

BROADWAY FINANCIAL CORP \DE\  
Form 10-Q  
November 13, 2015  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
**Washington D.C. 20549**

**FORM 10-Q**

(Mark One)

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

For the quarterly period ended September 30, 2015

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

For transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number **000-27464**

**BROADWAY FINANCIAL CORPORATION**

(Exact name of registrant as specified in its charter)

Delaware

95-4547287

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(State or other jurisdiction of  
incorporation or organization)

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

**5055 Wilshire Boulevard, Suite 500**

**Los Angeles, California**  
(Address of principal executive offices)

**90036**  
(Zip Code)

**(323) 634-1700**

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate 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 large accelerated filer, an accelerated filer, a non-accelerated, or a smaller reporting company. See the definition 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 by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: As of November 5, 2015, 21,405,188 shares of the Registrant's voting common stock and 7,671,520 shares of the Registrant's non-voting common stock were outstanding.

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|  | <b>September 30,<br/>2015</b> | <b>December 31,<br/>2014</b> |
|--|-------------------------------|------------------------------|
| <b>Assets</b>  |                               |                              |
| Cash and due from banks  | \$ 5,434                      | \$ 5,740                     |
| Federal funds  | 145,047                       | 15,050                       |
| Cash and cash equivalents  | 150,481                       | 20,790                       |
| Securities available-for-sale, at fair value   | 14,796                        | 17,075                       |
| Loans receivable held for sale, at lower of cost or fair value   | 27,945                        | 19,481                       |
| Loans receivable held for investment, net of allowance of \$6,728 and \$8,465, respectively  | 198,098                       | 276,643                      |
| Accrued interest receivable  | 963                           | 1,216                        |
| Federal Home Loan Bank (FHLB) stock  | 2,573                         | 4,254                        |
| Office properties and equipment, net   | 2,608                         | 2,697                        |
| Real estate owned (REO)  | 558                           | 2,082                        |
| Bank owned life insurance  | 2,867                         | 2,821                        |
| Investment in affordable housing limited partnership   | 973                           | 1,117                        |
| Other assets   | 2,045                         | 2,687                        |
| <b>Total assets</b>  | <b>\$ 403,907</b>             | <b>\$ 350,863</b>            |
| <b>Liabilities and stockholders equity</b>   |                               |                              |
| <b>Liabilities:</b>  |                               |                              |
| Deposits   | \$ 274,921                    | \$ 217,867                   |
| FHLB advances  | 77,500                        | 86,000                       |
| Junior subordinated debentures   | 5,100                         | 5,100                        |
| Advance payments by borrowers for taxes and insurance  | 1,502                         | 1,081                        |
| Accrued expenses and other liabilities   | 4,236                         | 3,557                        |
| <b>Total liabilities</b>   | <b>363,259</b>                | <b>313,605</b>               |
| <b>Stockholders Equity:</b>  |                               |                              |
| Common stock, \$.01 par value, voting, authorized 50,000,000 shares at September 30, 2015 and December 31, 2014; issued 21,509,179 shares at September 30, 2015 and December 31, 2014; outstanding 21,405,188 shares at September 30, 2015 and December 31, 2014 | 215                           | 215                          |
| Common stock, \$.01 par value, non-voting, authorized 25,000,000 shares at September 30, 2015 and December 31, 2014; issued and outstanding 7,671,520 shares at September 30, 2015 and December 31, 2014   | 77                            | 77                           |
| Additional paid-in capital   | 44,669                        | 44,669                       |
| Accumulated deficit  | (3,109)                       | (6,539)                      |
| Accumulated other comprehensive income   | 125                           | 165                          |
| Treasury stock-at cost, 103,991 shares at September 30, 2015 and December 31, 2014   | (1,329)                       | (1,329)                      |
| <b>Total stockholders equity</b>   | <b>40,648</b>                 | <b>37,258</b>                |
| <b>Total liabilities and stockholders equity</b>   | <b>\$ 403,907</b>             | <b>\$ 350,863</b>            |

*See accompanying notes to unaudited consolidated financial statements.*



Table of Contents**BROADWAY FINANCIAL CORPORATION AND SUBSIDIARY****Consolidated Statements of Income and Comprehensive Income****(Unaudited)**

|  | <b>Three Months Ended<br/>September 30,</b> |             | <b>Nine Months Ended<br/>September 30,</b> |             |
|--|---|-------------|--|-------------|
|  | <b>2015</b>                                 | <b>2014</b> | <b>2015</b>                                | <b>2014</b> |
|  | <b>(In thousands, except per share)</b>     |             |  |             |
| <b>Interest income:</b>  |   |             |  |             |
| Interest and fees on loans receivable                                | \$ 3,524                                    | \$ 3,681    | \$ 11,027                                  | \$ 10,996   |
| Interest on mortgage-backed and other securities                     | 84  | 103         | 268  | 271         |
| Other interest income  | 121   | 91          | 451  | 279         |
| Total interest income  | 3,729                                       | 3,875       | 11,746                                     | 11,546      |
| <b>Interest expense:</b>   |   |             |  |             |
| Interest on deposits   | 485   | 421         | 1,335                                      | 1,309       |
| Interest on borrowings   | 446   | 538         | 1,513                                      | 1,608       |
| Total interest expense   | 931   | 959         | 2,848                                      | 2,917       |
| Net interest income before loan loss provision recapture             | 2,798                                       | 2,916       | 8,898                                      | 8,629       |
| Loan loss provision recapture  | 200   | 950         | 1,700                                      | 2,532       |
| Net interest income after loan loss provision recapture              | 2,998                                       | 3,866       | 10,598                                     | 11,161      |
| <b>Non-interest income:</b>  |   |             |  |             |
| Service charges  | 117   | 103         | 325  | 333         |
| Net gain on sale of loans  | 738   | -           | 1,252                                      | -           |
| Net gain on sale of REOs   | 75  | 52          | 75   | 2           |
| CDFI grant   | -   | -           | 355  | 200         |
| Other  | 62  | 10          | 120  | 27          |
| Total non-interest income  | 992   | 165         | 2,127                                      | 562         |
| <b>Non-interest expense:</b>   |   |             |  |             |
| Compensation and benefits  | 1,765                                       | 1,829       | 5,203                                      | 5,024       |
| Occupancy expense, net   | 312   | 321         | 898  | 901         |
| Information services   | 222   | 203         | 684  | 640         |
| Professional services  | 209   | 135         | 687  | 798         |
| Office services and supplies   | 68  | 96          | 228  | 292         |
| FDIC assessments   | 122   | 177         | 297  | 527         |
| REO  | 25  | 82          | 225  | 507         |
| Corporate insurance  | 71  | 65          | 267  | 293         |
| Other  | 209   | 358         | 790  | 925         |
| Total non-interest expense   | 3,003                                       | 3,266       | 9,279                                      | 9,907       |
| Income before income taxes   | 987   | 765         | 3,446                                      | 1,816       |
| Income tax expense   | 8   | -           | 16   | 3           |
| Net income   | \$ 979                                      | \$ 765      | \$ 3,430                                   | \$ 1,813    |
| Other comprehensive income (loss), net of tax:                       |   |             |  |             |
| Change in unrealized gains (losses) on securities available-for-sale | \$ 21                                       | \$ (70)     | \$ (40)                                    | \$ 3        |
| Income tax effect  | -   | -           | -  | -           |
| Other comprehensive income (loss), net of tax                        | 21  | (70)        | (40)                                       | 3           |
| Comprehensive income   | \$ 1,000                                    | \$ 695      | \$ 3,390                                   | \$ 1,816    |
| Earnings per common share-basic                                      | \$ 0.03                                     | \$ 0.04     | \$ 0.12                                    | \$ 0.09     |

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|                                   |    |      |    |      |    |      |    |      |
|-----------------------------------|----|------|----|------|----|------|----|------|
| Earnings per common share-diluted | \$ | 0.03 | \$ | 0.04 | \$ | 0.12 | \$ | 0.09 |
|-----------------------------------|----|------|----|------|----|------|----|------|

*See accompanying notes to unaudited consolidated financial statements.*

Table of Contents**BROADWAY FINANCIAL CORPORATION AND SUBSIDIARY****Consolidated Statements of Cash Flows****(Unaudited)**

|   | <b>Nine Months Ended September 30,</b> |             |
|---|--|-------------|
|   | <b>2015</b>                            | <b>2014</b> |
|   | <b>(In thousands)</b>                  |             |
| <b>Cash flows from operating activities:</b>  |  |             |
| Net income  | \$ 3,430                               | \$ 1,813    |
| Adjustments to reconcile net income to net cash provided by (used in) operating activities: |  |             |
| Loan loss provision recapture   | (1,700)                                | (2,532)     |
| Provision for losses on REOs  | 121                                    | 394         |
| Depreciation  | 177                                    | 180         |
| Net amortization of deferred loan origination costs   | 214                                    | 171         |
| Net amortization of premiums on mortgage-backed securities                                  | 42                                     | 41          |
| Amortization of investment in affordable housing limited partnership                        | 144                                    | 144         |
| Stock-based compensation expense  | -                                      | 11          |
| Earnings on bank owned life insurance   | (46)                                   | (49)        |
| Originations of for-sale loans receivable   | (57,635)                               | -           |
| Proceeds from for-sale loans receivable   | 45,518                                 | -           |
| Net gain on sale of loans   | (1,252)                                | -           |
| Net gain on sale of REOs  | (75)                                   | (2)         |
| Amortization of deferred gain on debt restructuring   | -                                      | (111)       |
| Stock-based compensation non-employee   | -                                      | 25          |
| Net change in accrued interest receivable   | 253                                    | (66)        |
| Net change in other assets  | 642                                    | 56          |
| Net change in advance payments by borrowers for taxes and insurance                         | 421                                    | 529         |
| Net change in accrued expenses and other liabilities  | 679                                    | 555         |
| Net cash provided by (used in) operating activities   | (9,067)                                | 1,159       |
| <b>Cash flows from investing activities:</b>  |  |             |
| Net change in loans receivable held for investment  | (12,374)                               | (34,635)    |
| Proceeds from sales of loans receivable transferred to held-for-sale                        | 95,923                                 | -           |
| Principal repayments on loans receivable transferred to held-for-sale                       | 544                                    | -           |
| Available-for-sale securities:  |  |             |
| Prepayments and amortizations   | 2,197                                  | 1,960       |
| Purchases   | -                                      | (10,463)    |
| Proceeds from sales of REO  | 2,321                                  | 2,505       |
| Redemption of FHLB stock  | 1,869                                  | -           |
| Purchase of FHLB stock  | (188)                                  | -           |
| Additions to office properties and equipment  | (88)                                   | (213)       |
| Net cash provided by (used in) investing activities   | 90,204                                 | (40,846)    |
| <b>Cash flows from financing activities:</b>  |  |             |
| Net change in deposits  | 57,054                                 | 2,687       |
| Proceeds from FHLB advances   | 21,000                                 | 8,000       |
| Repayments of FHLB advances   | (29,500)                               | (8,000)     |
| Net cash provided by financing activities   | 48,554                                 | 2,687       |
| Net change in cash and cash equivalents   | 129,691                                | (37,000)    |
| Cash and cash equivalents at beginning of the period  | 20,790                                 | 58,196      |
| Cash and cash equivalents at end of the period  | \$ 150,481                             | \$ 21,196   |
| <b>Supplemental disclosures of cash flow information:</b>                                   |  |             |
| Cash paid for interest  | \$ 2,866                               | \$ 2,801    |
| Cash paid for income taxes  | 2                                      | 3           |



**Supplemental disclosures of non-cash investing and financing activities:**

|   |           |          |
|---|-----------|----------|
| Transfers of loans receivable held for investment to REO                            | \$ 843    | \$ 3,313 |
| Transfers of loans receivable held for investment to loans receivable held for sale | \$ 91,562 | \$ -     |
| Issuance of common stock for services   | \$ -      | \$ 25    |

*See accompanying notes to unaudited consolidated financial statements.*

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**BROADWAY FINANCIAL CORPORATION AND SUBSIDIARY**

**Notes to Unaudited Consolidated Financial Statements**

**September 30, 2015**

**NOTE (1) Basis of Financial Statement Presentation**

The accompanying unaudited consolidated financial statements include Broadway Financial Corporation (the Company) and its wholly owned subsidiary, Broadway Federal Bank, f.s.b. (the Bank). Also included in the unaudited consolidated financial statements is Broadway Service Corporation, a wholly owned subsidiary of the Bank. All significant intercompany balances and transactions have been eliminated in consolidation.

The unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions for quarterly reports on Form 10-Q. These unaudited consolidated financial statements do not include all disclosures associated with the Company's consolidated annual financial statements included in its Annual Report on Form 10-K for the year ended December 31, 2014 and, accordingly, should be read in conjunction with such audited consolidated financial statements. In the opinion of management, all adjustments (all of which are normal and recurring in nature) considered necessary for a fair presentation have been included. Operating results for the three and nine months ended September 30, 2015 are not necessarily indicative of the results that may be expected for the year ending December 31, 2015.

Some items in the consolidated financial statements for the prior period were reclassified to conform to the current presentation. Reclassifications had no effect on prior period consolidated net income or loss or stockholders' equity.

*Recent Accounting Pronouncements*

In August 2014, the FASB issued ASU 2014-15, Presentation of Financial Statements - Going Concern (Subtopic 205-40) - Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern. ASU 2014-15 incorporates into U.S. GAAP a requirement that management complete a going concern evaluation similar to that performed by an entity's external auditor. Under the new guidance, management will be required to perform interim and annual assessments of an entity's ability to continue as a going concern within one year of the date of issuance of the entity's financial statements. Further, an entity must provide certain disclosures if there is substantial doubt about the entity's ability to continue as a going concern. ASU 2014-15 is effective for annual periods ending after December 15, 2016, and interim periods thereafter. Early adoption is permitted. Adoption of this standard is not expected to have a material impact on the Company's consolidated financial statements.

In January 2015, the FASB issued ASU 2015-01, Income Statement - Extraordinary and Unusual Items (Subtopic 225-20) - Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Items. ASU 2015-01 eliminates from U.S. GAAP the concept of

extraordinary items, which, among other things, required an entity to segregate extraordinary items considered to be unusual and infrequent from the results of ordinary operations and show the item separately in the income statement, net of tax, after income from continuing operations. ASU 2015-01 is effective for annual periods ending after December 15, 2015, and interim periods thereafter. Early adoption is permitted. Adoption of this standard is not expected to have a material impact on the Company's consolidated financial statements.

In April 2015, the FASB issued ASU 2015-03, *Simplifying the Presentation of Debt Issuance Costs*. Under ASU 2015-03, the Company will present debt issuance costs in the balance sheet as a reduction from the related debt liability rather than as an asset. Amortization of such costs will continue to be reported as interest expense. ASU 2015-03 is effective for annual periods ending after December 15, 2015, and interim periods thereafter. Early adoption is permitted. Retrospective adoption is required. Adoption of this standard is not expected to have a material impact on the Company's consolidated financial statements.

Table of Contents**BROADWAY FINANCIAL CORPORATION AND SUBSIDIARY****Notes to Unaudited Consolidated Financial Statements (continued)****NOTE (2) Earnings Per Share of Common Stock**

Basic earnings per share of common stock is computed by dividing income available to common stockholders by the weighted average number of shares of common stock outstanding for the period. Diluted earnings per share of common stock is computed by dividing income available to common stockholders by the weighted average number of shares of common stock outstanding for the period, increased for the dilutive effect of common stock equivalents.

The following table shows how the Company computed basic and diluted earnings per share of common stock for the three and nine months ended September 30, 2015 and 2014:

|   | For the three months ended<br>September 30,        |            | For the nine months ended<br>September 30, |            |
|---|--|------------|--|------------|
|   | 2015   | 2014       | 2015                                       | 2014       |
|   | (Dollars in thousands, except share and per share) |            |  |            |
| <b>Basic</b>  |  |            |  |            |
| Net income  | \$ 979   | \$ 765     | \$ 3,430                                   | \$ 1,813   |
| Weighted average common shares outstanding                  | 29,076,708   | 20,247,159 | 29,076,708                                 | 20,238,679 |
| Earnings per common share - basic                           | \$ 0.03  | \$ 0.04    | \$ 0.12                                    | \$ 0.09    |
| <b>Diluted</b>  |  |            |  |            |
| Net income  | \$ 979   | \$ 765     | \$ 3,430                                   | \$ 1,813   |
| Weighted average common shares outstanding                  | 29,076,708   | 20,247,159 | 29,076,708                                 | 20,238,679 |
| Add: dilutive effects of assumed exercises of stock options | -  | -          | -  | -          |
| Weighted average common shares - fully dilutive             | 29,076,708   | 20,247,159 | 29,076,708                                 | 20,238,679 |
| Earnings per common share - diluted                         | \$ 0.03  | \$ 0.04    | \$ 0.12                                    | \$ 0.09    |

Stock options for 93,750 shares of common stock were not considered in computing diluted earnings per common share for the three and nine months ended September 30, 2015 and 2014, respectively, because they were anti-dilutive.

Table of Contents**BROADWAY FINANCIAL CORPORATION AND SUBSIDIARY****Notes to Unaudited Consolidated Financial Statements (continued)****NOTE (3) Securities**

The following table summarizes the amortized cost and fair value of the available-for-sale investment securities portfolios at September 30, 2015 and December 31, 2014 and the corresponding amounts of unrealized gains and losses which are recognized in accumulated other comprehensive income (loss):

|                                     | Amortized Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Fair Value |
|-------------------------------------|----------------|------------------------------|-------------------------------|------------|
|                                     | (In thousands) |                              |                               |            |
| <b>September 30, 2015:</b>          |                |                              |                               |            |
| Residential mortgage-backed         | \$ 12,329      | \$ 471                       | \$ -                          | \$ 12,800  |
| U.S. Government and federal agency  | 1,942          | 54                           | -                             | 1,996      |
| Total available-for-sale securities | \$ 14,271      | \$ 525                       | \$ -                          | \$ 14,796  |
| <b>December 31, 2014:</b>           |                |                              |                               |            |
| Residential mortgage-backed         | \$ 14,578      | \$ 540                       | \$ -                          | \$ 15,118  |
| U.S. Government and federal agency  | 1,932          | 25                           | -                             | 1,957      |
| Total available-for-sale securities | \$ 16,510      | \$ 565                       | \$ -                          | \$ 17,075  |

At September 30, 2015, the Bank's investment portfolio had an estimated remaining life of 4.3 years. The amortized cost and fair value of the investment securities portfolio are shown by contractual maturity at September 30, 2015. Expected maturities may differ from contractual maturities if borrowers have the right to call or prepay obligations with or without call or prepayment penalties. Securities not due at a single maturity date, primarily residential mortgage-backed securities, are shown separately.

| Maturity                    | Available-for-Sale |            |
|-----------------------------|--------------------|------------|
|                             | Amortized Cost     | Fair Value |
|                             | (In thousands)     |            |
| Within one year             | \$ -               | \$ -       |
| One to five years           | 1,942              | 1,996      |
| Five to ten years           | -                  | -          |
| Beyond ten years            | -                  | -          |
| Residential mortgage-backed | 12,329             | 12,800     |
| Total                       | \$ 14,271          | \$ 14,796  |

At September 30, 2015 and December 31, 2014, securities pledged to secure public deposits had a carrying amount of \$731 thousand and \$1.2 million, respectively. At September 30, 2015 and December 31, 2014, there were no holdings of securities by any one issuer, other than the U.S. Government and its agencies, in an amount greater than 10% of stockholders' equity.

There were no sales of securities during the three and nine months ended September 30, 2015 and 2014.

**NOTE (4) Loans Receivable Held for Sale**

Loans receivable held for sale totaled \$27.9 million and \$19.5 million at September 30, 2015 and December 31, 2014, respectively, and consisted of multi-family loans. As part of the Bank's loan concentration risk management program, \$91.6 million of multi-family loans were transferred from the held-for-investment portfolio to the held-for-sale portfolio during the first nine months of 2015. The Bank also allocated \$57.6 million, or 57%, of its total loan originations during the period as held-for-sale and completed sales of \$140.2 million of multi-family loans during the nine months ended September 30, 2015 for a net gain of \$1.3 million.

Table of Contents**BROADWAY FINANCIAL CORPORATION AND SUBSIDIARY****Notes to Unaudited Consolidated Financial Statements (continued)****NOTE (5) Loans Receivable Held for Investment**

Loans at September 30, 2015 and December 31, 2014 were as follows:

|  | September 30, 2015 | December 31, 2014 |
|--|--------------------|-------------------|
|  | (In thousands)     |                   |
| Real estate:   |                    |                   |
| Single family  | \$ 31,740          | \$ 39,792         |
| Multi-family   | 110,577            | 171,792           |
| Commercial real estate   | 12,304             | 16,722            |
| Church   | 48,952             | 54,599            |
| Construction   | 351                | 387               |
| Commercial other   | 250                | 262               |
| Consumer   | 11                 | 9                 |
| Gross loans receivable before deferred loan costs and premiums | 204,185            | 283,563           |
| Unamortized net deferred loan costs and premiums               | 641                | 1,545             |
| Gross loans receivable   | 204,826            | 285,108           |
| Allowance for loan losses                                      | (6,728)            | (8,465)           |
| Loans receivable, net  | \$ 198,098         | \$ 276,643        |

The following tables present the activity in the allowance for loan losses by loan type for the three and nine months ended September 30, 2015 and 2014:

|  | Three Months Ended September 30, 2015 |                  |  |          |              |                       |          |      | Total    |
|--|---------------------------------------|------------------|--|----------|--------------|-----------------------|----------|------|----------|
|  | Single<br>family                      | Multi-<br>family | Real Estate<br>Commercial<br>real estate | Church   | Construction | Commercial<br>- other | Consumer |      |          |
|  | (In thousands)                        |                  |  |          |              |                       |          |      |          |
| Beginning balance                        | \$ 1,150                              | \$ 1,845         | \$ 404                                   | \$ 3,508 | \$ 4         | \$ 12                 | \$ -     | \$ - | \$ 6,923 |
| Provision for (recapture of) loan losses | (189)                                 | 135              | 75                                       | (221)    | -            | -                     | -        | -    | (200)    |
| Recoveries                               | -                                     | -                | -  | 5        | -            | -                     | -        | -    | 5        |
| Loans charged off                        | -                                     | -                | -  | -        | -            | -                     | -        | -    | -        |
| Ending balance                           | \$ 961                                | \$ 1,980         | \$ 479                                   | \$ 3,292 | \$ 4         | \$ 12                 | \$ -     | \$ - | \$ 6,728 |

|                   | Nine Months Ended September 30, 2015 |                  |  |          |              |                       |          |      | Total    |
|-------------------|--------------------------------------|------------------|--|----------|--------------|-----------------------|----------|------|----------|
|                   | Single<br>family                     | Multi-<br>family | Real Estate<br>Commercial<br>real estate | Church   | Construction | Commercial<br>- other | Consumer |      |          |
|                   | (In thousands)                       |                  |  |          |              |                       |          |      |          |
| Beginning balance | \$ 1,174                             | \$ 2,726         | \$ 496                                   | \$ 4,047 | \$ 7         | \$ 12                 | \$ 3     | \$ - | \$ 8,465 |

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|  |        |          |        |          |      |       |      |          |
|--|--------|----------|--------|----------|------|-------|------|----------|
| Provision for (recapture of) loan losses | (210)  | (746)    | (17)   | (721)    | (3)  | -     | (3)  | (1,700)  |
| Recoveries                               | -      | -        | -      | 16       | -    | -     | -    | 16       |
| Loans charged off                        | (3)    | -        | -      | (50)     | -    | -     | -    | (53)     |
| Ending balance                           | \$ 961 | \$ 1,980 | \$ 479 | \$ 3,292 | \$ 4 | \$ 12 | \$ - | \$ 6,728 |



Table of Contents**BROADWAY FINANCIAL CORPORATION AND SUBSIDIARY****Notes to Unaudited Consolidated Financial Statements (continued)****Three Months Ended September 30, 2014**

|   | Single<br>family | Multi-<br>family | Real Estate<br>Commercial<br>real estate | Church   | Construction | Commercial<br>- other | Consumer | Total    |
|---|------------------|------------------|--|----------|--------------|-----------------------|----------|----------|
|   | (In thousands)   |                  |  |          |              |                       |          |          |
| Beginning balance                           | \$ 1,849         | \$ 2,304         | \$ 1,081                                 | \$ 4,112 | \$ 7         | \$ 19                 | \$ 4     | \$ 9,376 |
| Provision for (recapture<br>of) loan losses | (465)            | 327              | (96)                                     | (724)    | -            | 10                    | (2)      | (950)    |
| Recoveries                                  | -                | -                | -  | 682      | -            | -                     | -        | 682      |
| Loans charged off                           | (40)             | -                | -  | (1)      | -            | -                     | -        | (41)     |
| Ending balance                              | \$ 1,344         | \$ 2,631         | \$ 985                                   | \$ 4,069 | \$ 7         | \$ 29                 | \$ 2     | \$ 9,067 |

