land loans                                                             | 5,445                    | 1,152                    | 462                                  | 7,059             | 6,273                 | 13,332       |
| Commercial loans:                                                      |                          |                          |                                      |                   |                       |              |
| Secured                                                                | 17                       |                          | 3,143                                | 3,160             | 26,193                | 29,353       |
| Unsecured                                                              | 435                      | 3                        | 63                                   | 501               | 9,387                 | 9,888        |
| Municipal loans                                                        |                          |                          |                                      |                   | 6,471                 | 6,471        |
| Warehouse lines                                                        |                          |                          |                                      |                   | 9,862                 | 9,862        |
| Health care                                                            |                          |                          |                                      |                   | 29,510                | 29,510       |
| Other                                                                  |                          |                          |                                      |                   | 8,425                 | 8,425        |
| Commercial leases:                                                     |                          |                          |                                      |                   |                       |              |
| Investment rated commercial leases                                     | 294                      |                          |                                      | 294               | 84,378                | 84,672       |
| Below investment grade                                                 |                          |                          |                                      |                   | 6,263                 | 6,263        |
| Non-rated                                                              | 290                      |                          | 23                                   | 313               | 37,053                | 37,366       |
| Lease pools                                                            |                          |                          |                                      |                   | 7,824                 | 7,824        |
| Consumer loans                                                         | 7                        |                          |                                      | 7                 | 2,152                 | 2,159        |
| Total                                                                  | \$ 21,228 <sup>(1)</sup> | \$ 12,761 <sup>(1)</sup> | \$ 43,829                            | \$ 77,818         | \$ 1,163,975          | \$ 1,241,793 |

(1) 46% of the combined 30-89 days past due loans have matured and are in the process of analysis and renewal.



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**NOTE 4 LOANS RECEIVABLE (continued)**

The following table presents the aging of the recorded investment in past due purchased impaired loans by class of loans:

|                                                                     | 30-59 Days<br>Past Due | 60-89 Days<br>Past Due | 90 Days<br>or<br>Greater<br>Past Due | Total<br>Past Due | Loans Not<br>Past Due | Total            |
|---------------------------------------------------------------------|------------------------|------------------------|--------------------------------------|-------------------|-----------------------|------------------|
| <b><u>December 31, 2011</u></b>                                     |                        |                        |                                      |                   |                       |                  |
| One-to-four family residential real estate loans non-owner occupied | \$                     | \$                     | \$ 2,835                             | \$ 2,835          | \$ 1,087              | \$ 3,922         |
| Multi-family mortgage loans                                         |                        |                        | 1,418                                | 1,418             |                       | 1,418            |
| Nonresidential real estate loans                                    | 996                    |                        | 1,681                                | 2,677             | 688                   | 3,365            |
| Construction loans                                                  |                        |                        | 813                                  | 813               |                       | 813              |
| Land loans                                                          |                        |                        | 3,578                                | 3,578             | 369                   | 3,947            |
| Commercial loans secured                                            |                        |                        | 807                                  | 807               | 162                   | 969              |
| Commercial loans unsecured                                          |                        |                        | 34                                   | 34                |                       | 34               |
| <b>Total</b>                                                        | <b>\$ 996</b>          | <b>\$</b>              | <b>\$ 11,166</b>                     | <b>\$ 12,162</b>  | <b>\$ 2,306</b>       | <b>\$ 14,468</b> |

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**NOTE 4 LOANS RECEIVABLE (continued)****Troubled Debt Restructurings**

The Company evaluates loan extensions or modifications in accordance with FASB ASC 310-40 with respect to the classification of the loan as a troubled debt restructuring (TDR). In general, if the Company grants a loan extension or modification to a borrower for other than an insignificant period of time that includes a below market interest rate, principal forgiveness, payment forbearance or other concession intended to minimize the economic loss to the Company, the loan extension or loan modification is classified as a TDR. In cases where borrowers are granted new terms that provide for a reduction of either interest or principal then due and payable, management measures any impairment on the restructured loan in the same manner as for impaired loans as noted above.

The Company had \$16.8 million of TDRs at March 31, 2012, compared to \$18.1 million at December 31, 2011, with \$1.1 million in specific valuation allowances allocated to those loans at March 31, 2012, and \$1.2 million in specific valuation reserves allocated at December 31, 2011. The Company had no outstanding commitments to borrowers whose loans are classified as TDRs.

The following table presents loans by class classified as TDRs:

|                                                            | March 31,<br>2012 | December 31,<br>2011 |
|------------------------------------------------------------|-------------------|----------------------|
| One-to-four family residential real estate                 | \$ 5,447          | \$ 5,619             |
| Multi-family mortgage                                      | 5,771             | 5,783                |
| Nonresidential real estate                                 | 1,017             | 2,220                |
| Commercial loans - secured                                 | 215               | 238                  |
| <b>Troubled debt restructured loans - accrual loans</b>    | <b>12,450</b>     | <b>13,860</b>        |
| One-to-four family residential real estate                 | 358               | 556                  |
| Multi-family mortgage                                      | 1,217             | 717                  |
| Nonresidential real estate                                 | 2,786             | 2,960                |
| Commercial loans - secured                                 |                   |                      |
| Consumer loans                                             | 3                 | 3                    |
| <b>Troubled debt restructured loans - nonaccrual loans</b> | <b>4,364</b>      | <b>4,236</b>         |
| <b>Total troubled debt restructured loans</b>              | <b>\$ 16,814</b>  | <b>\$ 18,096</b>     |

During the periods ending March 31, 2012 and 2011, the terms of certain loans were modified and classified as TDRs. The modification of the terms of such loans included one or a combination of the following: a reduction of the stated interest rate of the loan; an extension of the maturity date at a stated rate of interest lower than the current market rate for new debt with similar risk; or a permanent reduction of the recorded investment in the loan.

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**NOTE 4 LOANS RECEIVABLE (continued)**

The following tables present loans by class that were modified as TDRs during the three months ended March 31, 2012:

|                                            | <b>Number<br/>of<br/>loans</b> | <b>Pre-Modification<br/>outstanding<br/>recorded investment</b> | <b>Post-Modification<br/>outstanding<br/>recorded investment</b> |
|--------------------------------------------|--------------------------------|-----------------------------------------------------------------|------------------------------------------------------------------|
| One-to-four family residential real estate | 2                              | \$ 392                                                          | \$ 392                                                           |
| Multi-family mortgage                      | 1                              | 700                                                             | 500                                                              |
| <b>Total</b>                               | <b>3</b>                       | <b>\$ 1,092</b>                                                 | <b>\$ 892</b>                                                    |

|                                            | <b>Due to<br/>reduction in<br/>interest<br/>rate</b> | <b>Due to<br/>extension of<br/>maturity date</b> | <b>Due to<br/>permanent<br/>reduction in<br/>recorded<br/>investment</b> | <b>Total</b>  |
|--------------------------------------------|------------------------------------------------------|--------------------------------------------------|--------------------------------------------------------------------------|---------------|
| One-to-four family residential real estate | \$ 372                                               | \$ 20                                            | \$                                                                       | \$ 392        |
| Multi-family mortgage                      |                                                      |                                                  | 500                                                                      | 500           |
| <b>Total</b>                               | <b>\$ 372</b>                                        | <b>\$ 20</b>                                     | <b>\$ 500</b>                                                            | <b>\$ 892</b> |

The TDRs described above had no impact on interest income, increased the allowance for loan losses by \$183,000 and resulted in charge offs of \$470,000 during the three months ended March 31, 2012.

The following table presents loans by class modified as TDRs for which there was a payment default within twelve months following the modification during the three months ended March 31, 2012:

|                                            | <b>Number<br/>of<br/>loans</b> | <b>Recorded<br/>investment</b> |
|--------------------------------------------|--------------------------------|--------------------------------|
| One-to-four family residential real estate | 1                              | \$ 278                         |
| Nonresidential real estate                 | 1                              | 700                            |
| <b>Total</b>                               | <b>2</b>                       | <b>\$ 978</b>                  |

The following tables present loans by class that were modified as TDRs during the three months ended March 31, 2011:

|                                                                        | Number<br>of<br>borrowers | Pre-Modification<br>outstanding<br>recorded investment | Post-Modification<br>outstanding<br>recorded investment |
|------------------------------------------------------------------------|---------------------------|--------------------------------------------------------|---------------------------------------------------------|
| One-to-four family residential real estate<br>loans non-owner occupied | 1                         | \$ 5,514                                               | \$ 4,200                                                |

This loan was classified as a TDR due to permanent reduction in recorded investment. The TDR described above decreased interest income by \$41,000, increased the allowance for loan losses by \$757,000 and resulted in charge offs of \$500,000 during the three months ended March 31, 2011.

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**NOTE 4 LOANS RECEIVABLE (continued)**

A loan is considered to be in payment default once it is 90 days contractually past due under the modified terms.

The terms of certain other loans were modified during the quarter ended March 31, 2012 that did not meet the definition of a TDR. These loans have a total recorded investment as of March 31, 2012 of \$1.7 million. The modification of these loans involved either a modification of the terms of a loan to borrowers who were not experiencing financial difficulties or a delay in a payment that was considered to be insignificant.

In order to determine whether a borrower is experiencing financial difficulty, an evaluation is performed of the probability that the borrower will be in payment default on any of its debt in the foreseeable future without the modification. This evaluation is performed under the Company's internal underwriting policy.

**Credit Quality Indicators**

The Company categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt, including 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 based on credit risk. This analysis includes non-homogeneous loans, such as commercial and commercial real estate loans. This analysis is performed on a monthly basis. The Company uses the following definitions for risk ratings:

**Watch List.** Loans classified as Watch List exhibit transitory risk. Loan debt service coverage is somewhat erratic, future coverage is uncertain, liquidity is strained and leverage capacity is considered minimal. Indicators of potential deterioration of repayment sources have resulted in uncertainty or unknown factors concerning credit status.

**Special Mention.** A Special Mention asset has potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the asset or in the institution's credit position at some future date. Special Mention assets are not adversely classified and do not expose an institution to sufficient risk to warrant adverse classification.

**Substandard.** A Substandard asset is inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. Assets so classified must have a well-defined weakness, or weaknesses, that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the bank will sustain some loss if the deficiencies are not corrected. The risk rating guidance published by the Office of the Comptroller of the Currency clarifies that a loan with a well-defined weakness does not have to present a probability of default for the loan to be rated Substandard, and that an individual loan's loss potential does not have to be distinct for the loan to be rated Substandard.

**Doubtful.** An asset classified doubtful has all the weaknesses inherent in one classified substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable.

Loans not meeting the criteria above that are analyzed individually as part of the above described process are considered Pass rated loans. Watch list loans are also considered Pass rated loans.

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(Table amounts in thousands, except share and per share data)

**NOTE 4 LOANS RECEIVABLE (continued)**

Based on the most recent analysis performed, the risk category of loans by class of loans is as follows:

|                                                                     | Pass       | Watch<br>List | Special<br>Mention | Substandard | Doubtful | Total        |
|---------------------------------------------------------------------|------------|---------------|--------------------|-------------|----------|--------------|
| <b>March 31, 2012</b>                                               |            |               |                    |             |          |              |
| One-to-four family residential real estate loans                    | \$ 172,385 | \$ 2,703      | \$ 531             | \$ 7,462    | \$       | \$ 183,081   |
| One-to-four family residential real estate loans non-owner occupied | 59,259     | 6,474         | 448                | 13,001      |          | 79,182       |
| Multi-family mortgage loans                                         | 290,984    | 25,874        | 6,496              | 21,215      | 715      | 345,284      |
| Wholesale commercial lending                                        | 58,767     | 3,528         |                    | 2,762       |          | 65,057       |
| Nonresidential real estate loans                                    | 212,897    | 20,713        | 21,447             | 53,037      |          | 308,094      |
| Construction loans                                                  | 965        |               | 408                | 834         |          | 2,207        |
| Land loans                                                          | 7,229      | 167           |                    | 9,680       |          | 17,076       |
| Commercial loans:                                                   |            |               |                    |             |          |              |
| Secured                                                             | 22,662     | 1,003         | 399                | 3,705       | 376      | 28,145       |
| Unsecured                                                           | 5,576      | 709           | 80                 | 3,075       | 583      | 10,023       |
| Municipal loans                                                     | 5,846      |               |                    |             |          | 5,846        |
| Warehouse lines                                                     | 9,378      |               |                    |             |          | 9,378        |
| Health care                                                         | 16,929     | 2,456         | 1,272              |             |          | 20,657       |
| Other                                                               | 7,949      |               |                    |             |          | 7,949        |
| Commercial leases:                                                  |            |               |                    |             |          |              |
| Investment rated commercial leases                                  | 78,922     |               |                    |             |          | 78,922       |
| Below investment grade                                              | 7,176      | 118           |                    |             |          | 7,294        |
| Non-rated                                                           | 32,326     | 48            |                    | 22          |          | 32,396       |
| Lease pools                                                         | 5,707      |               |                    |             |          | 5,707        |
| Consumer loans                                                      | 2,203      |               |                    | 8           |          | 2,211        |
| Total                                                               | \$ 997,160 | \$ 63,793     | \$ 31,081          | \$ 114,801  | \$ 1,674 | \$ 1,208,509 |

- (1) The Company has assigned the purchased impaired loans that it acquired in its acquisition of Downers Grove National Bank to the Substandard risk classification category.
- (2) The Dodd-Frank Act abolished the Bank's former primary federal regulator, the Office of Thrift Supervision (OTS), effective on July 21, 2011, and transferred the authority for examining, regulating and supervising federal savings banks from the OTS to the Office of the Comptroller of the Currency (OCC). The OCC's published guidance on the assignment of loan risk ratings is different in some respects from the published guidance of the OTS, particularly as it relates to performing loans with well-defined weaknesses that do not present a probability of default or loss. At March 31, 2012, \$38.6 million of loans that were classified Substandard pursuant to applicable OCC loan risk rating guidance were performing and on accrual status.

