BROADWAY FINANCIAL CORP \DE\
Form 10-Q
August 11, 2017
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2017

[ ] 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**

(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
5055 Wilshire Boulevard, Suite 500 **Los Angeles, California**	**90036**
(Address of principal executive offices)	(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 x No o

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 x No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated, a smaller reporting company, or an emerging growth company. See the definition of large accelerated filer, accelerated filer, smaller reporting company, and emerging growth company in Rule 12b-2 of the Exchange Act.

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

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes o No x

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date: As of August 4, 2017, 18,694,823 shares of the Registrant s voting common stock and 8,756,396 shares of the Registrant s non-voting common stock were outstanding.

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BROADWAY FINANCIAL CORPORATION AND SUBSIDIARY

Consolidated Statements of Financial Condition

(In thousands, except share and per share amounts)

	June 30, 2017 (Unaudited)	December 31, 2016
Assets		
Cash and due from banks	$ 2,379	$ 1,516
Interest-bearing deposits in other banks	14,456	16,914
Cash and cash equivalents	16,835	18,430
Securities available-for-sale, at fair value	12,029	13,202
Loans receivable held for sale, at lower of cost or fair value	39,037	-
Loans receivable held for investment, net of allowance of $4,246 and $4,603, respectively	350,308	379,454
Accrued interest receivable	1,103	1,178
Federal Home Loan Bank (FHLB) stock	2,916	2,573
Office properties and equipment, net	2,509	2,479
Bank owned life insurance	2,967	2,940
Deferred tax assets, net	5,975	6,907
Other assets	1,816	1,920
Total assets	**$ 435,495**	**$ 429,083**
Liabilities and stockholders equity		
Liabilities:		
Deposits	$ 273,847	$ 287,427
FHLB advances	104,000	85,000
Junior subordinated debentures	5,100	5,100
Advance payments by borrowers for taxes and insurance	1,009	828
Accrued expenses and other liabilities	3,995	5,202
Total liabilities	**387,951**	**383,557**
Stockholders Equity:		
Preferred stock, $.01 par value, authorized 1,000,000 shares; none issued or outstanding	-	-
Common stock, $.01 par value, voting, authorized 50,000,000 shares at June 30, 2017 and December 31, 2016; issued 21,312,649 shares at June 30, 2017 and 21,282,647 shares at December 31, 2016; outstanding 18,694,823 shares at June 30, 2017 and 18,664,821 shares at December 31, 2016	213	212
Common stock, $.01 par value, non-voting, authorized 25,000,000 shares at June 30, 2017 and December 31, 2016; issued and outstanding 8,756,396 shares at June 30, 2017 and December 31, 2016	87	87
Additional paid-in capital	46,026	45,819
Retained earnings	7,778	6,013
Unearned Employee Stock Ownership Plan (ESOP) shares	(1,133)	(1,176)
Accumulated other comprehensive income (loss)	(101)	(103)
Treasury stock-at cost, 2,617,826 shares at June 30, 2017 and December 31, 2016	(5,326)	(5,326)
Total stockholders equity	**47,544**	**45,526**
Total liabilities and stockholders equity	**$ 435,495**	**$ 429,083**

See accompanying notes to unaudited consolidated financial statements.