**Nine Months Ended September 30, 2014**

|   | Single<br>family | Multi-<br>family | Real Estate<br>Commercial<br>real estate | Church   | Construction | Commercial<br>- other | Consumer | Total     |
|---|------------------|------------------|--|----------|--------------|-----------------------|----------|-----------|
|   | (In thousands)   |                  |  |          |              |                       |          |           |
| Beginning balance                           | \$ 1,930         | \$ 1,726         | \$ 1,473                                 | \$ 4,949 | \$ 7         | \$ 55                 | \$ 6     | \$ 10,146 |
| Provision for (recapture<br>of) loan losses | (455)            | 905              | (479)                                    | (1,408)  | -            | (1,091)               | (4)      | (2,532)   |
| Recoveries                                  | 2                | -                | -  | 851      | -            | 1,083                 | -        | 1,936     |
| Loans charged off                           | (133)            | -                | (9)                                      | (323)    | -            | (18)                  | -        | (483)     |
| Ending balance                              | \$ 1,344         | \$ 2,631         | \$ 985                                   | \$ 4,069 | \$ 7         | \$ 29                 | \$ 2     | \$ 9,067  |

The following tables present the balance in the allowance for loan losses and the recorded investment (unpaid contractual principal balance less charge-offs, less interest applied to principal, plus unamortized deferred costs and premiums) by loan type and based on impairment method as of September 30, 2015 and December 31, 2014:

**September 30, 2015**

|  | Single<br>family | Multi-<br>family | Real Estate<br>Commercial<br>real estate | Church    | Construction | Commercial<br>- other | Consumer | Total      |
|--|------------------|------------------|--|-----------|--------------|-----------------------|----------|------------|
|  | (In thousands)   |                  |  |           |              |                       |          |            |
| <b>Allowance for loan losses:</b>                  |                  |                  |  |           |              |                       |          |            |
| Ending allowance balance<br>attributable to loans: |                  |                  |  |           |              |                       |          |            |
| Individually evaluated for<br>impairment           | \$ 135           | \$ 2             | \$ 95                                    | \$ 1,084  | \$ -         | \$ 10                 | \$ -     | \$ 1,326   |
| Collectively evaluated for<br>impairment           | 826              | 1,978            | 384                                      | 2,208     | 4            | 2                     | -        | 5,402      |
| Total ending allowance<br>balance                  | \$ 961           | \$ 1,980         | \$ 479                                   | \$ 3,292  | \$ 4         | \$ 12                 | \$ -     | \$ 6,728   |
| <b>Loans:</b>                                      |                  |                  |  |           |              |                       |          |            |
| Loans individually evaluated<br>for impairment     | \$ 1,142         | \$ 1,456         | \$ 2,744                                 | \$ 13,368 | \$ -         | \$ 67                 | \$ -     | \$ 18,777  |
| Loans collectively evaluated<br>for impairment     | 30,792           | 110,055          | 9,566                                    | 35,091    | 351          | 183                   | 11       | 186,049    |
| Total ending loans balance                         | \$ 31,934        | \$ 111,511       | \$ 12,310                                | \$ 48,459 | \$ 351       | \$ 250                | \$ 11    | \$ 204,826 |



Table of Contents**BROADWAY FINANCIAL CORPORATION AND SUBSIDIARY****Notes to Unaudited Consolidated Financial Statements (continued)**

|   | December 31, 2014 |              |                                    |           |              |                    |          | Total      |
|---|-------------------|--------------|------------------------------------|-----------|--------------|--------------------|----------|------------|
|   | Single family     | Multi-family | Real Estate Commercial real estate | Church    | Construction | Commercial - other | Consumer |            |
|   | (In thousands)    |              |                                    |           |              |                    |          |            |
| <b>Allowance for loan losses:</b>               |                   |              |                                    |           |              |                    |          |            |
| Ending allowance balance attributable to loans: |                   |              |                                    |           |              |                    |          |            |
| Individually evaluated for impairment           | \$ 132            | \$ 115       | \$ 161                             | \$ 1,088  | \$ -         | \$ 10              | \$ -     | \$ 1,506   |
| Collectively evaluated for impairment           | 1,042             | 2,611        | 335                                | 2,959     | 7            | 2                  | 3        | 6,959      |
| Total ending allowance balance                  | \$ 1,174          | \$ 2,726     | \$ 496                             | \$ 4,047  | \$ 7         | \$ 12              | \$ 3     | \$ 8,465   |
| <b>Loans:</b>                                   |                   |              |                                    |           |              |                    |          |            |
| Loans individually evaluated for impairment     | \$ 1,414          | \$ 2,765     | \$ 4,636                           | \$ 14,602 | \$ -         | \$ 102             | \$ -     | \$ 23,519  |
| Loans collectively evaluated for impairment     | 38,641            | 170,785      | 12,083                             | 39,525    | 387          | 159                | 9        | 261,589    |
| Total ending loans balance                      | \$ 40,055         | \$ 173,550   | \$ 16,719                          | \$ 54,127 | \$ 387       | \$ 261             | \$ 9     | \$ 285,108 |

The following table presents information related to loans individually evaluated for impairment by loan type as of September 30, 2015 and December 31, 2014:

|  | September 30, 2015       |                     |                                     | December 31, 2014        |                     |                                     |
|--|--------------------------|---------------------|-------------------------------------|--------------------------|---------------------|-------------------------------------|
|  | Unpaid Principal Balance | Recorded Investment | Allowance for Loan Losses Allocated | Unpaid Principal Balance | Recorded Investment | Allowance for Loan Losses Allocated |
|  | (In thousands)           |                     |                                     |                          |                     |                                     |
| <b>With no related allowance recorded:</b> |                          |                     |                                     |                          |                     |                                     |
| Single family                              | \$ 1,233                 | \$ 476              | \$ -                                | \$ 1,448                 | \$ 736              | \$ -                                |
| Multi-family                               | 914                      | 790                 | -                                   | 1,384                    | 1,263               | -                                   |
| Commercial real estate                     | 1,855                    | 1,039               | -                                   | 4,836                    | 1,174               | -                                   |
| Church                                     | 6,038                    | 4,029               | -                                   | 6,234                    | 4,350               | -                                   |
| Commercial - other                         | -                        | -                   | -                                   | 34                       | 34                  | -                                   |
| <b>With an allowance recorded:</b>         |                          |                     |                                     |                          |                     |                                     |
| Single family                              | 666                      | 666                 | 135                                 | 678                      | 678                 | 132                                 |
| Multi-family                               | 666                      | 666                 | 2                                   | 1,541                    | 1,502               | 115                                 |
| Commercial real estate                     | 1,705                    | 1,705               | 95                                  | 3,473                    | 3,462               | 161                                 |
| Church                                     | 9,737                    | 9,339               | 1,084                               | 10,751                   | 10,252              | 1,088                               |
| Commercial -other                          | 67                       | 67                  | 10                                  | 68                       | 68                  | 10                                  |
| Total                                      | \$ 22,881                | \$ 18,777           | \$ 1,326                            | \$ 30,447                | \$ 23,519           | \$ 1,506                            |

The recorded investment in loans excludes accrued interest receivable due to immateriality. For purposes of this disclosure, the unpaid principal balance is not reduced for net charge-offs.

Table of Contents**BROADWAY FINANCIAL CORPORATION AND SUBSIDIARY****Notes to Unaudited Consolidated Financial Statements (continued)**

The following tables present the monthly average of loans individually evaluated for impairment by loan type and the related interest income for the three and nine months ended September 30, 2015 and 2014.

|                        | <b>Three Months Ended September 30, 2015</b> |  | <b>Nine Months Ended September 30, 2015</b> |  |
|------------------------|--|--|---|--|
|                        | <b>Average Recorded Investment</b>           | <b>Cash Basis Interest Income Recognized</b> | <b>Average Recorded Investment</b>          | <b>Cash Basis Interest Income Recognized</b> |
|                        | (In thousands)                               |  |   |  |
| Single family          | \$ 1,239                                     | \$ 42  | \$ 1,317                                    | \$ 57  |
| Multi-family           | 1,461  | 10   | 2,051                                       | 125  |
| Commercial real estate | 2,766  | 56   | 3,375                                       | 217  |
| Church                 | 13,410                                       | 174  | 13,841                                      | 460  |
| Commercial -other      | 73   | 1  | 83  | 4  |
| <b>Total</b>           | <b>\$ 18,949</b>                             | <b>\$ 283</b>                                | <b>\$ 20,667</b>                            | <b>\$ 863</b>                                |

  

|                        | <b>Three Months Ended September 30, 2014</b> |  | <b>Nine Months Ended September 30, 2014</b> |  |
|------------------------|--|--|---|--|
|                        | <b>Average Recorded Investment</b>           | <b>Cash Basis Interest Income Recognized</b> | <b>Average Recorded Investment</b>          | <b>Cash Basis Interest Income Recognized</b> |
|                        | (In thousands)                               |  |   |  |
| Single family          | \$ 2,038                                     | \$ 25  | \$ 2,601                                    | \$ 60  |
| Multi-family           | 3,250  | 20   | 3,554                                       | 66   |
| Commercial real estate | 4,716  | 106  | 4,792                                       | 295  |
| Church                 | 16,419                                       | 158  | 17,882                                      | 491  |
| Commercial -other      | 117  | 3  | 130   | 8  |
| <b>Total</b>           | <b>\$ 26,540</b>                             | <b>\$ 312</b>                                | <b>\$ 28,959</b>                            | <b>\$ 920</b>                                |

Cash-basis interest income recognized represents cash received for interest payments on accruing impaired loans. Interest payments collected on non-accrual loans are characterized as payments of principal rather than payments of the outstanding accrued interest on the loans until the remaining principal on the non-accrual loans is considered to be fully collectible. Foregone interest income that would have been recognized had loans performed in accordance with their original terms amounted to \$147 thousand and \$337 thousand for the three months ended September 30, 2015 and 2014, respectively, and \$597 thousand and \$1.2 million for the nine months ended September 30, 2015 and 2014, respectively, and were not included in the consolidated results of operations.

The following tables present the aging of the recorded investment in past due loans as of September 30, 2015 and December 31, 2014 by loan type:

September 30, 2015

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|  | 30-59<br>Days<br>Past Due | 60-89<br>Days<br>Past Due | Greater than<br>90 Days<br>Past Due<br>(In thousands) | Total<br>Past Due | Current    |
|--|---------------------------|---------------------------|---|-------------------|------------|
| <b>Loans receivable held for investment:</b> |                           |                           |   |                   |            |
| Single family                                | \$ 79                     | \$ -                      | \$ -  | \$ 79             | \$ 31,855  |
| Multi-family                                 | 333                       | -                         | 457   | 790               | 110,721    |
| Commercial real estate                       | -                         | -                         | -   | -                 | 12,310     |
| Church                                       | -                         | -                         | 395   | 395               | 48,064     |
| Construction                                 | -                         | -                         | -   | -                 | 351        |
| Commercial - other                           | -                         | -                         | -   | -                 | 250        |
| Consumer                                     | -                         | -                         | -   | -                 | 11         |
| Total  | \$ 412                    | \$ -                      | \$ 852  | \$ 1,264          | \$ 203,562 |

Table of Contents**BROADWAY FINANCIAL CORPORATION AND SUBSIDIARY****Notes to Unaudited Consolidated Financial Statements (continued)**

|  | <b>30-59<br/>Days<br/>Past Due</b> | <b>60-89<br/>Days<br/>Past Due</b> | <b>December 31, 2014<br/>Greater than<br/>90 Days<br/>Past Due<br/>(In thousands)</b> | <b>Total<br/>Past Due</b> | <b>Current</b> |
|--|------------------------------------|------------------------------------|---|---------------------------|----------------|
| <b>Loans receivable held for investment:</b> |                                    |                                    |   |                           |                |
| Single family                                | \$ -                               | \$ -                               | \$ -  | \$ -                      | \$ 40,055      |
| Multi-family                                 | 455                                | -                                  | -   | 455                       | 173,095        |
| Commercial real estate                       | 856                                | -                                  | -   | 856                       | 15,863         |
| Church                                       | -                                  | 180                                | 987   | 1,167                     | 52,960         |
| Construction                                 | -                                  | -                                  | -   | -                         | 387            |
| Commercial - other                           | 34                                 | -                                  | -   | 34                        | 227            |
| Consumer                                     | -                                  | -                                  | -   | -                         | 9              |
| Total  | \$ 1,345                           | \$ 180                             | \$ 987  | \$ 2,512                  | \$ 282,596     |

The following table presents the recorded investment in non-accrual loans by loan type as of September 30, 2015 and December 31, 2014:

|  | <b>September 30, 2015</b> | <b>December 31, 2014</b> |
|--|---------------------------|--------------------------|
|  | <b>(In thousands)</b>     |                          |
| <b>Loans receivable held for investment:</b> |                           |                          |
| Single family                                | \$ 476                    | \$ 736                   |
| Multi-family                                 | 790                       | 1,618                    |
| Commercial real estate                       | 1,039                     | 1,174                    |
| Church                                       | 3,372                     | 5,232                    |
| Commercial - other                           | 67                        | 102                      |
| Total non-accrual loans                      | \$ 5,744                  | \$ 8,862                 |

There were no loans 90 days or more delinquent that were accruing interest as of September 30, 2015 or December 31, 2014.