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**NOTE 4 LOANS RECEIVABLE (continued)**

|                                                                        | Pass         | Watch<br>List | Special<br>Mention | Substandard | Doubtful | Total        |
|------------------------------------------------------------------------|--------------|---------------|--------------------|-------------|----------|--------------|
| <b>December 31, 2011</b>                                               |              |               |                    |             |          |              |
| One-to-four family residential real estate loans                       | \$ 183,611   | \$ 657        | \$ 51              | \$ 7,108    | \$       | \$ 191,427   |
| One-to-four family residential real estate loans non-owner<br>occupied | 61,455       | 7,058         |                    | 12,092      |          | 80,605       |
| Multi-family mortgage loans                                            | 301,339      | 24,288        | 6,021              | 21,855      | 1,648    | 355,151      |
| Wholesale commercial lending                                           | 64,743       | 959           |                    | 2,762       |          | 68,464       |
| Nonresidential real estate loans                                       | 208,826      | 30,428        | 18,659             | 53,728      |          | 311,641      |
| Construction loans                                                     | 968          |               | 363                | 1,325       |          | 2,656        |
| Land loans                                                             | 7,519        | 143           |                    | 9,534       |          | 17,196       |
| Commercial loans:                                                      |              |               |                    |             |          |              |
| Secured                                                                | 24,152       | 937           | 415                | 4,049       | 464      | 30,017       |
| Unsecured                                                              | 6,436        | 343           | 38                 | 3,010       | 46       | 9,873        |
| Municipal loans                                                        | 6,381        |               |                    |             |          | 6,381        |
| Warehouse lines                                                        | 9,830        |               |                    |             |          | 9,830        |
| Health care                                                            | 27,046       | 1,014         | 1,376              |             |          | 29,436       |
| Other                                                                  | 8,395        |               |                    |             |          | 8,395        |
| Commercial leases:                                                     |              |               |                    |             |          |              |
| Investment rated commercial leases                                     | 83,947       |               |                    |             |          | 83,947       |
| Below investment grade                                                 | 6,004        | 205           |                    |             |          | 6,209        |
| Non-rated                                                              | 36,944       | 82            |                    | 22          |          | 37,048       |
| Lease pools                                                            | 7,786        |               |                    |             |          | 7,786        |
| Consumer loans                                                         | 2,144        |               |                    | 3           |          | 2,147        |
| Total                                                                  | \$ 1,047,526 | \$ 66,114     | \$ 26,923          | \$ 115,488  | \$ 2,158 | \$ 1,258,209 |

- (1) The Company has assigned the purchased impaired loans that it acquired in its acquisition of Downers Grove National Bank to the Substandard risk classification category.
- (1) The Dodd-Frank Act abolished the Bank's former primary federal regulator, the OTS, effective on July 21, 2011, and transferred the authority for examining, regulating and supervising federal savings banks from the OTS to the OCC. The OCC's published guidance on the assignment of loan risk ratings is different in some respects from the published guidance of the OTS, particularly as it relates to performing loans with well-defined weaknesses that do not present a probability of default or loss. At December 31, 2011, \$41.4 million of loans that were classified Substandard pursuant to applicable OCC loan risk rating guidance were performing and on accrual status.

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**NOTE 5 FAIR VALUE**

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.

The Company used the following methods and significant assumptions to estimate the fair value of each type of financial instrument:

**Securities:** The fair values of marketable equity securities are generally determined by quoted prices, in active markets, for each specific security (Level 1). If Level 1 measurement inputs are not available for a marketable equity security, we determine its fair value based on the quoted price of a similar security traded in an active market (Level 2). The fair values of debt securities are generally determined by matrix pricing, which is a mathematical technique widely used in the industry to value debt securities without relying exclusively on quoted prices for the specific securities, but rather by relying on the securities' relationship to other benchmark quoted securities (Level 2).

**Loans Held for Sale:** Loans held for sale are carried at the lower of cost or fair value, which is evaluated on a pool-level basis. The fair value of loans held for sale is determined using quoted prices for similar assets, adjusted for specific attributes of that loan or other observable market data, such as outstanding commitments from third party investors (Level 2).

**Impaired Loans:** At the time a loan is considered impaired, it is valued at the lower of cost or fair value. Impaired loans carried at fair value generally receive specific allocations of the allowance for loan losses. For collateral dependent loans, fair value is commonly based on recent real estate appraisals. These real estate appraisals may include up to three approaches to value: the sales comparison approach, the income approach (for income-producing property) and the cost approach. Adjustments are routinely made in the appraisal process by the independent appraisers to adjust for differences between the comparable sales and income data available, if applicable. Such adjustments may be significant and typically result in a Level 3 classification of the inputs for determining fair value. In addition, a discount is typically applied to account for sales and holding expenses. Non-real estate collateral may be valued using an appraisal, net book value per the borrower's financial statements, or aging reports, adjusted or discounted based on management's historical knowledge, changes in market conditions from the time of the valuation, and management's expertise and knowledge of the client and client's business, resulting in a Level 3 fair value classification. Impaired loans are evaluated on a quarterly basis for additional impairment and adjusted accordingly. The method utilized to estimate the fair value of loans do not necessarily represent an exit price.

**Other Real Estate Owned:** Assets acquired through foreclosure or transfers in lieu of foreclosure are initially recorded at fair value less costs to sell when acquired, establishing a new cost basis. These assets are subsequently accounted for at lower of cost or fair value less estimated costs to sell. Fair value is commonly based on recent real estate appraisals. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the independent appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are usually significant and



typically result in a Level 3 classification of the inputs for determining fair value.

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**NOTE 5 FAIR VALUE (continued)**

**Mortgage Servicing Rights:** On a quarterly basis, loan servicing rights are evaluated for impairment based upon the fair value of the rights as compared to carrying amount. The fair values of mortgage servicing rights are based on a valuation model that calculates the present value of estimated net servicing income. The valuation model incorporates assumptions that market participants would use in estimating future net servicing income. The Company is able to compare the valuation model inputs and results to widely available published industry data for reasonableness (Level 2).

The following table sets forth the Company's financial assets that were accounted for at fair value and are classified in their entirety based on the lowest level of input that is significant to the fair value measurement.

|                                                 | Fair Value Measurements Using                                                          |                                                  |                                                    | Total     |
|-------------------------------------------------|----------------------------------------------------------------------------------------|--------------------------------------------------|----------------------------------------------------|-----------|
|                                                 | Quoted Prices<br>in<br>Active<br>Markets<br>for<br>Identical<br>Assets<br>(Level<br>1) | Significant<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) |           |
| <b>March 31, 2012</b>                           |                                                                                        |                                                  |                                                    |           |
| Securities:                                     |                                                                                        |                                                  |                                                    |           |
| Certificates of deposit                         | \$                                                                                     | \$ 24,401                                        | \$                                                 | \$ 24,401 |
| Municipal securities                            |                                                                                        | 547                                              |                                                    | 547       |
| Equity mutual fund                              | 523                                                                                    |                                                  |                                                    | 523       |
| Mortgage-backed securities residential          |                                                                                        | 34,898                                           |                                                    | 34,898    |
| Collateralized mortgage obligations residential |                                                                                        | 20,826                                           |                                                    | 20,826    |
| SBA-guaranteed loan participation certificates  |                                                                                        | 46                                               |                                                    | 46        |
|                                                 | \$ 523                                                                                 | \$ 80,718                                        | \$                                                 | \$ 81,241 |
| <b>December 31, 2011</b>                        |                                                                                        |                                                  |                                                    |           |
| Securities:                                     |                                                                                        |                                                  |                                                    |           |
| Certificates of deposit                         | \$                                                                                     | \$ 30,448                                        | \$                                                 | \$ 30,448 |
| Municipal securities                            |                                                                                        | 551                                              |                                                    | 551       |
| Equity mutual fund                              | 524                                                                                    |                                                  |                                                    | 524       |
| Mortgage-backed securities residential          |                                                                                        | 36,076                                           |                                                    | 36,076    |
| Collateralized mortgage obligations residential |                                                                                        | 25,186                                           |                                                    | 25,186    |
| SBA-guaranteed loan participation certificates  |                                                                                        | 47                                               |                                                    | 47        |
|                                                 | \$ 524                                                                                 | \$ 92,308                                        | \$                                                 | \$ 92,832 |



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**NOTE 5 FAIR VALUE (continued)**

The following table sets forth the Company's assets that were measured at fair value on a non-recurring basis:

|                                                  | Fair Value Measurement Using                                                           |                                                  |                                                    | Total     |
|--------------------------------------------------|----------------------------------------------------------------------------------------|--------------------------------------------------|----------------------------------------------------|-----------|
|                                                  | Quoted Prices<br>in<br>Active<br>Markets<br>for<br>Identical<br>Assets<br>(Level<br>1) | Significant<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) |           |
| <b>March 31, 2012</b>                            |                                                                                        |                                                  |                                                    |           |
| Impaired loans:                                  |                                                                                        |                                                  |                                                    |           |
| One to four family residential real estate loans | \$                                                                                     | \$                                               | \$ 3,646                                           | \$ 3,646  |
| Multi-family mortgage loans                      |                                                                                        |                                                  | 5,597                                              | 5,597     |
| Nonresidential real estate loans                 |                                                                                        |                                                  | 20,002                                             | 20,002    |
| Construction and land loans                      |                                                                                        |                                                  | 2,245                                              | 2,245     |
| Commercial loans                                 |                                                                                        |                                                  | 847                                                | 847       |
| Impaired loans                                   | \$                                                                                     | \$                                               | \$ 32,337                                          | \$ 32,337 |
| Other real estate owned:                         |                                                                                        |                                                  |                                                    |           |
| One to four family residential real estate       | \$                                                                                     | \$                                               | \$ 4,972                                           | \$ 4,972  |
| Multi-family mortgage                            |                                                                                        |                                                  | 3,005                                              | 3,005     |
| Nonresidential real estate                       |                                                                                        |                                                  | 7,020                                              | 7,020     |
| Land                                             |                                                                                        |                                                  | 5,192                                              | 5,192     |
| Other real estate owned                          | \$                                                                                     | \$                                               | \$ 20,189                                          | \$ 20,189 |
| Mortgage servicing rights                        | \$                                                                                     | \$ 311                                           | \$                                                 | \$ 311    |
| <b>December 31, 2011</b>                         |                                                                                        |                                                  |                                                    |           |
| Impaired loans:                                  |                                                                                        |                                                  |                                                    |           |
| One to four family residential real estate loans | \$                                                                                     | \$                                               | \$ 4,024                                           | \$ 4,024  |
| Multi-family mortgage loans                      |                                                                                        |                                                  | 6,285                                              | 6,285     |
| Nonresidential real estate loans                 |                                                                                        |                                                  | 17,239                                             | 17,239    |
| Construction and land loans                      |                                                                                        |                                                  | 2,304                                              | 2,304     |
| Commercial loans                                 |                                                                                        |                                                  | 844                                                | 844       |
| Impaired loans                                   | \$                                                                                     | \$                                               | \$ 30,696                                          | \$ 30,696 |

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Other real estate owned:

|                                            |           |           |           |               |                  |
|--------------------------------------------|-----------|-----------|-----------|---------------|------------------|
| One to four family residential real estate | \$        | \$        | \$        | 5,655         | \$ 5,655         |
| Multi-family mortgage                      |           |           |           | 3,655         | 3,655            |
| Nonresidential real estate                 |           |           |           | 7,451         | 7,451            |
| Land                                       |           |           |           | 5,719         | 5,719            |
| <b>Other real estate owned</b>             | <b>\$</b> | <b>\$</b> | <b>\$</b> | <b>22,480</b> | <b>\$ 22,480</b> |
| <br>Mortgage servicing rights              | <br>\$    | <br>\$    | <br>344   | <br>\$        | <br>\$ 344       |

Impaired loans, excluding purchased impaired loans, that are measured for impairment using the fair value of the collateral for collateral-dependent loans, had a carrying amount of \$74.2 million, with a valuation allowance of \$14.6 million at March 31, 2012, compared to a carrying amount of \$73.7 million, with a valuation allowance of \$15.0 million at December 31, 2011, resulting in a decrease in the provision for loan losses for these impaired loans of \$398,000 for the quarter ended March 31, 2012.

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(Table amounts in thousands, except share and per share data)

**NOTE 5 FAIR VALUE (continued)**

Other real estate owned ( OREO ), which is carried at the lower of cost or fair value less costs to sell, had a carrying value of \$20.2 million at March 31, 2012, which included write-downs of \$389,000 for the quarter ended March 31, 2012, compared to \$22.5 million at December 31, 2011, which included write-downs of \$4.0 million for the year ended December 31, 2011.