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BROADWAY FINANCIAL CORPORATION AND SUBSIDIARY

Consolidated Statements of Income and Comprehensive Income

(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
	(In thousands, except per share)			
Interest income:				
Interest and fees on loans receivable	$ 3,944	$ 3,591	$ 7,908	$ 7,020
Interest on mortgage-backed and other securities	73	84	148	167
Other interest income	119	98	217	201
Total interest income	4,136	3,773	8,273	7,388
Interest expense:				
Interest on deposits	597	511	1,171	1,028
Interest on borrowings	537	421	1,021	848
Total interest expense	1,134	932	2,192	1,876
Net interest income	3,002	2,841	6,081	5,512
Loan loss provision recapture	300	250	650	550
Net interest income after loan loss provision recapture	3,302	3,091	6,731	6,062
Non-interest income:				
Service charges	100	120	221	246
Gain on sale of loans	196	-	223	-
CDFI grant	-	-	-	265
Income from litigation settlement	-	-	1,183	-
Other	26	79	54	231
Total non-interest income	322	199	1,681	742
Non-interest expense:				
Compensation and benefits	1,328	1,709	3,315	3,612
Occupancy expense	315	289	620	582
Information services	208	180	408	386
Professional services	231	320	405	447
Office services and supplies	81	72	153	142
FDIC assessments	41	58	84	83
Other	464	343	726	598
Total non-interest expense	2,668	2,971	5,711	5,850
Income before income taxes	956	319	2,701	954
Income taxes	423	-	936	2
Net income	$ 533	$ 319	$ 1,765	$ 952
Other comprehensive income, net of tax:				
Unrealized gains on securities available-for-sale arising during the period	$ 9	$ 43	$ 3	$ 163
Income tax	3	38	1	67

Other comprehensive income, net of tax		6		5		2		96
Comprehensive income	$	539	$	324	$	1,767	$	1,048
Earnings per common share-basic	$	0.02	$	0.01	$	0.07	$	0.03
Earnings per common share-diluted	$	0.02	$	0.01	$	0.07	$	0.03

See accompanying notes to unaudited consolidated financial statements.

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BROADWAY FINANCIAL CORPORATION AND SUBSIDIARY

Consolidated Statements of Cash Flows

(Unaudited)

	Six Months Ended June 30, 2017	Six Months Ended June 30, 2016
	(In thousands)	
Cash flows from operating activities:		
Net income	$ 1,765	$ 952
Adjustments to reconcile net income to net cash used in (provided by) operating activities:		
Loan loss provision recapture	(650)	(550)
Depreciation	129	124
Net amortization of deferred loan origination costs	134	92
Net amortization of premiums on mortgage-backed securities	17	23
Amortization of investment in affordable housing limited partnership	98	97
Stock-based compensation expense	204	13
ESOP compensation expense	47	45
Earnings on bank owned life insurance	(27)	(29)
Originations of loans receivable held for sale	(86,002)	-
Repayments on loans receivable held for sale	200	-
Proceeds from sales of loans receivable held for sale	46,988	-
Gain on sale of loans receivable held for sale	(223)	-
Net gain on sale of REOs	-	(22)
Net change in deferred taxes	931	-
Net change in accrued interest receivable	75	(63)
Net change in other assets	6	246
Net change in advance payments by borrowers for taxes and insurance	181	-
Net change in accrued expenses and other liabilities	(1,207)	(783)
Net cash (used in) provided by operating activities	(37,334)	145
Cash flows from investing activities:		
Net change in loans receivable held for investment	29,662	(36,635)
Purchase of available-for-sale securities	-	(2,505)
Prepayments on available-for-sale securities	1,159	1,332
Proceeds from sales of REO	-	382
Purchase of FHLB stock	(343)	-
Additions to office properties and equipment	(159)	(26)
Net cash provided by (used in) investing activities	30,319	(37,452)
Cash flows from financing activities:		
Net change in deposits	(13,580)	7,158
Proceeds from FHLB advances	44,000	-
Repayments of FHLB advances	(25,000)	(2,000)
Net cash provided by financing activities	5,420	5,158
Net change in cash and cash equivalents	(1,595)	(32,149)
Cash and cash equivalents at beginning of the period	18,430	67,839

Cash and cash equivalents at end of the period	$ 16,835	$ 35,690
Supplemental disclosures of cash flow information:		
Cash paid for interest	$ 2,241	$ 1,872
Cash paid for income taxes	20	8

See accompanying notes to unaudited consolidated financial statements.