**Troubled Debt Restructurings**

At September 30, 2015, loans classified as troubled debt restructurings ( TDRs ) totaled \$17.0 million, of which \$4.0 million were included in non-accrual loans and \$13.0 million were on accrual status. At December 31, 2014, loans classified as TDRs totaled \$20.2 million, of which \$5.5 million were included in non-accrual loans and \$14.7 million were on accrual status. The Company has allocated \$1.3 million of specific reserves for accruing TDRs as of September 30, 2015 and December 31, 2014. TDRs on accrual status are comprised of loans that were accruing at the time of restructuring or loans that have complied with the terms of their restructured agreements for a satisfactory period of time, and for which the Bank anticipates full repayment of both principal and interest. TDRs that are on non-accrual status can be returned to accrual status after a period of sustained performance, generally determined to be six months of timely payments as modified. A well-documented credit analysis that supports a return to accrual status based on the borrower's financial condition and prospects for repayment under the revised

terms is also required. As of September 30, 2015 and December 31, 2014, the Company had no commitment to lend additional amounts to customers with outstanding loans that are classified as TDRs. No loans were modified during the three and nine months ended September 30, 2015 and 2014.



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**BROADWAY FINANCIAL CORPORATION AND SUBSIDIARY**

**Notes to Unaudited Consolidated Financial Statements (continued)**

**Credit Quality Indicators**

The Company categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. For single family residential, consumer and other smaller balance homogenous loans, a credit grade is established at inception, and generally only adjusted based on performance. Information about payment status is disclosed elsewhere herein. The Company analyzes all other loans individually by classifying the loans as to credit risk. This analysis is performed at least on a quarterly basis. The Company uses the following definitions for risk ratings:

- **Watch.** Loans classified as watch exhibit weaknesses that could threaten the current net worth and paying capacity of the obligors. Watch graded loans are generally performing and are not more than 59 days past due. A watch rating is used when a material deficiency exists but correction is anticipated within an acceptable time frame.
- **Special Mention.** Loans classified as special mention have a potential weakness that deserves management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or of the institution's credit position at some future date.
- **Substandard.** Loans classified as substandard are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected.
- **Doubtful.** Loans classified as doubtful have all the weaknesses inherent in those classified as 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.
- **Loss.** Loans classified as loss are considered uncollectible and of such little value that to continue to carry the loan as an active asset is no longer warranted.

Loans not meeting the criteria above that are analyzed individually as part of the above described process are considered to be pass rated loans. Pass rated loans are generally well protected by the current net worth and paying capacity of the obligor or by the value of the underlying collateral. Pass rated loans are not more than 59 days past due and are generally performing in accordance with the loan terms. Based on the most recent analysis performed, the risk category of loans by loan type as of September 30, 2015 and December 31, 2014 is as follows:

|                        | <b>September 30, 2015</b> |               |                        |                    |                 |             |
|------------------------|---------------------------|---------------|------------------------|--------------------|-----------------|-------------|
|                        | <b>Pass</b>               | <b>Watch</b>  | <b>Special Mention</b> | <b>Substandard</b> | <b>Doubtful</b> | <b>Loss</b> |
|                        | <b>(In thousands)</b>     |               |                        |                    |                 |             |
| Single family          | \$ 28,811                 | \$ -          | \$ 2,647               | \$ 476             | \$ -            | \$ -        |
| Multi-family           | 108,895                   | -             | 646                    | 1,970              | -               | -           |
| Commercial real estate | 8,915                     | -             | -                      | 3,395              | -               | -           |
| Church                 | 37,194                    | 779           | 1,437                  | 9,049              | -               | -           |
| Construction           | 351                       | -             | -                      | -                  | -               | -           |
| Commercial - other     | 183                       | -             | -                      | 67                 | -               | -           |
| Consumer               | 11                        | -             | -                      | -                  | -               | -           |
| <b>Total</b>           | <b>\$ 184,360</b>         | <b>\$ 779</b> | <b>\$ 4,730</b>        | <b>\$ 14,957</b>   | <b>\$ -</b>     | <b>\$ -</b> |

Table of Contents**BROADWAY FINANCIAL CORPORATION AND SUBSIDIARY****Notes to Unaudited Consolidated Financial Statements (continued)**

|                        | <b>December 31, 2014</b> |              |                        |                    |                 |             |
|------------------------|--------------------------|--------------|------------------------|--------------------|-----------------|-------------|
|                        | <b>Pass</b>              | <b>Watch</b> | <b>Special Mention</b> | <b>Substandard</b> | <b>Doubtful</b> | <b>Loss</b> |
|                        | <b>(In thousands)</b>    |              |                        |                    |                 |             |
| Single family          | \$ 35,850                | \$ -         | \$ 3,465               | \$ 740             | \$ -            | \$ -        |
| Multi-family           | 170,700                  | -            | 613                    | 2,237              | -               | -           |
| Commercial real estate | 13,218                   | -            | 284                    | 3,217              | -               | -           |
| Church                 | 41,716                   | -            | 2,202                  | 10,209             | -               | -           |
| Construction           | 387                      | -            | -                      | -                  | -               | -           |
| Commercial - other     | 159                      | -            | -                      | 102                | -               | -           |
| Consumer               | 9                        | -            | -                      | -                  | -               | -           |
| Total                  | \$ 262,039               | \$ -         | \$ 6,564               | \$ 16,505          | \$ -            | \$ -        |

**NOTE (6) Junior Subordinated Debentures**

On March 17, 2004, the Company issued \$6.0 million of Floating Rate Junior Subordinated Debentures (the Debentures) in a private placement to a trust that was capitalized to purchase subordinated debt and preferred stock of multiple community banks. Interest on the Debentures is payable quarterly at a rate per annum equal to the 3-Month LIBOR plus 2.54%. The interest rate is determined as of each March 17, June 17, September 17, and December 17, and was 2.87% at September 30, 2015. On October 16, 2014, the Company made payments of \$900 thousand of principal on Debentures, executed a Supplemental Indenture for the Debentures that extended the maturity of the Debentures to March 17, 2024, and modified the payment terms of the remaining \$5.1 million principal amount thereof. The modified terms of the Debentures require quarterly payments of interest only for the next five years at the original rate of 3-Month LIBOR plus 2.54%. Starting in June 2019, the Company will be required to make quarterly payments of equal amounts of principal, plus interest, until the Debentures are fully amortized on March 17, 2024. The obligation of the Company to make the payments of principal and interest shall be subject to receipt by the Company of any required regulatory approval or non-objection. The Debentures may be called for redemption at any time by the Company.

**NOTE (7) 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.

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Level 2: Significant 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 fair value:

The fair values of securities available-for-sale are determined by obtaining quoted prices on nationally recognized securities exchanges (Level 1 inputs) or matrix pricing, which is a mathematical technique 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 inputs).

Table of Contents**BROADWAY FINANCIAL CORPORATION AND SUBSIDIARY****Notes to Unaudited Consolidated Financial Statements (continued)**

The fair value of impaired loans that are collateral dependent is generally based upon the fair value of the collateral which is obtained from 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. Impaired loans are evaluated on a quarterly basis for additional impairment and adjusted accordingly.

Assets acquired through or by transfer in lieu of loan 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 the lower of cost or fair value less estimated costs to sell. Fair value is commonly based on recent real estate appraisals which are updated every nine months. 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. Real estate owned properties are evaluated on a quarterly basis for additional impairment and adjusted accordingly.

Appraisals for collateral-dependent impaired loans and real estate owned are performed by certified general appraisers (for commercial properties) or certified residential appraisers (for residential properties) whose qualifications and licenses have been reviewed and verified by the Company. Once received, an independent third-party licensed appraiser reviews the appraisals for accuracy and reasonableness, reviewing the assumptions and approaches utilized in the appraisal as well as the overall resulting fair value in comparison with independent data sources such as recent market data or industry-wide statistics.

**Assets Measured on a Recurring Basis**

Assets measured at fair value on a recurring basis are summarized below:

|   | Fair Value Measurements at September 30, 2015                                 |   |  | Total     |
|---|---|---|--|-----------|
|   | Quoted Prices<br>in Active<br>Markets for<br>Identical<br>Assets<br>(Level 1) | Significant<br>Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) |           |
|   | (In thousands)  |   |  |           |
| <b>Assets:</b>  |   |   |  |           |
| Securities available-for-sale - residential mortgage-backed | \$ -  | \$ 12,800   | \$ -   | \$ 12,800 |
|   | 1,996   | -   | -  | 1,996     |

Securities available-for-sale - U.S. Government and  
federal agency

Table of Contents**BROADWAY FINANCIAL CORPORATION AND SUBSIDIARY****Notes to Unaudited Consolidated Financial Statements (continued)**

|  | Fair Value Measurements at December 31, 2014                                  |   |  | Total     |
|--|---|---|--|-----------|
|  | Quoted Prices<br>in Active<br>Markets for<br>Identical<br>Assets<br>(Level 1) | Significant<br>Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) |           |
|  | (In thousands)  |   |  |           |
| <b>Assets:</b>   |   |   |  |           |
| Securities available-for-sale - residential mortgage-backed        | \$ -  | \$ 15,118   | \$ -   | \$ 15,118 |
| Securities available-for-sale - U.S. Government and federal agency | 1,957   | -   | -  | 1,957     |

There were no transfers between Level 1, Level 2, or Level 3 during the three and nine months ended September 30, 2015 and 2014.

**Assets Measured on a Non-Recurring Basis**

Assets are considered to be reflected at fair value on a non-recurring basis if the fair value measurement of the instrument does not necessarily result in a change in the amount recorded on the balance sheet. Generally, a non-recurring valuation is the result of the application of other accounting pronouncements that require assets to be assessed for impairment or recorded at the lower of cost or fair value.

The following table provides information regarding the carrying values of our assets measured at fair value on a non-recurring basis at the dates indicated. The fair value measurement for all of these assets falls within Level 3 of the fair value hierarchy.

|   | September 30, 2015 | December 31, 2014 |
|---|--------------------|-------------------|
|   | (In thousands)     |                   |
| <b>Assets:</b>                                      |                    |                   |
| Impaired loans carried at fair value of collateral: |                    |                   |
| Single family                                       | 476                | 549               |
| Multi-family  | -                  | 323               |
| Commercial real estate                              | 1,039              | 1,177             |
| Church  | 2,051              | 3,779             |
| Real estate owned:                                  |                    |                   |
| Church  | 558                | 2,082             |





Table of Contents**BROADWAY FINANCIAL CORPORATION AND SUBSIDIARY****Notes to Unaudited Consolidated Financial Statements (continued)**

The following tables present quantitative information about Level 3 fair value measurements for financial instruments measured at fair value on a non-recurring basis at September 30, 2015 and December 31, 2014:

|                   |                        | <b>September 30, 2015</b> |  |   |   |
|-------------------|------------------------|---------------------------|--|---|---|
|                   |                        | <b>Fair Value</b>         | <b>Valuation<br/>Technique(s)<br/>(Dollars in thousands)</b> | <b>Unobservable<br/>Input(s)</b>                        | <b>Range<br/>(Weighted<br/>Average)</b> |
| Impaired loans    | single family          | \$ 476                    | Sales comparison approach                                    | Adjustment for differences between the comparable sales | -6% to 1%<br>(-3%)                      |
| Impaired loans    | commercial real estate | 1,039                     | Sales comparison approach                                    | Adjustment for differences between the comparable sales | -1% to 4%<br>(0%)                       |
|                   |                        |                           | Income approach  | Capitalization rate                                     | 4.75% to 7.25%<br>(6.59%)               |
| Impaired loans    | church                 | 2,051                     | Sales comparison approach                                    | Adjustment for differences between the comparable sales | -12% to 6%<br>(0%)                      |
| Real estate owned | church                 | 558                       | Sales comparison approach                                    | Adjustment for differences between the comparable sales | 29%                                     |
|                   |                        |                           | Income approach  | Capitalization rate                                     | 6.5%                                    |