Mortgage servicing rights, which are carried at lower of cost or fair value, had a carrying amount of \$1.2 million at March 31, 2012, of which \$877,000 related to fixed rate loans and \$296,000 related to adjustable rate loans. Mortgage servicing rights had a carrying amount of \$1.2 million at December 31, 2011, of which \$895,000 related to fixed rate loans and \$309,000 related to adjustable rate loans. A pre tax provision of \$13,000 on our mortgage servicing rights portfolio was included in noninterest income for the quarter ended March 31 2012, compared to no provision for or recovery of mortgage servicing rights for the same period in 2011.

The following table presents quantitative information, based on certain empirical data with respect to level 3 fair value measurements for financial instruments measured at fair value on a non-recurring basis at March 31, 2012:

|                                                  | Fair Value       | Valuation Technique(s) | Unobservable Input(s)                          | Range (Weighted Average) |
|--------------------------------------------------|------------------|------------------------|------------------------------------------------|--------------------------|
| <b>Impaired loans:</b>                           |                  |                        |                                                |                          |
| One to four family residential real estate loans |                  |                        | Discount applied to valuation                  | 0%-25%<br>(7.47%)        |
| Multi-family mortgage loans                      | \$ 3,646         | Sales comparison       | Comparison between sales and income approaches | 5% to 21%<br>(11.11%)    |
|                                                  | 5,597            | Sales comparison       |                                                | 6.2% to 15.5%            |
|                                                  |                  | Income approach        | Cap Rate                                       | (10.88%)                 |
| Nonresidential real estate loans                 |                  |                        | Comparison between sales and income approaches | 0% to 26%<br>(4.66%)     |
|                                                  | 20,002           | Sales comparison       |                                                | 7.3% to 9.5%             |
|                                                  |                  | Income approach        | Cap Rate                                       | (8.60%)                  |
| Construction and land loans                      |                  |                        | Discount applied to valuation                  | 10% to 100%<br>(30.97%)  |
|                                                  | 2,245            | Sales comparison       |                                                | 0% to 30%                |
| Commercial loans                                 |                  |                        | Discount applied to valuation                  | (28.75%)                 |
|                                                  | 847              | Sales comparison       |                                                |                          |
| <b>Impaired loans</b>                            | <b>\$ 32,337</b> |                        |                                                |                          |

Other real estate owned:

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|                                            |           |                  |                                                |               |
|--------------------------------------------|-----------|------------------|------------------------------------------------|---------------|
| One to four family residential real estate |           |                  |                                                | 0% to 59%     |
|                                            | \$ 4,972  | Sales comparison | Discount applied to valuation                  | (14.98%)      |
| Multi-family mortgage                      |           |                  | Comparison between sales and income approaches | -8 to 5%      |
|                                            | 3,005     | Sales comparison |                                                | (0%)          |
|                                            |           | Income approach  | Cap Rate                                       | 9% to 9.5%    |
| Nonresidential real estate                 |           |                  |                                                | (9.36%)       |
|                                            | 7,020     | Sales comparison | Comparison between sales and income approaches | 0% to 26%     |
|                                            |           |                  |                                                | (4.66%)       |
|                                            |           | Income approach  | Cap Rate                                       | 8.5% to 12.5% |
| Land                                       |           |                  |                                                | (9.33%)       |
|                                            | 5,192     | Sales comparison | Discount applied to valuation                  | 1% to 49%     |
|                                            |           |                  |                                                | (18.83%)      |
| Other real estate owned                    | \$ 20,189 |                  |                                                |               |

**Table of Contents****BANKFINANCIAL CORPORATION****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

(Table amounts in thousands, except share and per share data)

**NOTE 5 FAIR VALUE (continued)**

The carrying amount and estimated fair value of financial instruments is as follows:

|                                                    | Carrying Amount | Fair Value Measurements at March 31, 2012 Using: |              |         | Total        |
|----------------------------------------------------|-----------------|--------------------------------------------------|--------------|---------|--------------|
|                                                    |                 | Level 1                                          | Level 2      | Level 3 |              |
| <b>Financial assets</b>                            |                 |                                                  |              |         |              |
| Cash and cash equivalents                          | \$ 178,080      | \$ 24,037                                        | \$ 154,043   | \$      | \$ 178,080   |
| Securities                                         | 81,241          | 523                                              | 80,718       |         | 81,241       |
| Loans held-for-sale                                | 521             |                                                  | 521          |         | 521          |
| Loans receivable, net of allowance for loan losses | 1,177,719       |                                                  | 1,094,781    | 32,337  | 1,127,118    |
| FHLBC stock                                        | 11,336          |                                                  |              |         | N/A          |
| Accrued interest receivable                        | 4,911           |                                                  | 4,911        |         | 4,911        |
| <b>Financial liabilities</b>                       |                 |                                                  |              |         |              |
| Noninterest-bearing demand deposits                | \$ (144,182)    | \$                                               | \$ (144,182) | \$      | \$ (144,182) |
| Savings deposits                                   | (147,706)       |                                                  | (147,706)    |         | (147,706)    |
| NOW and money market accounts                      | (682,095)       |                                                  | (682,095)    |         | (682,095)    |
| Certificates of deposit                            | (346,597)       |                                                  | (349,209)    |         | (349,209)    |
| Borrowings                                         | (9,995)         |                                                  | (10,054)     |         | (10,054)     |
| Accrued interest payable                           | (189)           |                                                  | (189)        |         | (189)        |

|                                                    | December 31, 2011 |                      |
|----------------------------------------------------|-------------------|----------------------|
|                                                    | Carrying Amount   | Estimated Fair Value |
| <b>Financial assets</b>                            |                   |                      |
| Cash and cash equivalents                          | \$ 120,704        | \$ 120,704           |
| Securities                                         | 92,832            | 92,832               |
| Loans held-for-sale                                | 1,918             | 1,918                |
| Loans receivable, net of allowance for loan losses | 1,227,391         | 1,217,377            |
| FHLBC stock                                        | 16,346            | N/A                  |
| Accrued interest receivable                        | 5,573             | 5,573                |
| <b>Financial liabilities</b>                       |                   |                      |
| Noninterest-bearing demand deposits                | \$ (142,084)      | \$ (142,084)         |
| Savings deposits                                   | (144,515)         | (144,515)            |
| NOW and money market accounts                      | (681,542)         | (681,542)            |
| Certificates of deposit                            | (364,411)         | (365,952)            |
| Borrowings                                         | (9,322)           | (9,412)              |
| Accrued interest payable                           | (212)             | (212)                |

For purposes of the above, the following assumptions were used:

**Cash and Cash Equivalents:** The estimated fair values for cash and cash equivalents are based on their carrying value due to the short-term nature of these assets.



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**Loans:** The estimated fair value for loans has been determined by calculating the present value of future cash flows based on the current rate the Company would charge for similar loans with similar maturities, applied for an estimated time period until the loan is assumed to be re-priced or repaid. The estimated fair values of loans held-for-sale are based on quoted market prices.

**FHLBC Stock:** It is not practicable to determine the fair value of Federal Home Loan Bank of Chicago ( FHLBC ) stock due to the restrictions placed on its transferability.

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**BANKFINANCIAL CORPORATION**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

(Table amounts in thousands, except share and per share data)

**NOTE 5 FAIR VALUE (continued)**

**Deposit Liabilities:** The estimated fair value for certificates of deposit has been determined by calculating the present value of future cash flows based on estimates of rates the Company would pay on such deposits, applied for the time period until maturity. The estimated fair values of noninterest-bearing demand, NOW, money market, and savings deposits are assumed to approximate their carrying values as management establishes rates on these deposits at a level that approximates the local market area. Additionally, these deposits can be withdrawn on demand.

**Borrowings:** The estimated fair values of advances from the FHLBC and notes payable are based on current market rates for similar financing. The estimated fair value of securities sold under agreements to repurchase is assumed to equal its carrying value due to the short-term nature of the liability.

**Accrued Interest:** The estimated fair values of accrued interest receivable and payable are assumed to equal their carrying value.

**Off-Balance-Sheet Instruments:** Off-balance-sheet items consist principally of unfunded loan commitments, standby letters of credit, and unused lines of credit. The estimated fair values of unfunded loan commitments, standby letters of credit, and unused lines of credit are not material.

While the above estimates are based on management's judgment of the most appropriate factors, as of the balance sheet date, there is no assurance that the estimated fair values would have been realized if the assets were disposed of or the liabilities settled at that date, since market values may differ depending on the various circumstances. The estimated fair values would also not apply to subsequent dates.

In addition, other assets and liabilities that are not financial instruments, such as premises and equipment, are not included in the above disclosures.

**NOTE 6 RECENT ACCOUNTING PRONOUNCEMENTS**

In May 2011, the FASB issued an accounting standards update to improve the comparability between U.S. GAAP fair value accounting and reporting requirements and International Financial Reporting Standards (IFRS) fair value accounting and reporting requirements. Additional disclosures required by the update include: (1) disclosure of quantitative information regarding the unobservable inputs used in any fair value measurement classified as Level 3 in the fair value hierarchy in addition to an explanation of the valuation techniques used in valuing Level 3 items and information regarding the sensitivity in the valuation of Level 3 items to changes in the values assigned to unobservable inputs; (2) categorization by level within the fair value hierarchy of items not recognized on the Statement of Financial Position at fair value but for which fair values are required to be disclosed; and (3) instances where the fair values disclosed for non-financial assets were based on a highest and best use assumption when in fact the assets are not being utilized in that capacity. The amendments in the update are effective for interim and annual periods beginning on or after December 15, 2011. The provisions of this update did not have a material impact on the Company's financial position, results or operations or cash flows. See Note 5 to these Consolidated Financial Statements for the required disclosures.

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**BANKFINANCIAL CORPORATION**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

(Table amounts in thousands, except share and per share data)

**NOTE 6 RECENT ACCOUNTING PRONOUNCEMENTS (continued)**

In June 2011, the FASB issued an accounting standards update to increase the prominence of items included in Other Comprehensive Income and facilitate the convergence of U.S. GAAP with IFRS. The update prohibits continued exclusive presentation of Other Comprehensive Income in the statement of stockholders' equity. The update requires that all non-owner changes in stockholders' equity be presented in either a single continuous statement of comprehensive income or in two separate but continuous statements. The amendments in the update are effective for interim and annual periods beginning on or after December 15, 2011. The provisions of this update only changed the manner in which our Other Comprehensive Income was disclosed.

**NOTE 7 NEWLY ISSUED BUT NOT YET EFFECTIVE ACCOUNTING PRONOUNCEMENTS**

In December 2011, the FASB issued an accounting standards update to increase the disclosure requirements surrounding derivative instruments that are offset within the balance sheet pursuant to the provisions of current GAAP. The objective of the update is to provide greater comparability between issuers reporting under U.S. GAAP versus IFRS and provide users the ability to evaluate the effect of netting arrangements on a company's financial statements. The provisions of the update are effective for annual and interim periods beginning on or after January 1, 2013 and are not expected to add to the Company's current level of disclosures.

**Table of Contents****ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS****Cautionary Statement Regarding Forward-Looking Information****Forward Looking Statements**

This Quarterly Report on Form 10-Q contains, and other periodic and current reports, press releases and other public stockholder communications of BankFinancial Corporation may contain, forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, that involve significant risks and uncertainties. Forward-looking statements may include statements relating to our future plans, strategies and expectations, as well as our future revenues, earnings, losses, financial performance, financial condition, asset quality metrics and future prospects. Forward looking statements are generally identifiable by use of the words believe, may, will, should, could, expect, estimate, intend, anticipate, project, plan, or similar expressions. Forward looking statements speak only as of the date made. They are frequently based on assumptions that may or may not materialize, and are subject to numerous uncertainties that could cause actual results to differ materially from those anticipated in the forward looking statements. We intend all forward-looking statements to be covered by the safe harbor provisions for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995, and are including this statement for the purpose of invoking these safe harbor provisions.

Factors that could cause actual results to differ materially from the results anticipated or projected and which could materially and adversely affect our operating results, financial condition or future prospects include, but are not limited to: (i) the failure of the real estate market to recover or further declines in real estate values that adversely impact the value of our loan collateral and OREO, asset dispositions and borrower equity in their investments; (ii) the persistence or worsening of adverse economic conditions in general and in the Chicago metropolitan area in particular, including high or increasing unemployment levels, that could result in increased delinquencies in our loan portfolio or a decline in the value of our investment securities and the collateral for our loans; (iii) results of supervisory monitoring or examinations by regulatory authorities, including the possibility that a regulatory authority could, among other things, require us to increase our loan classifications or allowance for loan losses, write-down assets, reduce credit concentrations or maintain specific capital levels; (iv) interest rate movements and their impact on customer behavior and our net interest margin; (v) less than anticipated loan growth due to a lack of demand for specific loan products, competitive pressures or a dearth of borrowers who meet our underwriting standards; (vi) changes, disruptions or illiquidity in national or global financial markets; (vii) the credit risks of lending activities, including risks that could cause changes in the level and direction of loan delinquencies and charge-offs or changes in estimates relating to the computation of our allowance for loan losses; (viii) monetary and fiscal policies of the U.S. Government, including policies of the U.S. Treasury and Federal Reserve Board; (ix) factors affecting our ability to access deposits or cost-effective funding, and the impact of competitors' pricing initiatives on our deposit products; (x) the impact of new legislation or regulatory changes, including the Dodd-Frank Act, on our products, services, operations and operating expenses; (xi) higher federal deposit insurance premiums; (xii) higher than expected overhead, infrastructure and compliance costs; (xiii) changes in accounting principles, policies or guidelines; and (xiv) our failure to achieve expected synergies and cost savings from acquisitions.