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BROADWAY FINANCIAL CORPORATION AND SUBSIDIARY

Notes to Unaudited Consolidated Financial Statements

June 30, 2017

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, 2016 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 six months ended June 30, 2017 are not necessarily indicative of the results that may be expected for the year ending December 31, 2017.

Recently Adopted Accounting Pronouncement

In March 2016, the FASB issued ASU 2016-09, Compensation Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting . ASU 2016-09 includes provisions intended to simplify various aspects related to how share-based payments are accounted for and presented in the financial statements. The areas for simplification include income tax consequences, forfeitures, classification of awards as either equity or liabilities and classification on the statement of cash flows. Under the new guidance, all excess tax benefits and deficiencies that occur when an award vests, is exercised, or expires are recognized in income tax expense as discrete period items. Previously, these transactions were typically recorded directly within equity. Consistent with this change, excess tax benefits and deficiencies are no longer included within estimated proceeds when performing the calculation for diluted earnings per share. The presentation of excess tax benefits in the statement of cash flows shifted to an operating activity from the prior classification as a financing activity. ASU 2016-09 also provides an accounting policy election to recognize forfeitures of awards as they occur when estimating stock-based compensation expense rather than the previous requirement to estimate forfeitures from inception. ASU 2016-09 became effective for the Company for reporting periods after January 1, 2017. The actual effects of adoption in 2017 will primarily depend upon the share price of the Company s stock, probability of exercise of certain stock options and the magnitude of windfalls for all awards upon either vesting or exercise. The effects on earnings per share calculations and election to account for forfeitures as incurred have not been significant.

Recently Issued Accounting Pronouncements (Not Yet Effective)

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (Topic 606) . ASU 2014-09 replaced existing revenue recognition guidance for contracts to provide goods or services to customers. The new guidance clarifies the principles for recognizing revenue and replaces nearly all existing revenue recognition guidance in U.S. GAAP. Quantitative and qualitative disclosures regarding the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers are also required. ASU 2014-09 as amended by ASU 2015-14, ASU 2016-08, ASU 2016-10, ASU 2016-12 and ASU 2016-20, is effective for interim and annual periods beginning after December 15, 2017 and is applied on either a modified retrospective or full retrospective basis. Early adoption is permitted for interim and annual periods beginning after December 15, 2016. The Company s revenue is mainly comprised of net interest income from financial assets and liabilities and to a lesser degree, noninterest income. The scope of ASU 2014-09 explicitly excludes net interest income as well as other revenues associated with financial assets and liabilities, including loans and securities. Accordingly, the majority of the Company s revenues will not be affected. The Company will continue to evaluate the effect that this guidance will have on other revenue streams within its scope, as well as changes in disclosures required by the new guidance. However, adoption of this standard is not expected to have a material impact on the Company s consolidated financial statements.

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BROADWAY FINANCIAL CORPORATION AND SUBSIDIARY

Notes to Unaudited Consolidated Financial Statements (continued)