Table of Contents**BROADWAY FINANCIAL CORPORATION AND SUBSIDIARY****Notes to Unaudited Consolidated Financial Statements (continued)**

|                   |                        | <b>December 31, 2014</b> |  |   |   |
|-------------------|------------------------|--------------------------|--|---|---|
|                   |                        | <b>Fair Value</b>        | <b>Valuation<br/>Technique(s)<br/>(Dollars in thousands)</b> | <b>Unobservable<br/>Input(s)</b>                        | <b>Range<br/>(Weighted<br/>Average)</b> |
| Impaired loans    | single family          | \$ 549                   | Sales comparison approach                                    | Adjustment for differences between the comparable sales | -1% to 9%<br>(-4%)                      |
| Impaired loans    | multi-family           | 323                      | Sales comparison approach                                    | Adjustment for differences between the comparable sales | -18%                                    |
|                   |                        |                          | Income approach  | Capitalization rate                                     | 7%                                      |
| Impaired loans    | commercial real estate | 1,177                    | Sales comparison approach                                    | Adjustment for differences between the comparable sales | 0% to 1%<br>(0%)                        |
|                   |                        |                          | Income approach  | Capitalization rate                                     | 5% to 7.25%<br>(6.64%)                  |
| Impaired loans    | church                 | 3,779                    | Sales comparison approach                                    | Adjustment for differences between the comparable sales | -12% to 18%<br>(5%)                     |
|                   |                        |                          | Income approach  | Capitalization rate                                     | 6%                                      |
| Real estate owned | church                 | 2,082                    | Sales comparison approach                                    | Adjustment for differences between the comparable sales | -1% to 2%<br>(0%)                       |

Table of Contents**BROADWAY FINANCIAL CORPORATION AND SUBSIDIARY****Notes to Unaudited Consolidated Financial Statements (continued)****Fair Values of Financial Instruments**

The carrying amounts and estimated fair values of financial instruments, at September 30, 2015 and December 31, 2014 were as follows:

**Fair Value Measurements at September 30, 2015**

| <b>Carrying Value</b>                | <b>Level 1</b> | <b>Level 2<br/>(In thousands)</b> | <b>Level 3</b> | <b>Total</b> |            |
|--------------------------------------|----------------|-----------------------------------|----------------|--------------|------------|
| <b>Financial Assets:</b>             |                |                                   |                |              |            |
| Cash and cash equivalents            | \$ 150,481     | \$ 150,481                        | \$ -           | \$ -         | \$ 150,481 |
| Securities available-for-sale        | 14,796         | 1,996                             | 12,800         | -            | 14,796     |
| Loans receivable held for sale       | 27,945         | -                                 | 28,335         | -            | 28,335     |
| Loans receivable held for investment | 198,098        | -                                 | -              | 198,356      | 198,356    |
| Accrued interest receivable          | 963            | 82                                | 84             | 797          | 963        |
| Federal Home Loan Bank stock         | 2,573          | 2,573                             | -              | -            | 2,573      |
| <b>Financial Liabilities:</b>        |                |                                   |                |              |            |
| Deposits                             | \$ 274,921     | \$ -                              | \$ 269,123     | \$ -         | \$ 269,123 |
| Federal Home Loan Bank advances      | 77,500         | -                                 | 79,693         | -            | 79,693     |
| Junior subordinated debentures       | 5,100          | -                                 | -              | 3,070        | 3,070      |
| Accrued interest payable             | 51             | -                                 | 46             | 5            | 51         |

**Fair Value Measurements at December 31, 2014**

| <b>Carrying Value</b>                | <b>Level 1</b> | <b>Level 2<br/>(In thousands)</b> | <b>Level 3</b> | <b>Total</b> |            |
|--------------------------------------|----------------|-----------------------------------|----------------|--------------|------------|
| <b>Financial Assets:</b>             |                |                                   |                |              |            |
| Cash and cash equivalents            | \$ 20,790      | \$ 20,790                         | \$ -           | \$ -         | \$ 20,790  |
| Securities available-for-sale        | 17,075         | 1,957                             | 15,118         | -            | 17,075     |
| Loans receivable held for sale       | 19,481         | -                                 | 19,679         | -            | 19,679     |
| Loans receivable held for investment | 276,643        | -                                 | -              | 277,000      | 277,000    |
| Accrued interest receivable          | 1,216          | 78                                | 88             | 1,050        | 1,216      |
| Federal Home Loan Bank stock         | 4,254          | 4,254                             | -              | -            | 4,254      |
| <b>Financial Liabilities:</b>        |                |                                   |                |              |            |
| Deposits                             | \$ 217,867     | \$ -                              | \$ 210,181     | \$ -         | \$ 210,181 |
| Federal Home Loan Bank advances      | 86,000         | -                                 | 88,246         | -            | 88,246     |
| Junior subordinated debentures       | 5,100          | -                                 | -              | 2,034        | 2,034      |
| Accrued interest payable             | 69             | -                                 | 39             | 30           | 69         |

The methods and assumptions, not previously presented, used to estimate fair values are described as follows:

*(a) Cash and Cash Equivalents*

The carrying amounts of cash and cash equivalents approximate fair values and are classified as Level 1.

*(b) Loans receivable held for sale*

The Company's loans receivable held for sale are carried at the lower of cost or fair value. The fair value of loans receivable held for sale is determined by pricing for comparable assets or by outstanding commitments from third party investors, resulting in a Level 2 classification.

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**BROADWAY FINANCIAL CORPORATION AND SUBSIDIARY**

**Notes to Unaudited Consolidated Financial Statements (continued)**

*(c) Loans receivable held for investment*

Fair values of loans, excluding loans receivable held for sale, are estimated as follows: For variable rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying values resulting in a Level 3 classification. Fair values for other loans are estimated using discounted cash flow analyses, using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality resulting in a Level 3 classification. Impaired loans are valued at the lower of cost or fair value as described previously. The methods utilized to estimate the fair value of loans do not necessarily represent an exit price.

*(d) FHLB Stock*

The carrying value of FHLB stock approximates its fair value as the shares can only be redeemed by the FHLB at par.

*(e) Accrued Interest Receivable/Payable*

The carrying amounts of accrued interest receivable/payable approximate their fair value and are classified the same as the related asset.

*(f) Deposits*

The fair values disclosed for demand deposits (e.g., interest and non-interest checking, passbook savings, and certain types of money market accounts) are, by definition, equal to the amount payable on demand at the reporting date (i.e., their carrying amount) resulting in Level 2 classification. Fair values for fixed rate certificates of deposit are estimated using discounted cash flow calculations that apply interest rates currently being offered on certificates to a schedule of aggregated expected monthly maturities on time deposits resulting in a Level 2 classification.

*(g) Federal Home Loan Bank Advances*

The fair values of the Federal Home Loan Bank advances are estimated using discounted cash flow analyses based on the current borrowing rates for similar types of borrowing arrangements resulting in a Level 2 classification.

*(h) Junior Subordinated Debentures*

The fair values of the Debentures are estimated using discounted cash flow analyses based on the current borrowing rates for similar types of borrowing arrangements resulting in a Level 3 classification.

**NOTE (8) Stock-based Compensation**

In 2008, the Company adopted the 2008 Long-Term Incentive Plan ( 2008 LTIP ), which was approved by its stockholders. The 2008 LTIP permits the grant of non-qualified and incentive stock options, stock appreciation rights, full value awards and cash incentive awards to the Company's non-employee directors and certain officers and employees for up to 2,000,000 shares of common stock. Option awards are generally granted with an exercise price equal to the market price of the Company's common stock at the date of grant; the option awards have vesting periods ranging from immediate vesting to 5 years and have 10-year contractual terms.

No options were granted during the three and nine months ended September 30, 2015 and 2014. The Company recorded no stock-based compensation expense during the three and nine months ended September 30, 2015, compared to \$0 and \$11 thousand of stock-based compensation expense recorded during the three and nine months ended September 30, 2014.

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**BROADWAY FINANCIAL CORPORATION AND SUBSIDIARY**

**Notes to Unaudited Consolidated Financial Statements (continued)**

**NOTE (9) Regulatory Matters**

Effective September 9, 2010, the Company and the Bank agreed to the issuance of cease and desist orders (the Orders) by the Office of Thrift Supervision, which was succeeded by the Office of the Comptroller of the Currency (OCC). The Order applicable to the Company prohibits the Company from paying dividends to its stockholders without the prior written approval of the FRB, which is now the federal regulator for savings and loan holding companies. In addition, the Company is not permitted to incur, issue, renew, repurchase, make payments on or increase any debt or redeem any capital stock without prior notice to and receipt of written notice of non-objection from the FRB. The FRB provided written notice of non-objection for the Company's payments of interest on the Debentures during the fourth quarter of 2014 and the first nine months of 2015.

Effective October 30, 2013, the Bank entered into a Consent Order with the OCC, which superseded the Order applicable to the Bank. The Bank's capital requirements are administered by the OCC and involve quantitative measures of assets, liabilities, and certain off-balance sheet items calculated under regulatory accounting practices. Capital amounts and classifications are also subject to qualitative judgments by the OCC. Failure to meet capital requirements can result in regulatory action.

As part of the Consent Order, the Bank is required to maintain a Tier 1 Leverage ratio (Tier 1 capital to adjusted total assets) of at least 9% and a Total Capital ratio (Total capital to risk-weighted assets) of at least 13%, both of which ratios are greater than the respective 4% and 8% levels for such ratios that are generally required under OCC regulations.

The Federal Reserve and the Federal Deposit Insurance Corporation approved final capital rules in July 2013 that substantially amend the existing capital rules for banks. These new rules reflect, in part, certain standards initially adopted by the Basel Committee on Banking Supervision in December 2010 (which standards are commonly referred to as Basel III) as well as requirements contemplated by the Dodd-Frank Act.

Beginning in the first quarter of 2015, the Bank became subject to the Basel III capital requirements, including the standardized approach for calculating risk-weighted assets in accordance with subpart D of the final capital rule. The final rules revise the definition and calculation of Tier 1 capital, Total capital, and include a new Common Equity Tier 1 capital.

Common Equity Tier 1 capital primarily includes common shareholders' equity less certain deductions for goodwill and other intangibles, net of related taxes, and deferred tax assets that arise from tax loss and credit carryforwards. Tier 1 capital is primarily comprised of Common Equity Tier 1 capital, perpetual preferred stock and certain qualifying capital instruments that are subject to phase-out from Tier 1 capital. Tier 2 capital primarily includes qualifying subordinated debt and qualifying ALLL.

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The new capital rules include a new Common Equity Tier 1 capital to risk-weighted assets minimum ratio of 4.5%, raise the minimum ratio of Tier 1 capital to risk-weighted assets from 4.0% to 6.0%, require a minimum ratio of Total capital to risk-weighted assets of 8.0%, and require a minimum Tier 1 Leverage ratio of 4.0%. A new capital conservation buffer is also established above the regulatory minimum capital requirements. This capital conservation buffer will be phased in beginning January 1, 2016 at 0.625% of risk-weighted assets and will increase each subsequent year by an additional 0.625% until reaching its final level of 2.5% on January 1, 2019. An institution that does not meet the conservation buffer will be subject to restrictions on certain activities, including payment of dividends, stock repurchases, and discretionary bonuses to executive officers.

The Bank met the minimum capital requirements under the Consent Order at September 30, 2015 and December 31, 2014. Actual and required capital amounts and ratios at September 30, 2015 and December 31, 2014, together with the higher capital requirements that the Bank is required to meet under the Consent Order applicable to it, are presented below.



Table of Contents**BROADWAY FINANCIAL CORPORATION AND SUBSIDIARY****Notes to Unaudited Consolidated Financial Statements (continued)**

|                            | Actual    |        | Required for<br>Capital Adequacy<br>Purposes |       | Capital<br>Requirements<br>under Consent<br>Order |        |
|----------------------------|-----------|--------|--|-------|---|--------|
|                            | Amount    | Ratio  | Amount<br>(Dollars in thousands)             | Ratio | Amount  | Ratio  |
| <b>September 30, 2015:</b> |           |        |  |       |   |        |
| Tier 1 Leverage            | \$ 43,716 | 11.83% | \$ 14,782                                    | 4.00% | \$ 33,259   | 9.00%  |
| Common Equity Tier 1       | \$ 43,716 | 20.08% | \$ 9,799                                     | 4.50% | N/A   | N/A    |
| Tier 1                     | \$ 43,716 | 20.08% | \$ 13,065                                    | 6.00% | N/A   | N/A    |
| Total Capital              | \$ 46,487 | 21.35% | \$ 17,420                                    | 8.00% | \$ 28,307   | 13.00% |
| <b>December 31, 2014:</b>  |           |        |  |       |   |        |
| Tier 1 Leverage            | \$ 39,773 | 11.34% | \$ 14,028                                    | 4.00% | \$ 31,562   | 9.00%  |
| Tier 1                     | \$ 39,773 | 16.41% | \$ 9,695                                     | 4.00% | N/A   | N/A    |
| Total Capital              | \$ 42,870 | 17.69% | \$ 19,390                                    | 8.00% | \$ 31,508   | 13.00% |

**NOTE (10) Income Taxes**

The Company and its subsidiaries are subject to U.S. federal and state income taxes. Income tax expense is the total of the current year income tax due or refundable and the change in deferred tax assets and liabilities. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carry-forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion, or all, of the deferred tax asset will not be realized. In assessing the realization of deferred tax assets, management evaluates both positive and negative evidence, including the existence of cumulative losses in the current year and the prior two years, the amount of taxes paid in available carry-back years, the forecasts of future income and tax planning strategies. This analysis is updated quarterly. Based on this analysis, the Company determined that a valuation allowance of \$7.6 million was required as of September 30, 2015, resulting in \$0 net deferred tax assets. The Company recorded a valuation allowance of \$8.8 million and \$0 net deferred tax assets as of December 31, 2014. The decreases in the valuation allowance for the three and nine months ended September 30, 2015 were \$342 thousand and \$1.2 million, respectively, which resulted from the net income generated in those periods.