These risks and uncertainties, as well as the Risk Factors set forth in Item 1A below, should be considered in evaluating forward-looking statements and undue reliance should not be placed on such statements. We do not undertake any obligation to update any forward-looking statement in the future, or to reflect circumstances and events that occur after the date on which the forward-looking statement was made.

**Critical Accounting Policies**

Critical accounting policies are defined as those that are reflective of significant judgments and uncertainties, and could potentially result in materially different results under different assumptions and conditions. We believe that the most critical accounting policies upon which our financial condition and results of operation depend, and which involve the most complex subjective decisions or assessments, are included in the discussion entitled "Critical Accounting Policies" in Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations," in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2011, and all amendments thereto, as filed with the Securities and Exchange Commission. There are no material changes to the critical accounting policies disclosed in the Annual Report on Form 10-K.

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### **Overview**

During the first quarter of 2012, the national and local economies showed limited signs of recovery. The principal challenges in the local economy continue to be persistent unemployment and uneven economic growth. Pricing and underwriting competition for multi-family and commercial real estate loans increased during the quarter. Competition for commercial and industrial loans remained intense in terms of both pricing and underwriting.

Loan portfolio balances declined in all categories except consumer loans. Residential loan balances continued to decline due to scheduled loan amortizations and loan prepayments. Multifamily loan balances and commercial real estate loan balances declined due to slightly lower loan origination volumes and certain targeted portfolio reductions; however, we believe that these portfolios are at or near a stabilized level. Commercial and industrial balances declined primarily because our largest healthcare borrower refinanced its loan at another institution. The refinancing occurred because the borrower's credit needs exceeded our regulatory loan-to-one-borrower limits and the borrower was unwilling to proceed with a loan participation arrangement. We expect modest growth in our commercial and industrial loan portfolio going forward. Although commercial lease origination volumes remained consistent in the first quarter of 2012, commercial lease balances declined due to unusually high volumes of scheduled lease repayments, which are expected to abate in future periods. Our focus for the remainder of 2012 will be to maintain current overall loan portfolio levels and to increase certain selected loan categories such as residential loans, commercial loans and commercial leases consistent with market opportunities.

Loan portfolio quality was stable to trending positive as the first quarter, 2012 ended. We negotiated several final consensual non-performing loan resolutions during the first quarter, 2012 that we expect will result in further improvements in our asset quality metrics in the second and third quarters, 2012. We believe that unemployment, consumer spending, borrower and investor perceptions of residential and commercial real estate valuations and the pace of judicial proceedings will continue to be the primary factors affecting our asset quality metrics and the pace of classified asset resolutions in 2012.

We continued to experience increasing purchaser interest in our classified asset collateral and OREO inventory, and the quantity of OREO under contract for sale on an orderly liquidation basis increased in the first quarter, 2012. We expect to continue accelerating the resolution of non-performing assets throughout the remainder of 2012.

Our general loan loss reserve requirement remained stable in the first quarter of 2012 due principally to a reduction of loan portfolio balances. Specific loan loss reserves were stable. Our underwriting standards remain consistent with historical standards, although our credit analyses continue to incorporate somewhat more conservative assumptions with respect to effective rents, expenses and occupancy levels given the current economic environment.

Given our excess liquidity position, we reduced our competitive posture with respect to pricing on single-service certificate of deposit accounts, which was successful in producing a decline in these account balances. Pricing conditions for local deposits, whether low-balance core deposits, certificates of deposit or high-balance, high-yield transaction accounts, remained generally favorable due to very low market yields and continued weak industry-wide loan demand. In addition, many competitors are still evaluating their deposit product configurations in the context of the Dodd-Frank Act and its related regulations; we expect we will adjust our deposit product offerings to explore such competitive advantages as may emerge in this new regulatory and competitive environment.

The Company's net interest spread and net interest margin were stable but we anticipate that current market conditions for new loans and lower effective yields resulting from scheduled loan repayments and loan renewals will likely cause some compression of our net interest margin and net interest spread. Given the quantity and volatility of the variables affecting our net interest margin and net interest spread, we are unable to confidently predict what the Company's net interest margin and net interest spread will be for the remainder of 2012.

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Non-interest income was lower in the first quarter of 2012 primarily due to lower deposit related fees. We continue to evaluate the expansion of non-interest income sources, particularly related to insurance and trust services, to offset any potential future adverse impact associated with the Dodd-Frank Act.

Non-interest expense was lower due to lower non-performing asset expenses, offset by slightly higher compensation expenses related to seasonal factors. We will continue our review of certain departments and operations for net operating contributions and further operating efficiencies throughout the remainder of 2012.

**Selected Financial Data**

The following tables summarize the major components of the changes in our balance sheet at March 31, 2012 and December 31, 2011, and in our statement of operations for the three-month periods ended March 31, 2012 and March 31, 2011.

|                                           | March 31,<br>2012      | December 31,<br>2011 | Change      |
|-------------------------------------------|------------------------|----------------------|-------------|
|                                           | (Dollars in thousands) |                      |             |
| <b>Selected Financial Condition Data:</b> |                        |                      |             |
| Total assets                              | \$ 1,549,137           | \$ 1,563,575         | \$ (14,438) |
| Cash and cash equivalents                 | 178,080                | 120,704              | 57,376      |
| Securities                                | 81,241                 | 92,832               | (11,591)    |
| Loans receivable, net                     | 1,177,719              | 1,227,391            | (49,672)    |
| Deposits                                  | 1,320,580              | 1,332,552            | (11,972)    |
| Borrowings                                | 9,995                  | 9,322                | 673         |
| Stockholders' equity                      | 202,111                | 199,857              | 2,254       |

|                                                     | Three months ended March 31,<br>2012 | 2011      | Change   |
|-----------------------------------------------------|--------------------------------------|-----------|----------|
|                                                     | (Dollars in thousands)               |           |          |
| <b>Selected Operating Data:</b>                     |                                      |           |          |
| Interest income                                     | \$ 16,634                            | \$ 15,348 | \$ 1,286 |
| Interest expense                                    | 1,240                                | 1,996     | (756)    |
| Net interest income                                 | 15,394                               | 13,352    | 2,042    |
| Provision for loan losses                           | 996                                  | 2,424     | (1,428)  |
| Net interest income after provision for loan losses | 14,398                               | 10,928    | 3,470    |
| Noninterest income                                  | 1,832                                | 1,571     | 261      |
| Noninterest expense                                 | 13,436                               | 14,255    | (819)    |
| Income (loss) before income taxes                   | 2,794                                | (1,756)   | 4,550    |
| Income tax expense (benefit)                        | 457                                  | (979)     | 1,436    |
| Net income (loss)                                   | \$ 2,337                             | \$ (777)  | \$ 3,114 |

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|                                                                           | <b>Three Months Ended March 31,</b> |             |
|---------------------------------------------------------------------------|-------------------------------------|-------------|
|                                                                           | <b>2012</b>                         | <b>2011</b> |
| <b>Performance Ratios:</b>                                                |                                     |             |
| Return on assets (ratio of net income (loss) to average total assets) (1) | 0.61%                               | (0.20)%     |
| Return on equity (ratio of net income (loss) to average equity) (1)       | 4.61                                | (1.23)      |
| Net interest rate spread (1) (2)                                          | 4.18                                | 3.68        |
| Net interest margin (1) (3)                                               | 4.26                                | 3.81        |
| Average equity to average assets                                          | 13.16                               | 16.48       |
| Efficiency ratio (4)                                                      | 78.00                               | 95.52       |
| Noninterest expense to average total assets (1)                           | 3.49                                | 3.71        |
| Average interest-earning assets to average interest-bearing liabilities   | 122.46                              | 122.64      |

- (1) Ratios are annualized.  
(2) The net interest rate spread represents the difference between the yield on average interest-earning assets and the cost of average interest-bearing liabilities for the period.  
(3) The net interest margin represents net interest income divided by average total interest-earning assets for the period.  
(4) The efficiency ratio represents noninterest expense divided by the sum of net interest income and noninterest income.

|                                                  | <b>At March 31,</b> | <b>At December 31,</b> |
|--------------------------------------------------|---------------------|------------------------|
|                                                  | <b>2012</b>         | <b>2011</b>            |
| <b>Selected Financial Ratios and Other Data:</b> |                     |                        |
| <b>Asset Quality Ratios:</b>                     |                     |                        |
| Nonperforming assets to total assets             | 6.38%               | 6.36%                  |
| Nonaccrual loans to total loans                  | 6.51                | 6.11                   |
| Allowance for loan losses to nonperforming loans | 40.20               | 41.25                  |
| Allowance for loan losses to total loans         | 2.62                | 2.52                   |
| <b>Capital Ratios:</b>                           |                     |                        |
| Equity to total assets at end of period          | 13.05               | 12.78                  |
| Tier 1 leverage ratio (Bank only)                | 10.98               | 10.50                  |
| <b>Other Data:</b>                               |                     |                        |
| Number of full service offices                   | 20                  | 20                     |
| Employees (full-time equivalent basis)           | 353                 | 357                    |

**Statement of Financial Condition at March 31, 2012 and December 31, 2011**

Total assets decreased \$14.4 million, or 0.9%, to \$1.549 billion at March 31, 2012, from \$1.564 billion at December 31, 2011. The decrease in total assets was primarily due to the decrease in net loans of \$49.7 million, or 4.0%, to 1.178 billion at March 31, 2012, from \$1.227 billion at December 31, 2011. Securities decreased \$11.6 million, or 12.5%, to \$81.2 million at March 31, 2012, from \$92.8 million at December 31, 2011. These decreases were partially offset by an increase of \$57.4 million, or 47.5%, in net cash and cash equivalents to \$178.1 million at March 31, 2012, from \$120.7 million at December 31, 2011.

Our loan portfolio consists primarily of investment and business loans (multi-family, nonresidential real estate, commercial, construction and land loans, and commercial leases), which together made up 78.1% of gross loans at March 31, 2012. Net loans receivable decreased \$49.7 million, or 4.0%, to \$1.178 billion at March 31, 2012, from \$1.227 billion at December 31, 2011. Significant loan repayments of \$156.7 million received in the first quarter affected all loan portfolios. Multi-family mortgage loans decreased by \$13.3 million, or 3.1%. Commercial loans decreased by \$11.9 million, or 12.7%, and commercial leases decreased by \$10.7 million, or 7.9%, as scheduled lease payments outpaced originations.





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Our allowance for loan losses decreased by \$88,000, or 0.3%, to \$31.6 million at March 31, 2012, from \$31.7 million at December 31, 2011. The decrease reflects the combined impact of a \$61,000 decrease in the portion of the specific allowance for loan losses that we allocate to impaired loans and a credit of \$27,000 to the general component of the allowance for loan losses.

Securities decreased \$11.6 million, or 12.5%, to \$81.2 million at March 31, 2012, from \$92.8 million at December 31, 2011, due primarily to the receipt of principal repayments of \$6.2 million in our residential mortgage-backed and collateralized mortgage obligation portfolio, combined with \$6.5 million in maturities of certificates of deposit held in our investment portfolio.

Other real estate owned decreased \$2.3 million to \$20.2 million at March 31, 2012, from \$22.5 million at December 31, 2011. The decrease was primarily due to the completion of \$2.8 million in sales in the first quarter, which was partially offset by the addition of \$1.1 million of foreclosed real estate collateral to other real estate owned.

We owned \$11.3 million of common stock of the Federal Home Loan Bank of Chicago ( FHLBC ) at March 31, 2012, compared to \$16.4 million at December 31, 2011. The decrease resulted from the FHLBC's redemption of \$5.1 million of our excess FHLBC stock at par value during the first quarter. During 2012 and 2011, the FHLBC declared and paid a cash dividend at an annualized rate of 10 basis points per share.

Deposits decreased \$12.0 million, or 0.9%, to \$1.321 billion at March 31, 2012, from \$1.333 billion at December 31, 2011. We managed our deposit portfolio, including the deposits acquired in the Downers Grove National Bank transaction, to retain the highest value core deposit relationships, eliminate unneeded single service certificate of deposit relationships, and reduce our cost of funds to the lowest practicable levels. In doing so, certificates of deposit decreased \$17.8 million, or 4.7%, to \$346.6 million at March 31, 2012, from \$364.4 million at December 31, 2011. We also increased our core deposits (savings, money market, noninterest-bearing demand and NOW accounts) by \$5.8 million, or 0.7%, bringing core deposits as a percentage of total deposits, representing 73.8% of total deposits at March 31, 2012, compared to 72.7% of total deposits at December 31, 2011.

Borrowings increased \$673,000, or 7.2%, to \$10.0 million at March 31, 2012, from \$9.3 million at December 31, 2011, primarily due to fluctuations in the balances of securities sold under agreements to repurchase.