In January 2016, the FASB issued ASU 2016-01, Financial Instruments Overall (Subtopic 825-10) - Recognition and Measurement of Financial Assets and Financial Liabilities . ASU 2016-01 (i) requires equity investments, with certain exceptions, to be measured at fair value with changes in fair value recognized in net income; (ii) simplifies the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify impairment; (iii) eliminates the requirement for public business entities to disclose the methods and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost on the balance sheet; (iv) requires public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes; (v) requires an entity to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to measure the liability at fair value in accordance with the fair value option for financial instruments; (vi) requires separate presentation of financial assets and financial liabilities by measurement category and form of financial asset on the balance sheet or the accompanying notes to the financial statements; and (vii) clarifies that an entity should evaluate the need for a valuation allowance on a deferred tax asset related to available-for-sale securities. For public business entities, the amendments in ASU 2016-01 are effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. Early application by public business entities to financial statements of fiscal years or interim periods that have not yet been issued are permitted as of the beginning of the fiscal year of adoption. While the Company is currently evaluating the impact of this standard, the Company does not expect its adoption to have a material impact on the Company s consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842) . Under ASU 2016-02, lessees will be required to recognize the following for all leases (with the exception of short-term leases, as defined) at the commencement date: (i) a lease liability, which is a lessee s obligation to make lease payments arising from a lease, measured on a discounted basis; and (ii) a right-of-use asset, which is an asset that represents the lessee s right to use, or control the use of, a specified asset for the lease term. Under the new guidance, lessor accounting is largely unchanged. Public business entities should apply the amendments in ASU 2016-02 for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early adoption is permitted. Lessees (for capital and operating leases) and lessors (for sales-type, direct financing, and operating leases) must apply a modified retrospective transition approach for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. The Company has identified certain contracts with respect to leased real estate and office equipment that are within the scope of ASU 2016-02. As a lessee in operating lease arrangements that are not considered short-tem, effective January 1, 2019, the Company expects a gross-up of its Consolidated Statements of Condition as a result of recognizing lease liabilities and right of use assets. However, it will likely not have a significant impact on the Company s Consolidated Statements of Income and Comprehensive Income or Cash Flows.

In June 2016, the FASB issued ASU 2016-13, Financial Instruments Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments . ASU 2016-13 requires an organization to measure all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts. Financial institutions and other organizations will now use forward-looking information to form their credit loss estimates. Many of the loss estimation techniques applied today will still be permitted, although the inputs to those techniques will change to reflect the full amount of expected credit losses over the life of the related financial assets. Organizations will continue to use judgment to determine which loss estimation method is appropriate for their circumstances. Additionally, the ASU amends the accounting for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. For public business entities, ASU 2016-13 is effective for fiscal years beginning after December 15, 2019, and interim periods within those fiscal years. Early adoption is permitted. While the Company is still evaluating the impact on its consolidated financial statements, the Company expects that ASU 2016-13 may result in an increase in the allowance for credit losses due to the following factors: 1) the allowance for credit losses will increase to provide for expected credit losses over the remaining expected life of the loan portfolio, and will consider expected future changes in macroeconomic conditions; and 2) an allowance may be established for estimated credit losses on available-for-sale debt securities. The amount of increase will be impacted by the portfolio composition and quality, as well as the economic conditions and forecasts as of the adoption date. While the Company has begun its implementation efforts by identifying key interpretive issues, and assessing its processes and identifying the system requirements against the new guidance to determine what modifications may be required, the Company cannot yet determine the overall impact of the new standard on its consolidated financial statements.

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BROADWAY FINANCIAL CORPORATION AND SUBSIDIARY

Notes to Unaudited Consolidated Financial Statements (continued)

In August 2016, the FASB issued ASU 2016-15, Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments . ASU 2016-15 provides guidance on the classification of certain cash receipts and payments on the consolidated statement of cash flows in order to reduce diversity in practice. ASU 2016-15 is effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. Early adoption is permitted. Adoption of this standard is not expected to have a material impact on the Company s consolidated financial statements.

In November 2016, the FASB issued ASU 2016-18, Statement of Cash Flows (Topic 230): Restricted Cash . ASU 2016-18 requires entities to show the changes in the total of cash, cash equivalents, restricted cash and restricted cash equivalents in the statement of cash flows. As a result, entities will no longer present transfers between cash and cash equivalents and restricted cash and restricted cash equivalents in the statement of cash flows. ASU 2016-18 is effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years, where the guidance should be applied using a retrospective transition method to each period presented. Early adoption is permitted. Adoption of this standard is not expected to have a material impact on the Company s consolidated financial statements.

NOTE (2) Earnings Per Share of Common Stock

Basic earnings per share of common stock is computed pursuant to the two-class method by dividing net income available to common stockholders less dividends paid on participating securities (unvested shares of restricted common stock) and any undistributed earnings attributable to participating securities by the weighted average common shares outstanding during the period. The weighted average common shares outstanding includes the weighted average number of shares of common stock outstanding less the weighted average number of unvested shares of restricted common stock. ESOP shares are considered outstanding for this calculation unless unearned. Diluted earnings per share of common stock includes the dilutive effect of unvested stock awards and additional potential common shares issuable under stock options.