**NOTE (11) Concentration of Credit Risk**

The Bank has a significant concentration of deposits with a long-time customer that accounted for approximately 19% of its deposits as of September 30, 2015. The Bank expects to maintain this relationship with the customer.

**NOTE (12) Subsequent Event**

The Bank is committed to purchasing \$110 million of prime single family residential loans early in the fourth quarter of 2015, subject to due diligence and appropriate documentation. This purchase will be funded from cash and cash equivalents.

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**ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

Management's Discussion and Analysis of Financial Condition and Results of Operations ( MD&A ) is intended to provide a reader of our financial statements with a narrative from the perspective of our management on our financial condition, results of operations, liquidity and certain other factors that may affect our future results. Our MD&A should be read in conjunction with the Consolidated Financial Statements and related Notes included in Part I Item 1, Financial Statements, of this Quarterly Report on Form 10-Q and our Annual Report on Form 10-K for the year ended December 31, 2014.

**Overview**

Total assets increased by \$53.0 million during the nine months ended September 30, 2015, primarily reflecting an increase in deposits in late September from one customer relationship. The growth in assets was primarily invested in cash and cash equivalents, which increased by \$129.7 million, reflecting the increase of \$57.1 million in deposits, plus the sale of \$140.2 million in multi-family residential ( MFR ) loans and repayments of \$30.6 million, net of originations of \$100.2 million, a decrease of \$2.3 million in securities available-for-sale and a decrease of \$1.5 million in REO. We completed the sales of MFR loans during the first nine months of 2015 in order to gain compliance with our loan concentration risk management program. As of September 30, 2015, the Bank's MFR loan concentration was below the limit prescribed by the Office of the Comptroller of the Currency ( OCC ).

At the end of the third quarter, management committed to purchase \$110 million of prime single family residential loans early in the fourth quarter of 2015, subject to due diligence and appropriate documentation. This purchase will be funded from cash and cash equivalents. We believe that this purchase will help us grow our core earnings and diversify our loan portfolio.

We recorded net income of \$979 thousand and \$3.4 million for the three and nine months ended September 30, 2015, compared to \$765 thousand and \$1.8 million for the three and nine months ended September 30, 2014, respectively. Results for the first nine months of 2015 included loan loss provision recapture of \$1.7 million, gain on sale of loans of \$1.3 million and a grant of \$355 thousand from the U.S. Department of the Treasury's Community Development Financial Institutions ( CDFI ) Fund. During the first nine months of 2014, we did not report any gains on sales of loans but we recorded loan loss provision recaptures of \$2.5 million and income from a grant of \$200 thousand from the CDFI fund. The growth in net income also reflects lower non-interest expense during the first nine months of 2015 compared to the same period in 2014.

We became subject to the Basel III capital requirements effective January 1, 2015. The Basel III capital rules include a new ratio of Common Equity Tier 1 capital to risk-weighted assets and increased the minimum capital requirements. A new capital conservation buffer has also been established at levels above the regulatory minimum capital requirements. The final rules also revise the definition and calculation of Tier 1 capital, Total capital and risk-weighted assets. The implementation of the Basel III capital requirements is transitional and phases in through the end of 2018. See Regulatory Capital for additional information. We have been in compliance with the new capital rules throughout 2015.

**Results of Operations**

*Net Income*

We recorded net income of \$979 thousand, or \$0.03 per diluted common share, and \$3.4 million, or \$0.12 per diluted common share, for the three and nine months ended September 30, 2015, respectively. For the same periods a year ago, we recorded net income of \$765 thousand, or \$0.04 per diluted common share, and \$1.8 million, or \$0.09 per diluted common share, respectively. The increases in net income during the three and nine months ended September 30, 2015 were primarily due to higher gains on the sale of loans and lower non-interest expense. Per share results in 2015 were impacted by the issuance of approximately 8.8 million shares in October 2014 in connection with a private placement that raised approximately \$9.7 million of new common equity capital.

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*Net Interest Income*

Net interest income before loan loss provision recapture was \$2.8 million for the third quarter of 2015, which is a decrease of \$118 thousand, or 4%, from \$2.9 million for the third quarter of 2014. The slight decrease in net interest income compared to the third quarter of 2014 was primarily due to lower interest income on loans and higher interest expense on deposits and was partially offset by lower interest expense on FHLB advances.

Interest income and fees on loans were \$3.5 million for the third quarter of 2015, down \$157 thousand, or 4%, from the third quarter of 2014. The decrease in loan interest income compared to the third quarter of 2014 was driven by a 37 basis point decrease in the average yield on loans to 4.91% for the third quarter of 2015 from 5.28% for the third quarter of 2014. The lower average yield on loans for the third quarter of 2015 was primarily due to new originations at interest rates below the weighted average interest rate on the portfolio, and payoffs of higher rate loans, coupled with the impact of the downward repricing of our adjustable rate loans. Partially offsetting this decrease was the impact of an \$8.7 million growth in the total average loan portfolio, including loans held for sale, which increased to \$287.3 million for the third quarter of 2015 from \$278.6 million for the third quarter of 2014. Nonetheless, interest income during the third quarter of 2015 was negatively impacted by the sale of \$59.0 million of MFR loans during the first half of 2015.

Total interest expense was \$931 thousand for the third quarter of 2015, down \$28 thousand, or 3%, from the third quarter of 2014. Interest expense on deposits was \$485 thousand for the third quarter of 2015, up \$64 thousand, or 15%, from the third quarter of 2014. The increase in deposit interest expense compared to the third quarter of 2014 was due to growth in money market and certificates of deposit accounts. The average balance of deposits increased by \$26.5 million to \$241.9 million in the third quarter of 2015 compared to \$215.4 million in the third quarter of 2014.

Interest expense on borrowings was \$446 thousand for the third quarter of 2015, down \$92 thousand, or 17%, from the third quarter of 2014. The decrease in interest expense on borrowings primarily reflected a decrease of \$81 thousand in interest expense on FHLB advances and a decrease of \$11 thousand in interest expense on the Debentures as a result of a partial repayment in late 2014. The decrease of \$81 thousand in interest expense on FHLB advances was primarily due to a decrease of 35 basis points in the average cost of FHLB advances and a decrease of \$2.0 million in the average balance of FHLB advances.

For the nine months ended September 30, 2015, net interest income before loan loss provision recapture totaled \$8.9 million, up \$269 thousand, or 3%, from \$8.6 million of net interest income before loan loss provision recapture for the same period a year ago, as the impact of higher average interest-earning assets more than offset the impact of lower net interest margin. Average interest-earning assets increased by \$28.6 million to \$352.6 million for the nine months ended September 30, 2015 compared to \$324.0 million for the same period in 2014. Net interest margin decreased by 19 basis points to 3.36% for the nine months ended September 30, 2015 from 3.55% for the same period in 2014.

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The following tables set forth average balance sheets, average yields and costs, and certain other information for the periods indicated. All average balances are daily average balances. The yields set forth below include the effect of deferred loan fees, and discounts and premiums that are amortized or accreted to interest income or expense. We do not accrue interest on loans on non-accrual status; however, the balance of these loans is included in the total average balance of loans receivable, which has the effect of reducing average loan yields.

## For the three months ended September 30,

| (Dollars in Thousands)                              | 2015            |          |                        | 2014            |          |                        |
|---|-----------------|----------|------------------------|-----------------|----------|------------------------|
|   | Average Balance | Interest | Average Yield/<br>Cost | Average Balance | Interest | Average Yield/<br>Cost |
| <b>Assets</b>                                       |                 |          |                        |                 |          |                        |
| Interest-earning assets:                            |                 |          |                        |                 |          |                        |
| Interest-earning deposits                           | \$ 4,924        | \$ 3     | 0.24%                  | \$ 2,988        | \$ 4     | 0.54%                  |
| Federal Funds sold and other short-term investments | 51,392          | 26       | 0.20%                  | 24,633          | 15       | 0.24%                  |
| Securities  | 15,243          | 84       | 2.20%                  | 17,924          | 103      | 2.30%                  |
| Loans receivable (1)                                | 287,349         | 3,524    | 4.91%                  | 278,649         | 3,681    | 5.28%                  |
| FHLB stock  | 2,737           | 92       | 13.45%                 | 3,737           | 72       | 7.71%                  |
| Total interest-earning assets                       | 361,645         | \$ 3,729 | 4.12%                  | 327,931         | \$ 3,875 | 4.73%                  |
| Non-interest-earning assets                         | 7,594           |          |                        | 7,361           |          |                        |
| Total assets  | \$ 369,239      |          |                        | \$ 335,292      |          |                        |
| <b>Liabilities and Stockholders Equity</b>          |                 |          |                        |                 |          |                        |
| Interest-bearing liabilities:                       |                 |          |                        |                 |          |                        |
| Money market deposits                               | \$ 23,688       | \$ 31    | 0.52%                  | \$ 15,523       | \$ 14    | 0.36%                  |
| Passbook deposits                                   | 36,259          | 29       | 0.32%                  | 36,339          | 30       | 0.33%                  |
| NOW and other demand deposits                       | 28,262          | 5        | 0.07%                  | 30,870          | 7        | 0.09%                  |
| Certificate accounts                                | 153,656         | 420      | 1.09%                  | 132,658         | 370      | 1.12%                  |
| Total deposits                                      | 241,865         | 485      | 0.80%                  | 215,390         | 421      | 0.78%                  |
| FHLB advances                                       | 77,500          | 409      | 2.11%                  | 79,500          | 490      | 2.46%                  |
| Junior subordinated debentures (2)                  | 5,100           | 37       | 2.90%                  | 6,000           | 48       | 3.20%                  |
| Senior debt (3)                                     | -               | -        | -                      | 2,831           | -        | -                      |
| Total interest-bearing liabilities                  | 324,465         | \$ 931   | 1.15%                  | 303,721         | \$ 959   | 1.26%                  |
| Non-interest-bearing liabilities                    | 4,861           |          |                        | 4,634           |          |                        |
| Stockholders Equity                                 | 39,915          |          |                        | 26,937          |          |                        |
| Total liabilities and stockholders equity           | \$ 369,239      |          |                        | \$ 335,292      |          |                        |
| Net interest rate spread (4)                        |                 | \$ 2,798 | 2.97%                  |                 | \$ 2,916 | 3.47%                  |
| Net interest rate margin (5)                        |                 |          | 3.09%                  |                 |          | 3.56%                  |

(1) Amount is net of deferred loan fees, loan discounts, and loans in process, and includes loans receivable held for sale.

(2) 2014 interest expense included compounding on past due interest. Interest on the Debentures was brought current in October 2014.

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- (3) No interest expense was recognized on the senior debt post restructuring because the floating interest rate on the remaining modified loan did not exceed the floor rate of 6% post modification. Paid off in October 2014.
- (4) Net interest rate spread represents the difference between the yield on average interest-earning assets and the cost of average interest-bearing liabilities.
- (5) Net interest rate margin represents net interest income as a percentage of average interest-earning assets.