Total stockholders' equity was \$202.1 million at March 31, 2012, compared to \$199.9 million at December 31, 2011. The increase in total stockholders' equity was primarily due to the combined impact of our net income of \$2.3 million, offset by our declaration of cash dividends totaling \$211,000, and a \$55,000 decrease in accumulated other comprehensive income during the quarter ended March 31, 2012. The unallocated shares of common stock that our ESOP owns were reflected as a \$13.0 million reduction to stockholders' equity at March 31, 2012, compared to a \$13.2 million reduction to stockholders' equity at December 31, 2011.

**Comparison of Operating Results for the Three Months Ended March 31, 2012 and 2011**

**Net Income (Loss).** We had net income of \$2.3 million for the three months ended March 31, 2012, compared to a net loss of \$777,000 for the three months ended March 31, 2011, due in substantial part to increased net interest income, lower provisions for loan losses and lower noninterest expense. Our income per share of common stock for the three months ended March 31, 2012 was \$0.12 per basic and fully diluted share, respectively, compared to a loss of \$0.04 per basic and fully diluted share, respectively, for the three months ended March 31, 2011.

**Net Interest Income.** Net interest income increased by \$2.0 million, or 15.3%, to \$15.4 million for the three months ended March 31, 2012, from \$13.4 million for the three months ended March 31, 2011. Our net interest rate spread increased 50 basis points to 4.18% for the three months ended March 31, 2012, compared to 3.68% for the three months ended March 31, 2011. Our net interest margin increased by 45 basis points to 4.26% for the three months ended March 31, 2012, from 3.81% for the three months ended March 31, 2011. Our average interest-earning assets increased \$34.4 million to \$1.454 billion for the three months ended March 31, 2012, from \$1.420 billion for the three months ended March 31, 2011, and our average interest-bearing liabilities increased \$29.8 million to \$1.187 billion for the three months ended March 31, 2012, from \$1.158 billion for the three months ended March 31, 2011. The increases in the average interest-earning assets and average interest-bearing liabilities were impacted by our acquisition in March 2011 of Downers Grove National Bank and a portfolio of performing Chicago area multi-family loans from Citibank.

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Interest income increased \$1.3 million, or 8.4%, to \$16.6 million for the three months ended March 31, 2012, from \$15.3 million for the three months ended March 31, 2011. The average yield on interest-earning assets increased 22 basis points to 4.60% for the three months ended March 31, 2012, compared to 4.38% for the same period in 2011. Total average interest-earning assets increased \$34.4 million, or 2.4%, to \$1.454 billion for the three months ended March 31, 2012, from \$1.420 billion for the same period in 2011. The increase in average interest-earning assets was due in substantial part to a \$118.0 million, or 10.6%, increase in average loans receivable, partially offset by a net decrease of \$30.5 million, or 25.6%, in the average balance of securities, and a net decrease of \$51.2 million, or 30.7%, in the average balance of interest-bearing deposits maintained at other insured depository institutions.

Interest income from loans, the most significant portion of interest income, increased \$1.7 million, or 11.8%, to \$16.1 million for the three months ended March 31, 2012, from \$14.4 million for the same period in 2011. The increase in interest income from loans was significantly impacted by the \$118.1 million of loans that we acquired in the Downers Grove National Bank transaction and our purchase of \$152.1 million of performing Chicago area multi-family loans. Average loans receivable increased to \$1.236 billion for the three months ended March 31, 2012, from \$1.118 billion for the same period in 2011. The average yield on loans increased one basis point to 5.24% for the three months ended March 31, 2012, compared to 5.23% for the same period in 2011.

Interest income from securities decreased by \$380,000, or 46.2%, to \$442,000 for the three months ended March 31, 2012, from \$822,000 for the same period in 2011. The decrease in interest income from securities was primarily due to a 79 basis point decrease in the average yield on securities to 2.01% for the three months ended March 31, 2012, from 2.80% for the same period in 2011. The average outstanding balance of securities also decreased for the three month period ended March 31, 2012 to \$88.4 million, from \$118.9 million, for the three months ended March 31, 2011.

Interest income on interest-bearing deposits maintained at other insured depository institutions decreased by \$37,000, or 32.7%, to \$76,000 for the three months ended March 31, 2012, from \$113,000 for the same period in 2011. The decrease in interest income from interest-bearing deposits was primarily due to a decrease of \$51.2 million, or 30.7%, in the average outstanding balance of interest-bearing deposits to \$115.6 million for the three months ended March 31, 2012, from \$166.8 million for the same period in 2011 and a one basis point increase in the average yield on interest-bearing deposits to 0.26% for the three months ended March 31, 2012 from 0.27% for the same period in 2011.

Interest expense decreased \$756,000, or 37.9%, to \$1.2 million for the three months ended March 31, 2012, from \$2.0 million for the three months ended March 31, 2011, reflecting a decrease in both interest expense on deposits and interest expense on borrowings.

Interest expense on deposits decreased by \$686,000, or 36.1%, to \$1.2 million for the three months ended March 31, 2012, from \$1.9 million for the three months ended March 31, 2011. The decrease in interest expense on deposits was primarily due to a 27 basis point decrease in the weighted average interest rates paid on deposit accounts, which was partially offset by a \$38.6 million, or 3.4%, increase in average balance of interest-bearing deposits.

The average cost of deposits was 0.41% for the three months ended March 31, 2012, compared to 0.68% for the same period in 2011. The average rate paid on savings accounts decreased 15 basis points to 0.10% from 0.25%. On a year over year basis, the average cost of money market accounts decreased 15 basis points to 0.37%, from 0.52%, the average cost of NOW accounts decreased eight basis points to 0.12%, from 0.20%, and the average cost of certificates of deposit decreased 45 basis points to 0.86% from 1.31%. The average balance of savings accounts increased \$37.9 million, or 35.2%, the average balance of NOW accounts increased \$28.0 million, or 9.2%, and the average balance of money market accounts increased \$2.2 million, or 0.7%, for the three months ended March 31, 2012, compared to the same period in 2011. These increases were partially offset by a decrease in the average balances of certificates of deposit of \$29.5 million, or 7.7% for the three months ended March 2012.

Interest expense on borrowings decreased \$70,000, or 72.9%, to \$26,000 for the three months ended March 31, 2012, from \$96,000 for the same period in 2011. The decrease in interest expense on borrowings was due to an \$8.7 million, or 48.8%, decrease of our average borrowings to \$9.2 million for the three months ended March 31, 2012, from \$17.9 million for the same period in 2011, and a 103 basis point decrease in interest rates paid on borrowings to 1.14% for the three months ended March 31, 2012, from 2.17% for the same period in 2011.

**Table of Contents****Average Balance Sheets**

The following table sets forth average balance sheets, average yields and costs, and certain other information for the periods indicated. No tax-equivalent yield adjustments were made, as the effect of these adjustments would not be material. Average balances are daily average balances. Nonaccrual loans have been included in the computation of average balances, but have been reflected in the table as loans carrying a zero yield. The yields set forth below include, where applicable, the effect of deferred fees and expenses, discounts and premiums, and purchase accounting adjustments that are amortized or accreted to interest income or expense.

|                                                                  | For the Three Months Ended March 31, |           |                   |                                   |           |                   |
|------------------------------------------------------------------|--------------------------------------|-----------|-------------------|-----------------------------------|-----------|-------------------|
|                                                                  | 2012                                 |           |                   | 2011                              |           |                   |
|                                                                  | Average<br>Outstanding<br>Balance    | Interest  | Yield/Rate<br>(1) | Average<br>Outstanding<br>Balance | Interest  | Yield/Rate<br>(1) |
|                                                                  | (dollars in thousands)               |           |                   |                                   |           |                   |
| <b>Interest-earning Assets:</b>                                  |                                      |           |                   |                                   |           |                   |
| Loans                                                            | \$ 1,236,234                         | \$ 16,112 | 5.24%             | \$ 1,118,256                      | \$ 14,410 | 5.23%             |
| Securities                                                       | 88,448                               | 442       | 2.01              | 118,913                           | 822       | 2.80              |
| Stock in FHLB                                                    | 13,868                               | 4         | 0.12              | 15,711                            | 3         | 0.08              |
| Other                                                            | 115,567                              | 76        | 0.26              | 166,793                           | 113       | 0.27              |
| Total interest-earning assets                                    | 1,454,117                            | 16,634    | 4.60              | 1,419,673                         | 15,348    | 4.38              |
| Noninterest-earning assets                                       | 87,698                               |           |                   | 118,053                           |           |                   |
| Total assets                                                     | \$ 1,541,815                         |           |                   | \$ 1,537,726                      |           |                   |
| <b>Interest-bearing Liabilities:</b>                             |                                      |           |                   |                                   |           |                   |
| Savings deposits                                                 | \$ 145,544                           | 37        | 0.10              | \$ 107,660                        | 66        | 0.25              |
| Money market accounts                                            | 345,339                              | 314       | 0.37              | 343,119                           | 440       | 0.52              |
| Interest-bearing NOW accounts                                    | 331,459                              | 98        | 0.12              | 303,459                           | 153       | 0.20              |
| Certificates of deposit                                          | 355,921                              | 765       | 0.86              | 385,458                           | 1,241     | 1.31              |
| Total deposits                                                   | 1,178,263                            | 1,214     | 0.41              | 1,139,696                         | 1,900     | 0.68              |
| Borrowings                                                       | 9,183                                | 26        | 1.14              | 17,919                            | 96        | 2.17              |
| Total interest-bearing liabilities                               | 1,187,446                            | 1,240     | 0.42              | 1,157,615                         | 1,996     | 0.70              |
| Noninterest-bearing deposits                                     | 131,914                              |           |                   | 108,087                           |           |                   |
| Noninterest-bearing liabilities                                  | 19,520                               |           |                   | 18,604                            |           |                   |
| Total liabilities                                                | 1,338,880                            |           |                   | 1,284,306                         |           |                   |
| Equity                                                           | 202,935                              |           |                   | 253,420                           |           |                   |
| Total liabilities and equity                                     | \$ 1,541,815                         |           |                   | \$ 1,537,726                      |           |                   |
| Net interest income                                              |                                      | \$ 15,394 |                   |                                   | \$ 13,352 |                   |
| Net interest rate spread (2)                                     |                                      |           | 4.18%             |                                   |           | 3.68%             |
| Net interest-earning assets (3)                                  | \$ 266,671                           |           |                   | \$ 262,058                        |           |                   |
| Net interest margin (4)                                          |                                      |           | 4.26%             |                                   |           | 3.81%             |
| Ratio of interest-earning assets to interest-bearing liabilities | 122.46%                              |           |                   | 122.64%                           |           |                   |

- (1) Annualized.
- (2) Net interest rate spread represents the difference between the yield on average interest-earning assets and the cost of average interest-bearing liabilities.
- (3) Net interest-earning assets represents total interest-earning assets less total interest-bearing liabilities.
- (4) Net interest margin represents net interest income divided by average total interest-earning assets.

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**Provision for Loan Losses.** We establish provisions for loan losses, which are charged to operations to maintain the allowance for loan losses at a level we consider necessary to absorb probable incurred credit losses in the loan portfolio. In determining the level of the allowance for loan losses, we consider past and current loss experience, evaluations of real estate collateral, current economic conditions, volume and type of lending, adverse situations that may affect a borrower's ability to repay a loan and the levels of nonaccrual and other classified loans. The amount of the allowance is based on estimates and the ultimate losses may vary from such estimates as more information becomes available or later events change. We assess the allowance for loan losses on a quarterly basis and make provisions for loan losses in order to maintain the allowance.

Based on our evaluation of the above factors, we recorded a \$27,000 credit to the general portion of the allowance for loan losses and a decrease of \$61,000 attributable to the specific portion of the allowance for loan losses that we allocate to impaired loans.

A loan balance is classified as a loss and charged-off when it is confirmed that there is no readily apparent source of repayment for the amount of the loan that is classified as loss. Confirmation can occur upon the receipt of updated third-party appraisal valuation information indicating that there is a low probability of repayment upon sale of the collateral, the final disposition of collateral where the net proceeds are insufficient to pay the loan balance in full, our failure to obtain possession of certain consumer-loan collateral within certain time limits specified by applicable federal regulations, the conclusion of legal proceedings where the borrower's obligation to repay is legally discharged (such as a Chapter 7 bankruptcy proceeding), or when it appears that further formal collection procedures are not likely to result in net proceeds in excess of the costs to collect.

**Past Due Loans**

The following table reflects investment and business loans past due less than 90 days at March 31, 2012, excluding purchased impaired loans.

|                                                     | Loan Balances            |                                                    | Total<br>30 - 89<br>Days<br>Past Due |
|-----------------------------------------------------|--------------------------|----------------------------------------------------|--------------------------------------|
|                                                     | 30 - 59 Days<br>Past Due | 60 - 89 Days<br>Past Due<br>(Dollars in thousands) |                                      |
| Multi-family mortgage loans                         | \$ 10,315                | \$                                                 | \$ 10,315                            |
| Nonresidential real estate loans                    | 2,254                    |                                                    | 2,254                                |
| Construction and land loans                         | 4,822                    |                                                    | 4,822                                |
| Commercial                                          | 3,991                    | 130                                                | 4,121                                |
| Past due investment and business loans              | \$ 21,382                | \$ 130                                             | \$ 21,512                            |
| Matured loans                                       | \$ 9,095                 | \$ 121                                             | \$ 9,216                             |
| % of past due investment and business matured loans | 42.54%                   | 93.08%                                             | 42.84%                               |

At March 31, 2012, our past due multi-family, nonresidential real estate, construction and development and commercial loans totaled \$21.5 million. Of the \$21.5 million in past due loans, \$9.2 million, or 42.8%, were Pass rated matured loans that were in the process of renewal, and \$12.1 million, or 56.3% were loans on nonaccrual status. The remaining \$176,000 of the past due loans were subject to informal collection activity that was intended to bring the loan current.