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## For the nine months ended September 30,

| (Dollars in Thousands)                              | 2015            |           |                        | 2014            |           |                        |
|---|-----------------|-----------|------------------------|-----------------|-----------|------------------------|
|   | Average Balance | Interest  | Average Yield/<br>Cost | Average Balance | Interest  | Average Yield/<br>Cost |
| <b>Assets</b>                                       |                 |           |                        |                 |           |                        |
| Interest-earning assets:                            |                 |           |                        |                 |           |                        |
| Interest-earning deposits                           | \$ 3,218        | \$ 7      | 0.29%                  | \$ 2,999        | \$ 10     | 0.44%                  |
| Federal Funds sold and other short-term investments | 31,002          | 50        | 0.22%                  | 33,761          | 60        | 0.24%                  |
| Securities  | 15,902          | 268       | 2.25%                  | 14,962          | 271       | 2.42%                  |
| Loans receivable (1)                                | 298,987         | 11,027    | 4.92%                  | 268,512         | 10,996    | 5.46%                  |
| FHLB stock  | 3,506           | 394       | 14.98%                 | 3,737           | 209       | 7.46%                  |
| Total interest-earning assets                       | 352,615         | \$ 11,746 | 4.44%                  | 323,971         | \$ 11,546 | 4.75%                  |
| Non-interest-earning assets                         | 7,174           |           |                        | 8,275           |           |                        |
| Total assets  | \$ 359,790      |           |                        | \$ 332,246      |           |                        |
| <b>Liabilities and Stockholders Equity</b>          |                 |           |                        |                 |           |                        |
| Interest-bearing liabilities:                       |                 |           |                        |                 |           |                        |
| Money market deposits                               | \$ 19,231       | \$ 66     | 0.46%                  | \$ 15,629       | \$ 45     | 0.38%                  |
| Passbook deposits                                   | 36,585          | 87        | 0.32%                  | 36,725          | 89        | 0.32%                  |
| NOW and other demand deposits                       | 28,929          | 16        | 0.07%                  | 30,834          | 21        | 0.09%                  |
| Certificate accounts                                | 143,805         | 1,166     | 1.08%                  | 129,342         | 1,154     | 1.19%                  |
| Total deposits                                      | 228,550         | 1,335     | 0.78%                  | 212,530         | 1,309     | 0.82%                  |
| FHLB advances                                       | 82,811          | 1,405     | 2.26%                  | 79,500          | 1,466     | 2.46%                  |
| Junior subordinated debentures (2)                  | 5,100           | 108       | 2.82%                  | 6,000           | 142       | 3.16%                  |
| Senior debt (3)                                     | -               | -         | -                      | 2,867           | -         | -                      |
| Total interest-bearing liabilities                  | 316,461         | \$ 2,848  | 1.20%                  | 300,897         | \$ 2,917  | 1.29%                  |
| Non-interest-bearing liabilities                    | 4,495           |           |                        | 4,936           |           |                        |
| Stockholders Equity                                 | 38,833          |           |                        | 26,413          |           |                        |
| Total liabilities and stockholders equity           | \$ 359,789      |           |                        | \$ 332,246      |           |                        |
| Net interest rate spread (4)                        |                 | \$ 8,898  | 3.24%                  |                 | \$ 8,629  | 3.46%                  |
| Net interest rate margin (5)                        |                 |           | 3.36%                  |                 |           | 3.55%                  |

(1) Amount is net of deferred loan fees, loan discounts, and loans in process, and includes loans receivable held for sale.

(2) 2014 interest expense included compounding on past due interest. Interest on the Debentures was brought current in October 2014.

(3) No interest expense was recognized on the senior debt post restructuring because the floating interest rate on the remaining modified loan did not exceed the floor rate of 6% post modification. Paid off in October 2014.

(4) Net interest rate spread represents the difference between the yield on average interest-earning assets and the cost of average interest-bearing liabilities.



- (5) Net interest rate margin represents net interest income as a percentage of average interest-earning assets.

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*Loan loss provision recapture*

We recorded a \$200 thousand loan loss provision recapture for the third quarter of 2015, compared to a \$950 thousand loan loss provision recapture for the third quarter of 2014. The loan loss provision recapture during the third quarter of 2015 was primarily due to the continued improvements in asset quality and declines in net charge-offs and overall historical loss factors. See *Allowance for Loan Losses* for additional information.

For the nine months ended September 30, 2015, we recorded a loan loss provision recapture of \$1.7 million compared to \$2.5 million for the same period a year ago. The loan loss provision recapture during the first nine months of 2015 primarily reflected a reduction in the loans held for investment portfolio and continued improvements in asset quality.

*Non-interest Income*

Non-interest income was \$992 thousand for the third quarter of 2015, up \$827 thousand, or 501%, from the third quarter of 2014. The increase in non-interest income from the third quarter of 2014 was primarily due to a gain of \$738 thousand on the sale of MFR loans and an increase of \$23 thousand in gain on sale of REOs.

For the nine months ended September 30, 2015, non-interest income totaled \$2.1 million compared to \$562 thousand for the same period a year ago. The increase in non-interest income was primarily due to a gain on sale of loans of \$1.3 million during the first nine months of 2015. We also received a CDFI grant that was \$155 thousand larger than last year and recorded higher gains on the sale of REOs during the first nine months of 2015 compared to the same period of 2014.

*Non-interest Expense*

Non-interest expense was \$3.0 million for the third quarter of 2015, down \$263 thousand, or 8%, from the third quarter of 2014. The decrease in non-interest expense from the third quarter of 2014 was primarily due to a decrease of \$64 thousand in compensation and benefits expense, a decrease of \$57 thousand in REO expense, primarily due to reduced valuation write-downs, a decrease of \$55 thousand in FDIC assessments, primarily due to a reduction in our assessment rate, and a decrease of \$149 thousand in other expense, primarily reflecting lower appraisal expenses and the reversal of previously recognized provisions related to unfunded loan commitments resulting from a decrease in unfunded loan commitments. These decreases were partially offset by an increase of \$74 thousand in professional services expense, primarily legal expense.

For the nine months ended September 30, 2015, non-interest expense totaled \$9.3 million compared to \$9.9 million for the same period a year ago. The decrease in non-interest expense during the first nine months of 2015 primarily reflected a decrease of \$111 thousand in professional services expense, a decrease of \$230 thousand in FDIC assessments, a decrease of \$282 thousand in REO expenses and a decrease of \$135 thousand in other expense, which were partially offset by an increase of \$179 thousand in compensation and benefits expense. Professional services expense for the first nine months of 2015 was lower than in the first nine months of 2014 due to legal and consulting fees incurred in 2014 in connection with negotiating an extension of the maturity of the Debentures. The decrease in REO expense during the first nine months

of 2015 was primarily due to lower provisions for losses on REO, reflecting fewer foreclosures and more stable property values. Other expense for the first nine months of 2015 was lower than in the first nine months of 2014 due to lower appraisal expenses, primarily because we have fewer problem loans. Compensation and benefits expense for the first nine months of 2015 increased primarily due to salary increases and a decrease in salaries deferred as loan origination costs.

*Income Taxes*

For the three months ended September 30, 2015, income tax expense was \$8 thousand, compared to \$0 for the three months ended September 30, 2014. For the nine months ended September 30, 2015, income tax expense was \$16 thousand compared to \$3 thousand for the nine months ended September 30, 2014. The lower tax expense and effective tax rate for 2015 and 2014 primarily reflected the statutory minimum taxes paid to the state of California, and the use of tax carryforwards to offset current taxable income in the periods presented.

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**Financial Condition**

*Total Assets*

Total assets were \$403.9 million at September 30, 2015, which represented an increase of \$53.0 million, or 15%, from total assets of \$350.9 million at December 31, 2014. The increase in assets during the first nine months of 2015 was primarily from an increase in deposits in late September from one customer relationship. The growth in assets was primarily invested in cash and cash equivalents, which increased by \$129.7 million, reflecting the increase of \$57.1 million in deposits, plus the sale of \$140.2 million in MFR loans and repayments of \$30.6 million, net of originations of \$100.2 million, a decrease of \$2.3 million in securities available-for-sale and a decrease of \$1.5 million in REO.

*Loans Receivable Held for Sale*

Loans receivable held for sale at September 30, 2015 and December 31, 2014 totaled \$27.9 million and \$19.5 million, respectively, and consisted of MFR loans. During the first nine months of 2015, we transferred \$91.6 million of MFR loans from the held-for-investment portfolio to the held-for-sale portfolio and allocated \$57.6 million, or 57%, of our loan originations during the period to the held-for-sale portfolio as part of our loan concentration risk management program and sold \$140.2 million of MFR loans during the period.

*Loans Receivable Held for Investment*

Our gross loan portfolio decreased by \$80.3 million to \$204.8 million at September 30, 2015, from \$285.1 million at December 31, 2014. The decrease in our loan portfolio during the first nine months of 2015 primarily consisted of a decrease of \$61.2 million in our MFR residential real estate loan portfolio primarily due to transfers to the held-for-sale portfolio, and decreases of \$8.1 million in our single family residential real estate loan portfolio, \$4.4 million in our commercial real estate loan portfolio and \$5.6 million in our church loan portfolio, due to payoffs.

Gross loans originated for investment (excluding the \$57.6 million of MFR loans originated for-sale) totaled \$42.6 million for the nine months ended September 30, 2015, compared to gross loans originated for investment of \$67.2 million for the nine months ended September 30, 2014. Loan repayments for the nine months ended September 30, 2015 totaled \$30.6 million, compared to \$32.1 million for the nine months ended September 30, 2014. Loans transferred to our held-for-sale portfolio during the nine months ended September 30, 2015 totaled \$91.6 million.

Gross loan charge-offs during the first nine months of 2015 totaled \$53 thousand, compared to gross loan charge-offs of \$483 thousand during the first nine months of 2014. Loans transferred to REO during the first nine months of 2015 totaled \$843 thousand, compared to \$3.3 million during the first nine months of 2014.

*Allowance for Loan Losses*

We record a provision for loan losses as a charge to earnings when necessary in order to maintain the allowance for loan losses ( ALLL ) at a level sufficient, in management's judgment, to absorb probable incurred losses in the loan portfolio. At least quarterly we conduct an assessment of the overall quality of the loan portfolio and general economic trends in the local market. The determination of the appropriate level for the allowance is based on that review, considering such factors as historical loss experience for each type of loan, the size and composition of our loan portfolio, the levels and composition of our loan delinquencies, non-performing loans and net loan charge-offs, the value of underlying collateral on problem loans, regulatory policies, general economic conditions, and other factors related to the collectability of loans in the portfolio.

Our ALLL decreased by \$1.7 million to \$6.7 million, or 3.28% of our gross loans receivable held for investment, at September 30, 2015, from \$8.5 million, or 2.97% of our gross loans receivable held for investment, at December 31, 2014, primarily reflecting \$1.7 million of loan loss provision recapture. The reduction in ALLL at September 30, 2015 compared to December 31, 2014, and the loan loss provision recaptures during 2015, reflect the results of our quarterly reviews of the adequacy of the ALLL. We continue to maintain our ALLL at a level that we believe is appropriate given the significant reduction in delinquencies and non-performing loans, the continued improvement in our asset quality metrics and the high quality of our loan originations.

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We believe that our asset quality is strong as our loan delinquencies and non-performing loans are at their lowest levels since December 2009. As of September 30, 2015, we had total delinquencies of \$1.3 million, compared to total delinquencies of \$2.5 million at December 31, 2014. Loan delinquencies decreased by \$1.2 million during the first nine months of 2015 primarily due to payoffs of \$292 thousand and transfers to REO of \$843 thousand.

Non-performing loans ( NPLs ) consist of delinquent loans that are 90 days or more past due and other loans, including troubled debt restructurings that do not qualify for accrual status. At September 30, 2015, NPLs totaled \$5.7 million, compared to \$8.9 million at December 31, 2014. The decrease of \$3.2 million in NPLs was primarily due to net loan upgrades to accrual status of \$423 thousand, transfers to REO of \$843 thousand, payoffs of \$1.3 million, repayments of \$525 thousand and charge-offs of \$53 thousand.

In connection with our review of the adequacy of our ALLL, we track the amount and percentage of our NPLs that are paying currently, but nonetheless must be classified as NPL for reasons unrelated to payments, such as lack of current financial information and an insufficient period of satisfactory performance. As of September 30, 2015, \$4.6 million, or 81%, of our total NPLs of \$5.7 million were current in their payments. Also, in determining the ALLL, we consider the ratio of the ALLL to NPLs, which increased to 117.13% at September 30, 2015 from 95.52% at December 31, 2014.

When reviewing the adequacy of the ALLL, we also consider the impact of charge-offs, including the changes and trends in loan charge-offs. Gross loan charge-offs during the first nine months of 2015 were \$53 thousand compared to \$483 thousand during the first nine months of 2014. The charge-offs during the first nine months of 2015 were primarily due to impairment losses on a foreclosed church loan and a delinquent single-family residential real estate loan that was fully written off. In determining charge-offs, we update our estimates of collateral values on NPLs by obtaining new appraisals at least every nine months. If the estimated fair value of the loan collateral less estimated selling costs is less than the recorded investment in the loan, a charge-off for the difference is recorded to reduce the loan to its estimated fair value, less estimated selling costs. Therefore, certain losses inherent in our total NPLs are recognized periodically through charge-offs. The impact of updating these estimates of collateral value and recognizing any required charge-offs is to increase charge-offs and reduce the ALLL required on these loans. As of September 30, 2015, we had written down 65% of our NPLs to estimated fair value less estimated selling costs. The remaining 35% of our NPLs at September 30, 2015 had specific reserves or were reported at cost because the fair value of collateral less estimated selling costs exceeded the recorded investment in the loan. As of September 30, 2015, the average loan-to-value on NPLs was 51%.