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### **Nonperforming Loans and Assets**

We review loans on a regular basis, and generally place loans on nonaccrual status when either principal or interest is 90 days or more past due. In addition, the Company places loans on nonaccrual status when we do not expect to receive full payment of interest or principal. Interest accrued and unpaid at the time a loan is placed on nonaccrual status is reversed from interest income. Interest payments received on nonaccrual loans are recognized in accordance with our significant accounting policies. Once a loan is placed on nonaccrual status, the borrower must generally demonstrate at least six months of payment performance before the loan is eligible to return to accrual status. We may have loans classified as 90 days or more delinquent and still accruing. Generally, we do not utilize this category of loan classification unless: (1) the loan is repaid in full shortly after the period end date; (2) the loan is well secured and there are no asserted or pending legal barriers to its collection; or (3) the borrower has remitted all scheduled payments and is otherwise in substantial compliance with the terms of the loan, but the processing of loan payments actually received or the renewal of the loan has not occurred for administrative reasons. At March 31, 2012, we had five loans totaling \$828,000 in this category and we had three loans totaling \$350,000 in this category at December 31, 2011.

We typically obtain new third party appraisals or collateral valuations when we place a loan on nonaccrual status, conduct impairment testing or conduct a TDR unless the existing valuation information for the collateral is sufficiently current to comply with the requirements of our Appraisal and Collateral Valuation Policy ( ACV Policy ). We also obtain new third party appraisals or collateral valuations when the judicial foreclosure process concludes with respect to real estate collateral, and when we otherwise acquire actual or constructive title to real estate collateral. In addition to third party appraisals, we use updated valuation information based on Multiple Listing Service data, broker opinions of value, actual sales prices of similar assets sold by us and approved sales prices in response to offers to purchase similar assets owned by us to provide interim valuation information for consolidated financial statement and management purposes. Our ACV Policy establishes the maximum useful life of a real estate appraisal at 18 months. Because appraisals and updated valuations utilize historical or ask side data in reaching valuation conclusions, the appraised or updated valuation may or may not reflect the actual sales price that we will receive at the time of sale.

Real estate appraisals may include up to three approaches to value: the sales comparison approach, the income approach (for income-producing property) and the cost approach. Not all appraisals utilize all three approaches. Depending on the nature of the collateral and market conditions, we may emphasize one approach over another in determining the fair value of real estate collateral. Appraisals may also contain different estimates of value based on the level of occupancy or planned future improvements. As-is valuations represent an estimate of value based on current market conditions with no changes to the use or condition of the real estate collateral. As-stabilized or as-completed valuations assume the real estate collateral will be improved to a stated standard or achieve its highest and best use in terms of occupancy. As-stabilized or as-completed valuations may be subject to a present value adjustment for market conditions or the schedule of improvements.

As part of the asset classification process, we develop an exit strategy for real estate collateral or OREO by assessing overall market conditions, the current use and condition of the asset, and its highest and best use. For most income producing real estate, we believe that investors value most highly a stable income stream from the asset; consequently, we perform a comparative evaluation to determine whether conducting a sale on an as is, as stabilized or as improved basis is most likely to produce the highest net realizable value. If we determine that the as stabilized or as improved basis is appropriate, we then complete the necessary improvements or tenant stabilization tasks, with the applicable time value discount and improvement expenses incorporated into our estimates of the expected costs to sell. As of March 31, 2012, substantially all of our impaired real estate loan collateral and OREO were valued on an as is basis.

Estimates of the net realizable value of real estate collateral also include a deduction for the expected costs to sell the collateral or such other deductions from the cash flows resulting from the operation and liquidation of the asset as are appropriate. For most real estate collateral subject to the judicial foreclosure process, we apply a 10.0% deduction to the value of the asset to determine the expected costs to sell the asset. This estimate includes one year of real estate taxes, sales commissions and miscellaneous repair and closing costs. If we receive a purchase offer that requires unbudgeted repairs, or if the expected resolution period for the asset exceeds one year, we then include, on a case-by-case basis, the costs of the additional real estate taxes and repairs and any other material holding costs in the expected costs to sell the collateral. For OREO, we only apply a 7.0% deduction to determine the expected costs to sell, as expenses for real estate taxes and repairs are expensed when incurred.

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The following table below sets forth the amounts and categories of our nonperforming loans and nonperforming assets at the dates indicated.

|                                                                                                 | March 31,<br>2012 | December 31,<br>2011<br>(Dollars in thousands) | Change          |
|-------------------------------------------------------------------------------------------------|-------------------|------------------------------------------------|-----------------|
| <b>Nonaccrual loans:</b>                                                                        |                   |                                                |                 |
| One-to-four family residential                                                                  | \$ 11,602         | \$ 10,709                                      | \$ 893          |
| Multi-family mortgage                                                                           | 13,264            | 14,983                                         | (1,719)         |
| Nonresidential real estate                                                                      | 32,892            | 30,396                                         | 2,496           |
| Construction and land                                                                           | 3,263             | 3,263                                          |                 |
| Commercial                                                                                      | 3,527             | 2,940                                          | 587             |
| Commercial leases                                                                               | 22                | 22                                             |                 |
| Consumer                                                                                        | 8                 | 3                                              | 5               |
| <b>Total nonaccrual loans</b>                                                                   | <b>64,578</b>     | <b>62,316</b>                                  | <b>2,262</b>    |
| <b>Other real estate owned:</b>                                                                 |                   |                                                |                 |
| One-to-four family residential                                                                  | 4,251             | 5,328                                          | (1,077)         |
| Multi-family mortgage                                                                           | 3,005             | 3,655                                          | (650)           |
| Nonresidential real estate                                                                      | 4,756             | 4,905                                          | (149)           |
| Land                                                                                            | 1,712             | 2,237                                          | (525)           |
| <b>Total other real estate owned</b>                                                            | <b>13,724</b>     | <b>16,125</b>                                  | <b>(2,401)</b>  |
| Nonperforming assets (excluding purchased impaired loans and purchased other real estate owned) | 78,302            | 78,441                                         | (139)           |
| <b>Purchased impaired loans</b>                                                                 |                   |                                                |                 |
| One-to-four family residential                                                                  | 3,670             | 3,941                                          | (271)           |
| Multi-family mortgage                                                                           | 1,454             | 1,418                                          | 36              |
| Nonresidential real estate                                                                      | 3,308             | 3,375                                          | (67)            |
| Construction and land                                                                           | 4,859             | 4,788                                          | 71              |
| Commercial                                                                                      | 841               | 1,078                                          | (237)           |
| <b>Total nonaccrual loans</b>                                                                   | <b>14,132</b>     | <b>14,600</b>                                  | <b>(468)</b>    |
| <b>Purchased other real estate owned:</b>                                                       |                   |                                                |                 |
| One-to-four family residential                                                                  | 721               | 327                                            | 394             |
| Nonresidential real estate                                                                      | 2,264             | 2,546                                          | (282)           |
| Land                                                                                            | 3,480             | 3,482                                          | (2)             |
| <b>Total other real estate owned</b>                                                            | <b>6,465</b>      | <b>6,355</b>                                   | <b>110</b>      |
| <b>Purchased impaired loans and other real estate owned</b>                                     | <b>20,597</b>     | <b>20,955</b>                                  | <b>(358)</b>    |
| <b>Total nonperforming assets</b>                                                               | <b>\$ 98,899</b>  | <b>\$ 99,396</b>                               | <b>\$ (497)</b> |
| <b>Ratios:</b>                                                                                  |                   |                                                |                 |
| Nonperforming loans to total loans                                                              | 6.51%             | 6.11%                                          |                 |
| Nonperforming loans to total loans <sup>(1)</sup>                                               | 5.34              | 4.95                                           |                 |
| Nonperforming assets to total assets                                                            | 6.38              | 6.36                                           |                 |
| Nonperforming loans to total assets <sup>(1)</sup>                                              | 5.05              | 5.02                                           |                 |

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- (1) These asset quality ratios exclude purchased impaired loans and purchased other real estate owned resulting from the Downers Grove National Bank acquisition.



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**Loans on Nonaccrual Status**

Non-accrual loans increased by \$2.3 million in the first quarter 2012, primarily due to the placement of loans to two commercial real estate borrowers on non-accrual status, which was partially offset by successful resolutions of other non-performing assets.

We placed a \$2.2 million loan secured by owner-occupied commercial real estate on non-accrual status in the first quarter of 2012. The loan matured in the fourth quarter of 2011 and demonstrated sufficient debt service coverage at market rates. During first quarter, 2012, the borrower advised us that certain personal health issues had arisen, and as a result, the interim 2012 performance of the business had deteriorated below an adequate level of debt service coverage and the liquidity disclosed on the borrower's personal financial statements was no longer available to support business. Given these developments, we placed the loan on non-accrual status and began formal collection proceedings.

We placed two loans acquired in the Downers Grove National Bank acquisition totaling \$1.6 million on non-accrual status in the first quarter of 2012. The loans are secured by income-producing commercial real estate and an on-site inspection confirmed that the properties remain fully-occupied. The decision to place the loans on non-accrual status was based on the borrower's failure to submit requested financial information and make scheduled payments in the first quarter, 2012. We have initiated formal collection proceedings.

Material activity related to significant non-performing assets previously disclosed was as follows:

We negotiated final consensual resolutions of several non-performing loan exposures totaling \$3.4 million during the first quarter of 2012. The resolutions are scheduled to close in the second quarter of 2012. To facilitate the resolutions, we recorded additional specific valuation allowances of \$482,000 in our results of operations for the first quarter of 2012.

Our second-largest total credit exposure is \$10.8 million, consisting of three loans secured by a combination of two income-producing commercial real estate properties leased to a credit tenant and several improved vacant land parcels held for future development. We were notified during third quarter of 2011 that the tenant for the two income producing properties had proposed to renew the lease on one facility at a 50% reduction to the current rental rate, and did not intend to renew the lease on the second facility. We concluded that, based on this development, it was not probable that the borrowers could continue to maintain the same debt service payments on the total outstanding credit exposure upon expiration of the current leases. Accordingly, we placed the loans on non-accrual status and established a special valuation allowance of \$1.4 million based on a discounted cash flow analysis of the expected cash flows and the net realizable value of the collateral. The lease was subsequently renewed on the first facility at the reduced rental rate, and the borrowers are reportedly seeking a new tenant or purchaser for the second facility. We obtained updated appraisals for the first facility based on the renewed lease, and for the second facility and the other collateral on an as vacant basis. Based on the updated appraisals, we recorded an additional \$1.9 million specific valuation allowance at December 31, 2011 with respect to this exposure. To resolve the basis of classification, and to permit time to lease the second facility, we proposed a loan renewal structure to the borrowers in which \$5.8 million of the loan exposure would be eligible for return to accrual status in 2012, and \$2.0 million would be maintained on a cash basis until the second income-producing facility is leased. The borrowers rejected the proposal primarily because it required them to provide us with additional collateral. We commenced foreclosure proceedings and actions on the notes against all of the borrowers in state court during the first quarter of 2012. Shortly before our motion for the appointment of a receiver for the income-producing property was scheduled to be heard, the borrower that beneficially owns the real estate collateral filed a Chapter 11 bankruptcy case. We will pursue our claims against that borrower and the real estate collateral in the context of the bankruptcy case, and will continue to pursue our claims on the notes against the individual borrowers in the state court action.

We have a \$6.1 million total credit exposure secured by industrial/flex suburban Chicago commercial real estate owned by a family. As disclosed in third quarter, 2011, the owners are liquidating this portfolio in an orderly sales process. Of the \$6.1 million in total credit exposure, four properties with a total loan balance



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of \$3.0 million have sufficient net operating income to make scheduled loan payments. Three properties with a total loan balance of \$3.2 million have insufficient net operating income to make scheduled loan payments; however, the owners have historically established a supplemental cash reserve to fund the difference necessary to make all scheduled loan payments pending the liquidation of the properties. The owners exhausted the supplemental cash reserve during fourth quarter of 2011; therefore, at December 31, 2011, we elected to place these three loans involving a total of \$3.1 million on non-accrual status and established a special valuation allowance of \$481,000 pending the verification of the sources of continuing debt service support. The borrower received a letter of intent to purchase four of these properties in the fourth quarter of 2012; however, the letter of intent was terminated just before the end of the first quarter of 2012. We are now discussing with the borrower the terms and conditions of a potential short-term renewal of these loans to facilitate the orderly liquidation of these properties during the remainder of 2012.