Recoveries during the first nine months of 2015 totaled \$16 thousand compared to \$1.9 million during the first nine months of 2014. Recoveries during the first nine months of 2014 were primarily due to payoffs of two non-accrual loans secured by church properties and two commercial loans which had been fully written off in late 2011 and due to a settlement of a loan which had been previously written down in exchange for property received in foreclosure, the fair value of which exceeded the cost basis of the related loan.

Impaired loans at September 30, 2015 were \$18.8 million, compared to \$23.5 million at December 31, 2014. Specific reserves for impaired loans were \$1.3 million, or 7.06% of the aggregate impaired loan amount at September 30, 2015, compared to \$1.5 million, or 6.40%, at December 31, 2014. Excluding specific reserves for impaired loans, our coverage ratio (general allowance as a percentage of total non-impaired loans) increased to 2.90% at September 30, 2015, from 2.66% at December 31, 2014.

Management believes that the ALLL is adequate to cover probable incurred losses in the loan portfolio as of September 30, 2015, but there can be no assurance that actual losses will not exceed the estimated amounts. In addition, the OCC and the FDIC periodically review the ALLL as an integral part of their examination process. These agencies may require an increase in the ALLL based on their judgments of the information available to them at the time of their examinations.



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*Real Estate Owned*

During the first nine months of 2015, REO decreased by \$1.5 million to \$558 thousand at September 30, 2015, from \$2.1 million at December 31, 2014. During the first nine months of 2015, two church loans totaling \$843 thousand were foreclosed and the properties securing the loans were transferred to REO. Three REO properties were sold during 2015 for net proceeds of \$2.3 million and a net gain of \$75 thousand. At September 30, 2015, the Bank's REO consisted of one church property, which was sold early in the fourth quarter of 2015.

*Deposits*

Deposits totaled \$274.9 million at September 30, 2015, up \$57.0 million from December 31, 2014. During the first nine months of 2015, certificates of deposit increased by \$44.1 million and represented 65% of total deposits at September 30, 2015, compared to 62% of total deposits at December 31, 2014. Core deposits (NOW, demand, money market and passbook accounts) increased by \$12.9 million during the first nine months of 2015 and represented 35% of total deposits at September 30, 2015, compared to 38% of total deposits at December 31, 2014. During the third quarter of 2015, a long-time customer deposited approximately \$12.5 million in his money market and NOW accounts, and opened a two-year certificate of deposit in the amount of \$40.0 million.

*Borrowings*

At September 30, 2015, total borrowings consisted of advances to the Bank from the FHLB of \$77.5 million and debentures issued by the Company of \$5.1 million. At December 31, 2014, total borrowings consisted of advances from the FHLB of \$86.0 million and Debentures of \$5.1 million. During the first nine months of 2015, we repaid \$8.5 million of the FHLB advance with proceeds from our loan sale in June.

*Stockholders' Equity*

Stockholders' equity was \$40.6 million, or 10.06% of the Company's total assets, at September 30, 2015, compared to \$37.3 million, or 10.62% of the Company's total assets, at December 31, 2014. The increase in stockholders' equity during the first nine months of 2015 was primarily due to net earnings for such period.



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**Liquidity**

The objective of liquidity management is to ensure that we have the continuing ability to fund operations and meet our obligations on a timely and cost-effective basis. The Bank's sources of funds include deposits, advances from the FHLB and other borrowings, proceeds from the sale of loans, REO, and investment securities, and payments of principal and interest on loans and investment securities. The Bank is currently approved by the FHLB to borrow up to 30% of total assets to the extent the Bank provides qualifying collateral and holds sufficient FHLB stock. This approved limit and collateral requirement would have permitted the Bank, as of September 30, 2015, to borrow an additional \$30.2 million. Also, the Bank has received cash from equity contributions by the Company during 2013 and 2014.

The Bank's primary uses of funds include withdrawal of and interest payments on deposits, originations of loans, purchases of investment securities, and payment of operating expenses. Also, when the Bank has more funds than required for reserve requirements or short-term liquidity needs, the Bank sells federal funds to the Federal Reserve Bank or other financial institutions. The Bank's liquid assets at September 30, 2015 consisted of \$150.5 million in cash and cash equivalents and \$14.1 million in securities available-for-sale that were not pledged, compared to liquid assets of \$20.8 million in cash and cash equivalents and \$15.9 million in securities available-for-sale that were not pledged at December 31, 2014. The high levels of liquid assets as of September 30, 2015 reflect the proceeds from \$82 million in loan sales that closed in September 2015 and the cash from new retail deposits. The Bank is committed to purchase \$110 million of prime single family residential loans early in the fourth quarter of 2015, subject to due diligence and appropriate documentation. This purchase will be funded from cash and cash equivalents. We believe that this purchase will help us grow our core earnings and diversify our loan portfolio.

Currently, we believe that the Bank has sufficient liquidity to support growth over the foreseeable future.

The Company's liquidity, separate from the Bank, is based primarily on the proceeds from financing transactions, such as the private placements completed in August 2013 and October 2014. The Company has not been able to obtain funds from the Bank since 2010 as the Order placed limitations on the Bank, including prohibition of the payment of dividends by the Bank without prior regulatory approval.

The Company recorded consolidated net cash outflows from operating activities of \$9.1 million during the nine months ended September 30, 2015, compared to consolidated net cash inflows from operating activities of \$1.2 million during the nine months ended September 30, 2014. Net cash outflows from operating activities during the first nine months of 2015 were primarily attributable to originations of loans held-for-sale.

The Company recorded consolidated net cash inflows from investing activities of \$90.2 million during the nine months ended September 30, 2015, compared to consolidated net cash outflows from investing activities of \$40.8 million during the nine months ended September 30, 2014. Net cash inflows from investing activities during the first nine months of 2015 were primarily attributable to proceeds from sale of loans, principal repayments on securities, proceeds from sale of REOs and proceeds from redemption of FHLB stock.

The Company recorded consolidated net cash inflows from financing activities of \$48.6 million and \$2.7 million during the nine months ended September 30, 2015 and 2014, respectively. Net cash inflows from financing activities during the first nine months of 2015 were primarily attributable to the increase in deposits described above.

**Capital Resources**

Our principal subsidiary, Broadway Federal, must comply with capital standards established by the OCC in the conduct of its business. Failure to comply with such capital requirements may result in significant limitations on its business or other sanctions. The Dodd-Frank Act, among other things, now imposes specific capital requirements on us as a savings and loan holding company as well. These requirements must be no less than those to which federally insured depository institutions are currently subject. The current regulatory capital requirements are described in Note 9 of the Notes to Consolidated Financial Statements and in Regulatory Capital below.

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The Federal Reserve and the Federal Deposit Insurance Corporation approved final capital rules in July 2013 that substantially amend the existing capital rules for banks. These new rules reflect, in part, certain standards initially adopted by the Basel Committee on Banking Supervision in December 2010 (which standards are commonly referred to as Basel III ) as well as requirements contemplated by the Dodd-Frank Act.

Beginning in the first quarter of 2015, we became subject to the Basel III capital requirements, including the standardized approach for calculating risk-weighted assets in accordance with subpart D of the final capital rule. The final rules also revise the definition and calculation of Tier 1 capital, Total capital, and include a new Common Equity Tier 1 capital.

Common Equity Tier 1 capital primarily includes common shareholders' equity less certain deductions for goodwill and other intangibles net of related taxes, and deferred tax assets that arise from tax loss and credit carryforwards. Tier 1 capital is primarily comprised of Common Equity Tier 1 capital, perpetual preferred stock and certain qualifying capital instruments that are subject to phase-out from Tier 1 capital. Tier 2 capital primarily includes qualifying subordinated debt and qualifying ALLL.

The new capital rules include a new Common Equity Tier 1 capital to risk-weighted assets minimum ratio of 4.5%, raise the minimum ratio of Tier 1 capital to risk-weighted assets from 4.0% to 6.0%, require a minimum ratio of Total capital to risk-weighted assets of 8.0%, and require a minimum Tier 1 Leverage ratio of 4.0%. A new capital conservation buffer is also established above the regulatory minimum capital requirements. This capital conservation buffer will be phased in beginning January 1, 2016 at 0.625% of risk-weighted assets and will increase each subsequent year by an additional 0.625% until reaching its final level of 2.5% on January 1, 2019. An institution that does not meet the conservation buffer will be subject to restrictions on certain activities, including payment of dividends, stock repurchases, and discretionary bonuses to executive officers.

The Bank is subject to higher capital requirements under the Consent Order entered into by the Bank with the OCC on October 30, 2013. The Consent Order raised the Bank's minimum capital requirements to 9% for Tier 1 Leverage ratio (Tier 1 capital to adjusted total assets) and 13% for Total Capital ratio (Total capital to risk-weighted assets). The Bank was in compliance with all capital requirements in effect at September 30, 2015 and December 31, 2014.

Actual and required capital amounts and ratios at September 30, 2015 and December 31, 2014, together with the higher capital requirements that the Bank is required to meet under the Consent Order applicable to it, are presented below.

|                            | Actual    |        | Required for<br>Capital Adequacy<br>Purposes |       | Capital<br>Requirements<br>under Consent<br>Order |       |
|----------------------------|-----------|--------|--|-------|---|-------|
|                            | Amount    | Ratio  | Amount<br>(Dollars in thousands)             | Ratio | Amount  | Ratio |
| <b>September 30, 2015:</b> |           |        |  |       |   |       |
| Tier 1 Leverage            | \$ 43,716 | 11.83% | \$ 14,782                                    | 4.00% | \$ 33,259   | 9.00% |

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|                      |           |        |           |       |           |        |
|----------------------|-----------|--------|-----------|-------|-----------|--------|
| Common Equity Tier 1 | \$ 43,716 | 20.08% | \$ 9,799  | 4.50% | N/A       | N/A    |
| Tier 1               | \$ 43,716 | 20.08% | \$ 13,065 | 6.00% | N/A       | N/A    |
| Total Capital        | \$ 46,487 | 21.35% | \$ 17,420 | 8.00% | \$ 28,307 | 13.00% |

**December 31, 2014:**

|                 |           |        |           |       |           |        |
|-----------------|-----------|--------|-----------|-------|-----------|--------|
| Tier 1 Leverage | \$ 39,773 | 11.34% | \$ 14,028 | 4.00% | \$ 31,562 | 9.00%  |
| Tier 1          | \$ 39,773 | 16.41% | \$ 9,695  | 4.00% | N/A       | N/A    |
| Total Capital   | \$ 42,870 | 17.69% | \$ 19,390 | 8.00% | \$ 31,508 | 13.00% |

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

Not Applicable

**ITEM 4. CONTROLS AND PROCEDURES**

**Evaluation of Disclosure Controls and Procedures**

An evaluation of the effectiveness of the design and operation of the Company's disclosure controls and procedures was performed under the supervision of the Company's Chief Executive Officer ( CEO ) and Chief Financial Officer ( CFO ) as of September 30, 2015. Based on that evaluation, the Company's CEO and CFO concluded that the Company's disclosure controls and procedures were effective as of September 30, 2015. There were no significant changes during the quarter ended September 30, 2015 in the Company's internal controls 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. OTHER INFORMATION

Item 1. LEGAL PROCEEDINGS

None

Item 1A. RISK FACTORS

Not Applicable

Item 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

None

Item 3. DEFAULTS UPON SENIOR SECURITIES

None

Item 4. MINE SAFETY DISCLOSURES

Not Applicable

Item 5. OTHER INFORMATION

None

Item 6. EXHIBITS

**Exhibit  
Number\***

|         |   |
|---------|---|
| 3.1     | Certificate of Incorporation of Registrant and amendments thereto (Exhibit 3.1 to Form 10-Q filed by the Registrant on November 13, 2014)         |
| 3.2     | Bylaws of Registrant (Exhibit 3.2 to Form 10-Q filed by the Registrant on November 14, 2013)  |
| 31.1    | Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002  |
| 31.2    | Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002  |
| 32.1    | Certification of Chief Executive Officer 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 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 Document   |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase Document   |
| 101.DEF | XBRL Taxonomy Extension Definitions Linkbase Document   |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase Document   |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase Document  |

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\* Exhibits followed by a parenthetical reference are incorporated by reference herein from the document filed by the Registrant with the SEC described therein. Except as otherwise indicated, the SEC File No. for each incorporated document is 000-27464.

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**SIGNATURES**

In accordance with the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Date: November 13, 2015

By: /s/ Wayne-Kent A. Bradshaw  
Wayne-Kent A. Bradshaw  
Chief Executive Officer

Date: November 13, 2015

By: /s/ Brenda J. Battey  
Brenda J. Battey  
Chief Financial Officer