We placed loans totaling \$2.0 million secured by an income-producing commercial real estate project on non-accrual status at September 30, 2011, due to the borrower's transfer of ownership of the project to a new owner without the Bank's consent. The notes matured in 2011 and the new owner continues to remit the monthly payments due under the terms of the matured notes. We are in the process of underwriting loan renewals to the new owner that would reflect a reduction of the principal balance of the original loans based on the results of an updated appraisal. At our option, the original borrower will remain responsible for any deficiency. The underwriting of the loan is now in the latter stages, and if the results of our underwriting of the new owner are acceptable, we expect to be in a position to return the loans to accrual status in 2012; however, we informed the owner that it must conclude the renewal process by the end of the second quarter of 2012 to avoid formal collection action.

We placed a total of \$1.9 million of loans to two borrowers on non-accrual status at December 31, 2011 due to the borrowers' partial compliance with loan renewal terms and forbearance agreements. The loans are secured by multi-family real estate collateral. The loans were placed on non-accrual status because the borrowers were in the process of remitting loan payments and supporting documentation but were not in full compliance with the required terms and conditions of the loan renewals or forbearance agreements at December 31, 2011. These borrowers are now in substantial compliance with the terms and conditions of the loan renewals and forbearance agreements, and if compliance continues, we expect to be in a position to return these loans to accrual status in 2012.

**Table of Contents****Other Real Estate Owned**

Real estate that is acquired through foreclosure or a deed in lieu of foreclosure is classified as OREO until it is sold. When real estate is acquired through foreclosure or by deed in lieu of foreclosure, it is recorded at its fair value, less the estimated costs of disposal as discussed above. If the fair value of the property is less than the loan balance, the difference is charged against the allowance for loan losses.

|                                          | Balance<br>at<br>December 31,<br>2011 | Additions | Write downs<br>and<br>receipts | Sale       | Balance at<br>March 31,<br>2012 |
|------------------------------------------|---------------------------------------|-----------|--------------------------------|------------|---------------------------------|
|                                          | (Dollars in thousands)                |           |                                |            |                                 |
| One to four family residential           | \$ 5,328                              | \$ 285    | \$                             | \$ (1,362) | \$ 4,251                        |
| Multi-family mortgage                    | 3,655                                 | 113       |                                | (763)      | 3,005                           |
| Nonresidential real estate               | 4,905                                 | 230       | (184)                          | (195)      | 4,756                           |
| Land                                     | 2,237                                 |           |                                | (525)      | 1,712                           |
|                                          | 16,125                                | 628       | (184)                          | (2,845)    | 13,724                          |
| <i>Acquired other real estate owned:</i> |                                       |           |                                |            |                                 |
| One to four family residential           | 327                                   | 394       |                                |            | 721                             |
| Nonresidential real estate               | 2,546                                 |           | (282)                          |            | 2,264                           |
| Land                                     | 3,482                                 | 105       | (107)                          |            | 3,480                           |
|                                          | 6,355                                 | 499       | (389)                          |            | 6,465                           |
| Total other real estate owned            | \$ 22,480                             | \$ 1,127  | \$ (573)                       | \$ (2,845) | \$ 20,189                       |

We closed sales of OREO in the amount of \$2.9 million of net book value in the first quarter of 2012, compared to sales of \$3.8 million in the fourth quarter of 2011. Based on current ordinary liquidation activity, we estimate that OREO sales of approximately \$5.1 million will close in the second and third quarters of 2012.

We market real estate for sale based on an estimate of its net realizable value. Depending on the levels of market interest received during the initial period of market exposure, we may reduce the offering price in subsequent periods; if we do so, the new offering price becomes the new net realizable value. We may also accept an offer to purchase a given real estate asset at a price below the net realizable value if there has been limited interest at the original offering price and we conclude that further market exposure time (even at a price lower than the current offering price but higher than the proposed actual sales price) will not produce materially better results given the holding costs and property management risks incurred over time.

**Table of Contents****Troubled Debt Restructuring**

The Company had \$16.8 million of TDRs at March 31, 2012, compared to \$18.1 million at December 31, 2011, with \$1.1 million in specific valuation allowances allocated to those loans at March 31, 2012 and December 31, 2011. The Company had no outstanding commitments to borrowers whose loans are classified as TDRs.

The following table presents loans by class classified as TDRs:

|                                                          | March 31,<br>2012      | December 31,<br>2011 |
|----------------------------------------------------------|------------------------|----------------------|
|                                                          | (Dollars in thousands) |                      |
| One-to-four family residential real estate               | \$ 5,447               | \$ 5,619             |
| Multi-family mortgages                                   | 5,771                  | 5,783                |
| Nonresidential real estate                               | 1,017                  | 2,220                |
| Commercial loans secured                                 | 215                    | 238                  |
| <b>Troubled debt restructured loans accrual loans</b>    | <b>12,450</b>          | <b>13,860</b>        |
| One-to-four family residential real estate               | 358                    | 556                  |
| Multi-family mortgage                                    | 1,217                  | 717                  |
| Nonresidential real estate                               | 2,786                  | 2,960                |
| Commercial loans secured                                 |                        |                      |
| Consumer loans                                           | 3                      | 3                    |
| <b>Troubled debt restructured loans nonaccrual loans</b> | <b>4,364</b>           | <b>4,236</b>         |
| <b>Total troubled debt restructured loans</b>            | <b>\$ 16,814</b>       | <b>\$ 18,096</b>     |

The TDRs described above had no impact on interest income, increased the allowance for loan losses by \$259,000 and resulted in charge offs of \$470,000 during the three months ended March 31, 2012.

**Noninterest income**

The following table summarizes noninterest income:

|                                               | Three months<br>ended March 31, |        |         |
|-----------------------------------------------|---------------------------------|--------|---------|
|                                               | 2012                            | 2011   | Change  |
|                                               | (Dollars in thousands)          |        |         |
| <b>Noninterest income:</b>                    |                                 |        |         |
| Deposit service charges and fees              | \$ 557                          | \$ 614 | \$ (57) |
| Other fee income                              | 385                             | 382    | 3       |
| Insurance commissions and annuities income    | 122                             | 169    | (47)    |
| Gain on sale of loans, net                    | 267                             | 19     | 248     |
| Loan servicing fees                           | 128                             | 132    | (4)     |
| Loss on disposition of premises and equipment |                                 | (10)   | 10      |
| Amortization of servicing assets              | (69)                            | (54)   | (15)    |
| Impairment of servicing assets                | (13)                            |        | (13)    |
| Earnings on bank owned life insurance         | 126                             | 158    | (32)    |
| Trust income                                  | 184                             | 76     | 108     |
| Other                                         | 145                             | 85     | 60      |

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|                                 |          |          |        |
|---------------------------------|----------|----------|--------|
| <b>Total noninterest income</b> | \$ 1,832 | \$ 1,571 | \$ 261 |
|---------------------------------|----------|----------|--------|

**Noninterest Income.** Noninterest income increased \$261,000, or 16.6%, to \$1.8 million for the three months ended March 31, 2012, from \$1.6 million for the same period in 2011. Deposit service charges and fees decreased \$57,000, or 9.3%, to \$557,000 for the three months ended March 31, 2012, from \$614,000 for the same period in 2011. Income from insurance commissions and annuities decreased \$47,000, or 27.8%, to \$122,000 for the three

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months ended March 31, 2012, from \$169,000 for the same period in 2011. Gains on sales of loans increased by \$248,000 to \$267,000 for the three months ended March 31, 2012, from \$19,000 for the same period in 2011, due to a increase in the volume of loan sales. In the first quarter 2012, we recorded a pre-tax provision of \$13,000 on our mortgage servicing rights portfolio, compared to no provision or recovery for the same period in 2011. Earnings on bank-owned life insurance were \$126,000 for the three months ended March 31, 2012, compared to \$158,000 for the same period in 2011. Trust income increased \$108,000 to \$184,000 for the three months ended March 31, 2012, from \$76,000 for the same period in 2011, due to the operation of the Trust Department acquired in the Downers Grove National Bank transaction on March 18, 2011.

**Noninterest Expense**

The following table summarizes noninterest expense:

|                                       | Three months ended<br>March 31, |                  | Change          |
|---------------------------------------|---------------------------------|------------------|-----------------|
|                                       | 2012                            | 2011             |                 |
|                                       | (Dollars in thousands)          |                  |                 |
| <b>Noninterest Expense:</b>           |                                 |                  |                 |
| Compensation and benefits             | \$ 6,659                        | \$ 6,600         | \$ 59           |
| Office occupancy and equipment        | 1,743                           | 1,868            | (125)           |
| Advertising and public relations      | 94                              | 237              | (143)           |
| Information technology                | 1,261                           | 948              | 313             |
| Supplies, telephone and postage       | 430                             | 375              | 55              |
| Amortization of intangibles           | 163                             | 382              | (219)           |
| Nonperforming asset management        | 1,191                           | 455              | 736             |
| Gain on sale other real estate owned  | (139)                           | (52)             | (87)            |
| Operations of other real estate owned | 351                             | 326              | 25              |
| Write down other real estate owned    | 389                             | 179              | 210             |
| FDIC insurance premiums               | 348                             | 567              | (219)           |
| Acquisition costs                     |                                 | 1,531            | (1,531)         |
| Other                                 | 946                             | 839              | 107             |
| <b>Total noninterest expense</b>      | <b>\$ 13,436</b>                | <b>\$ 14,255</b> | <b>\$ (819)</b> |

**Noninterest Expense.** Noninterest expense was \$13.4 million for the three months ended March 31, 2012, compared to \$14.3 million for the three months ended March 31, 2011, a decrease of \$819,000, or 5.7%. Information technology expense increased \$313,000, or 33.0%, to \$1.3 million, from \$948,000 for the same period in 2011. This increase reflects upgrades in the software combined with increases in equipment and processing costs associated with two Downers Grove National Bank branches acquired in March 2011.

Net expense from nonperforming asset management was \$1.2 million for the three months ended March 31, 2012, compared to \$455,000 for the same period in 2011. Net expense from nonperforming asset management included \$565,000 for real estate taxes for the three months ended March 31, 2012, an increase of \$264,000, compared to \$301,000 expenses for real estate taxes for the same period in 2011. The gain from sales of other real estate owned was \$139,000 for the three months ended March 31, 2012, compared to a gain of \$52,000 from sales of other real estate owned for the same period in 2011. Net expense from operations of other real estate owned was \$351,000 for the three months ended March 31, 2012, compared to \$326,000 for the same period in 2011. Net expense from operations of other real estate owned included \$166,000 for legal, insurance and receiver fee expenses for the three months ended March 31, 2012 compared to \$142,000 for the same period in 2011. Current period net expense from operations of other real estate owned for the current quarter also included \$389,000 in write-downs on other real estate owned, compared to \$179,000 for the same period in 2011.

Acquisition expense recorded in the first quarter 2011 included \$1.3 million in expenses relating to the acquisition of Downers Grove National Bank, including \$432,000 in data processing contracts and operational expenses, and \$678,000 that was recorded for contract and severance payments. Also recorded in the first quarter 2011 was \$278,000 of expenses relating to the multi-family loan purchase from Citibank.

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**Income Tax Expense (Benefit).** We recorded an income tax expense of \$457,000 for the three months ended March 31, 2012, compared to an income tax benefit of \$979,000 for the same period in 2011. The effective tax rate for the three months ended March 31, 2012 was 16.4% compared to 55.8% in 2011. Effective in 2011, the Illinois corporate income tax rate increased from 7.3% to 9.5%. As a result of this change, we recorded an additional tax benefit of \$227,000 for the three months ended March 31, 2011 related to the write-up of state deferred tax assets.

### **Liquidity and Capital Resources**

**Liquidity.** The overall objective of our liquidity management is to ensure the availability of sufficient cash funds to meet all financial commitments and to take advantage of lending and investment opportunities. We manage liquidity in order to meet deposit withdrawals on demand or at contractual maturity, to repay borrowings as they mature, and to fund new loans and investments as opportunities arise.

Our primary sources of funds are deposits, principal and interest payments on loans and securities, and, to a lesser extent, wholesale borrowings, the proceeds from maturing securities and short-term investments, and the proceeds from the sales of loans and securities. The scheduled amortization of loans and securities, as well as proceeds from borrowings, are predictable sources of funds. Other funding sources, however, such as deposit inflows, mortgage prepayments and mortgage loan sales are greatly influenced by market interest rates, economic conditions and competition. The Bank is a member of the FHLBC, which provides an additional source of short-term and long-term funding. The outstanding borrowing from the FHLBC was \$3.0 million at March 31, 2012, at an interest rate of 2.99%; this borrowing will mature in less than one year. Outstanding FHLBC borrowing was \$3.0 million at December 31, 2011.

The liquidity needs of the Company on an unconsolidated basis consist primarily of operating expenses, dividends to stockholders and stock repurchases. The primary source of liquidity for the Company currently is \$11.6 million in cash and cash equivalents as of March 31, 2012 and cash dividends from our subsidiary, the Bank.

As a result of the regulatory restructuring occasioned by the Dodd-Frank Act, the Company is now subject to Federal Reserve Board Supervisory Letter SR 09-4, which provides that a holding company should, among other things, inform the Federal Reserve Bank prior to declaring a dividend if its net income for the current quarter is not sufficient to fully fund the dividend, and inform the Federal Reserve Bank and consider eliminating, deferring or significantly reducing its dividends if its net income for the current quarter is not sufficient to fully fund the dividends, or if its net income for the past four quarters, net of dividends previously paid during that period, is not sufficient to fully fund the dividends. The Company declared cash dividends of \$211,000, or \$0.01 per share, to our stockholders during the first quarter of 2012.

As of March 31, 2012, we were not aware of any known trends, events or uncertainties that have or are reasonably likely to have a material impact on our liquidity. As of March 31, 2012, we had no other material commitments for capital expenditures.

**Capital Resources.** Total stockholders' equity was \$202.1 million at March 31, 2012, compared to \$199.9 million at December 31, 2011. The increase in total stockholders' equity was primarily due to the combined impact of our net income of \$2.3 million, offset by our declaration of cash dividends totaling \$211,000, and a \$55,000 decrease in accumulated other comprehensive income during the quarter ended March 31, 2012. The unallocated shares of common stock that our ESOP owns were reflected as a \$13.0 million reduction to stockholders' equity at March 31, 2012, compared to a \$13.2 million reduction to stockholders' equity at December 31, 2011.

Our Board of Directors has authorized the repurchase of up to 5,047,423 shares of our common stock. The authorization permits shares to be repurchased in open market or negotiated transactions, and pursuant to any trading plan that may be adopted in accordance with Rule 10b5-1 of the Securities and Exchange Commission. The authorization may be utilized at management's discretion, subject to the limitations set forth in Rule 10b-18 of the Securities and Exchange Commission and other applicable legal requirements, and to price and other internal limitations established by the Board of Directors. The repurchase authorization will expire on May 15, 2012, unless extended by the Board of Directors. As of March 31, 2012, the Company had repurchased 4,239,134 shares of its common stock out of the 5,047,423 shares that have been authorized for repurchase. Federal Reserve Board



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Supervisory Letter SR 09-4 provides that holding companies experiencing financial weaknesses such as operating losses should consult with the appropriate Federal Reserve supervisory staff before redeeming or repurchasing common stock. The Company has not initiated discussions with the Federal Reserve supervisory staff with respect to common stock repurchases, and has no plans to initiate such discussions in the immediate future. Due to the Company's operating loss in 2011, the Company will not undertake any further share repurchases without engaging in discussions with the Federal Reserve supervisory staff.

At March 31, 2012 and December 31, 2011, the actual regulatory capital ratios and minimum required regulatory ratios for the Bank were:

|                                                  | Actual Ratio | Minimum<br>Required for<br>Capital<br>Adequacy<br>Purposes | Minimum<br>Required to Be<br>Well Capitalized<br>Under<br>Prompt Corrective Action<br>Provisions |
|--------------------------------------------------|--------------|------------------------------------------------------------|--------------------------------------------------------------------------------------------------|
| <b>March 31, 2012</b>                            |              |                                                            |                                                                                                  |
| Total capital (to risk-weighted assets)          | 15.58%       | 8.00%                                                      | 10.00%                                                                                           |
| Tier 1 (core) capital (to risk-weighted assets)  | 14.31        | 4.00                                                       | 6.00                                                                                             |
| Tier 1 (core) capital (to adjusted total assets) | 10.98        | 4.00                                                       | 5.00                                                                                             |
| <b>December 31, 2011</b>                         |              |                                                            |                                                                                                  |
| Total capital (to risk-weighted assets)          | 14.73%       | 8.00%                                                      | 10.00%                                                                                           |
| Tier 1 (core) capital (to risk-weighted assets)  | 13.47        | 4.00                                                       | 6.00                                                                                             |
| Tier 1 (core) capital (to adjusted total assets) | 10.50        | 4.00                                                       | 5.00                                                                                             |

As of March 31, 2012 and December 31, 2011, the Bank as well capitalized under the OCC regulatory framework for prompt corrective action. There are no conditions or events since those notifications that management believes have changed the institution's category.

**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

**Qualitative Analysis.** A significant form of market risk is interest rate risk. Interest rate risk results from timing differences in the maturity or repricing of our assets, liabilities and off balance sheet contracts (*i.e.*, forward loan commitments), the effect of loan prepayments and deposit withdrawals, the difference in the behavior of lending and funding rates arising from the use of different indices and yield curve risk arising from changing rate relationships across the spectrum of maturities for constant or variable credit risk investments. In addition to directly affecting net interest income, changes in market interest rates can also affect the amount of new loan originations, the ability of borrowers to repay variable rate loans, the volume of loan prepayments and refinancings, the carrying value of investment securities classified as available-for-sale and the flow and mix of deposits.

The general objective of our interest rate risk management is to determine the appropriate level of risk given our business strategy and then manage that risk in a manner that is consistent with our policy to reduce, to the extent possible, the exposure of our net interest income to changes in market interest rates. Our Asset/Liability Management Committee (ALCO), which consists of certain members of senior management, evaluates the interest rate risk inherent in certain assets and liabilities, our operating environment and capital and liquidity requirements, and modifies our lending, investing and deposit gathering strategies accordingly. The Board of Directors Asset/Liability Management Committee then reviews the ALCO's activities and strategies, the effect of those strategies on our net interest margin, and the effect that changes in market interest rates would have on the economic value of our loan and securities portfolios as well as the intrinsic value of our deposits and borrowings, and reports to the full Board of Directors.

We actively evaluate interest rate risk in connection with our lending, investing and deposit activities. In an effort to better manage interest-rate risk, we have de-emphasized the origination of residential mortgage loans, and have increased our emphasis on the origination of nonresidential real estate loans, multi-family mortgage loans, commercial loans and commercial leases. In addition, depending on market interest rates and our capital and liquidity position, we generally sell all or a portion of our longer-term, fixed-rate residential loans, usually on a servicing-retained basis. Further, we primarily invest in shorter-duration securities, which generally have lower

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yields compared to longer-term investments. Shortening the average maturity of our interest-earning assets by increasing our investments in shorter-term loans and securities, as well as loans with variable rates of interest, helps to better match the maturities and interest rates of our assets and liabilities, thereby reducing the exposure of our net interest income to changes in market interest rates. Finally, we have classified all of our investment portfolio as available-for-sale so as to provide flexibility in liquidity management.

We utilize a combination of analyses to monitor the Bank's exposure to changes in interest rates. The economic value of equity analysis is a model that estimates the change in net portfolio value ( NPV ) over a range of interest rate scenarios. NPV is the discounted present value of expected cash flows from assets, liabilities and off-balance sheet contracts. In calculating changes in NPV, we assume estimated loan prepayment rates, reinvestment rates and deposit decay rates that seem most likely based on historical experience during prior interest rate changes.

Our net interest income analysis utilizes the data derived from the dynamic GAP analysis, described below, and applies several additional elements, including actual interest rate indices and margins, contractual limitations such as interest rate floors and caps and the U.S. Treasury yield curve as of the balance sheet date. In addition, we apply consistent parallel yield curve shifts (in both directions) to determine possible changes in net interest income if the theoretical yield curve shifts occurred instantaneously. Net interest income analysis also adjusts the dynamic GAP repricing analysis based on changes in prepayment rates resulting from the parallel yield curve shifts.

Our dynamic GAP analysis determines the relative balance between the repricing of assets and liabilities over multiple periods of time (ranging from overnight to five years). Dynamic GAP analysis includes expected cash flows from loans and mortgage-backed securities, applying prepayment rates based on the differential between the current interest rate and the market interest rate for each loan and security type. This analysis identifies mismatches in the timing of asset and liability repricing but does not necessarily provide an accurate indicator of interest rate risk because it omits the factors incorporated into the net interest income analysis.

**Quantitative Analysis.** The following table sets forth, as of March 31, 2012, the estimated changes in the Bank's NPV and net interest income that would result from the designated instantaneous parallel shift in the U.S. Treasury yield curve. Computations of prospective effects of hypothetical interest rate changes are based on numerous assumptions including relative levels of market interest rates, loan prepayments and deposit decay, and should not be relied upon as indicative of actual results.

| Change in Interest Rates (basis points) | Estimated Increase in NPV |         | Decrease in Estimated Net Interest Income |         |
|-----------------------------------------|---------------------------|---------|-------------------------------------------|---------|
|                                         | Amount                    | Percent | Amount                                    | Percent |
| +400                                    | \$ 25,545                 | 13.97%  | \$ (3,170)                                | (5.81)% |
| +300                                    | 22,416                    | 13.89   | (2,286)                                   | (4.19)  |
| +200                                    | 22,289                    | 13.81   | (1,466)                                   | (2.68)  |
| +100                                    | 21,858                    | 13.54   | (753)                                     | (1.38)  |
| 0                                       |                           |         |                                           |         |

The Company has opted not to include an estimate for a decrease in rates at March 31, 2012 as the results are not relevant given the current targeted fed funds rate of the Federal Open Market Committee. The table set forth above indicates that at March 31, 2012, in the event of an immediate 200 basis point increase in interest rates, the Bank would be expected to experience a 13.81% increase in NPV and a \$1.5 million decrease in net interest income. This data does not reflect any actions that we may undertake in response to changes in interest rates, such as changes in rates paid on certain deposit accounts based on local competitive factors, which could reduce the actual impact on NPV and net interest income, if any.

Certain shortcomings are inherent in the methodology used in the above interest rate risk measurements. Modeling changes in NPV and net interest income requires that we make certain assumptions that may or may not reflect the manner in which actual yields and costs respond to changes in market interest rates. The NPV and net interest income table presented above assumes that the composition of our interest-rate-sensitive assets and liabilities existing at the beginning of a period remains constant over the period being measured and, accordingly, the data does not reflect any actions that we may undertake in response to changes in interest rates, such as changes in rates paid on certain deposit accounts based on local competitive factors. The table also assumes that a particular change

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in interest rates is reflected uniformly across the yield curve regardless of the duration to maturity or the repricing characteristics of specific assets and liabilities. Accordingly, although the NPV and net interest income table provides an indication of our sensitivity to interest rate changes at a particular point in time, such measurements are not intended to and do not provide a precise forecast of the effect of changes in market interest rates on our net interest income and will differ from actual results.

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**ITEM 4. CONTROLS AND PROCEDURES**

An evaluation was performed under the supervision and with the participation of the Company's management, including the Chairman, Chief Executive Officer and President and the Executive Vice President and Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in Rule 13a-15(e) promulgated under the Securities and Exchange Act of 1934, as amended) as of March 31, 2012. Based on that evaluation, the Company's management, including the Chairman, President, and Chief Executive Officer and the Executive Vice President and Chief Financial Officer, concluded that the Company's disclosure controls and procedures were effective.

During the quarter ended March 31, 2012, there have been no changes in the Company's internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

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**PART II**

**ITEM 1. LEGAL PROCEEDINGS**

The Company and its subsidiaries are subject to various legal actions that are considered ordinary routine litigation incidental to the business of the Company, and no claim for money damages exceeds ten percent of the Company's consolidated assets. In the opinion of management, based on currently available information, the resolution of these legal actions is not expected to have a material adverse effect on the Company's results of operations.

**ITEM 1A. RISK FACTORS**

There have been no material changes to the risk factors disclosed in our Annual Report on Form 10-K for the year ended December 31, 2011.

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

(a) **Unregistered Sale of Equity Securities.** Not applicable.

(b) **Use of Proceeds.** Not applicable

(c) **Repurchases of Equity Securities.**

Our Board of Directors has authorized the repurchase of up to 5,047,423 shares of our common stock. In accordance with this authorization, we had repurchased 4,239,134 shares of our common stock as of March 31, 2012. There were no share repurchases conducted in the first quarter of 2012. The current share repurchase authorization will expire on May 15, 2012 unless extended.

**ITEM 3. DEFAULTS UPON SENIOR SECURITIES**

None

**ITEM 4. MINE SAFETY DISCLOSURES**

Not applicable

**ITEM 5. OTHER INFORMATION**

None

**ITEM 6. EXHIBITS**

The exhibits required by Item 601 of Regulation S-K are included with this Form 10-Q and are listed on the [Index to Exhibits](#) immediately following the Signatures.



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**SIGNATURES**

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

**BANKFINANCIAL CORPORATION**

(Registrant)

Date: May 7, 2012

/s/ F. MORGAN GASIOR

F. Morgan Gasior

Chairman of the Board, Chief Executive Officer and President

/s/ PAUL A. CLOUTIER

Paul A. Cloutier

Executive Vice President and Chief Financial Officer

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INDEX TO EXHIBITS

Exhibit

| Number  | Description                                                                                                                                                                                                |
|---------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 31.1    | Certification of F. Morgan Gasior, Chairman of the Board, Chief Executive Officer and President, Pursuant to Rule 13a-14(a) and Rule 15d-14(a).                                                            |
| 31.2    | Certification of Paul A. Cloutier, Executive Vice President and Chief Financial Officer, Pursuant to Rule 13a-14(a) and Rule 15d-14(a).                                                                    |
| 32.2    | Certification of F. Morgan Gasior, Chairman of the Board, Chief Executive Officer and President, Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |
| 32.2    | Certification of Paul A. Cloutier, Executive Vice President and Chief Financial Officer, Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.         |
| 101.INS | XBRL Instance Document                                                                                                                                                                                     |
| 101.SCH | XBRL Taxonomy Extension Schema                                                                                                                                                                             |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase                                                                                                                                                               |
| 101.DEF | XBRL Taxonomy Extension Calculation Linkbase                                                                                                                                                               |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase                                                                                                                                                                     |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase                                                                                                                                                              |