The following table shows how the Company computed basic and diluted earnings per share of common stock for the periods indicated:

	For the three months ended June 30,		For the six months ended June 30,	
	2017	2016	2017	2016
	(Dollars in thousands, except per share)			
Net income	$ 533	$ 319	$ 1,765	$ 952
Less net income attributable to participating securities	(1)	-	(4)	-
Income available to common stockholders	$ 532	$ 319	$ 1,761	$ 952

Weighted average common shares outstanding for basic earnings per common share	26,666,740	29,076,708	26,642,129	29,076,708
Add: dilutive effects of unvested restricted stock awards	56,552	-	63,655	-
Weighted average common shares outstanding for diluted earnings per common share	26,723,292	29,076,708	26,705,784	29,076,708
Earnings per common share - basic	$ 0.02	$ 0.01	$ 0.07	$ 0.03
Earnings per common share - diluted	$ 0.02	$ 0.01	$ 0.07	$ 0.03

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BROADWAY FINANCIAL CORPORATION AND SUBSIDIARY

Notes to Unaudited Consolidated Financial Statements (continued)

Stock options for 540,625 shares of common stock for the three and six months ended June 30, 2017 and 2016 were not considered in computing diluted earnings per common share because they were anti-dilutive.

NOTE (3) Securities

The following table summarizes the amortized cost and fair value of the available-for-sale investment securities portfolios as of the periods indicated and the corresponding amounts of unrealized gains and losses which are recognized in accumulated other comprehensive income (loss):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
		(In thousands)		
June 30, 2017:				
Residential mortgage-backed	$ 9,839	$ 201	$ -	$ 10,040
U.S. Government and federal agency	1,967	22	-	1,989
Total available-for-sale securities	$ 11,806	$ 223	$ -	$ 12,029
December 31, 2016:				
Residential mortgage-backed	$ 11,022	$ 192	$ -	$ 11,214
U.S. Government and federal agency	1,960	28	-	1,988
Total available-for-sale securities	$ 12,982	$ 220	$ -	$ 13,202

At June 30, 2017, the Bank had one U.S. Government and federal agency security with an amortized cost and an estimated fair value of $2.0 million and a contractual maturity of October 2, 2019. At June 30, 2017, the Bank had 24 residential mortgage-backed securities with an amortized cost of $9.8 million, an estimated fair value of $10.0 million and an estimated average remaining life of 4.0 years. Expected maturities may differ from contractual maturities if borrowers have the right to call or prepay obligations with or without call or prepayment penalties.

At June 30, 2017 and December 31, 2016, securities pledged to secure public deposits had a carrying amount of $537 thousand and $629 thousand, respectively. At June 30, 2017 and December 31, 2016, 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 six months ended June 30, 2017 and 2016.

NOTE (4) Loans Receivable Held for Sale

Loans receivable held for sale at June 30, 2017 totaled $39.0 million and consisted of multi-family loans. During the three and six months ended June 30, 2017, multi-family loans originated for sale totaled $37.2 million and $85.9 million, respectively. Sales of multi-family loans during the three and six months ended June 30, 2017 totaled $31.8 million and $46.6 million, respectively. There were no loans held for sale at December 31, 2016.

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BROADWAY FINANCIAL CORPORATION AND SUBSIDIARY

Notes to Unaudited Consolidated Financial Statements (continued)

NOTE (5) Loans Receivable Held for Investment

Loans receivable held for investment were as follows as of the periods indicated:

	June 30, 2017	December 31, 2016
	(In thousands)	
Real estate:		
Single family (1)	$ 95,828	$ 104,807
Multi-family	214,652	229,566
Commercial real estate	6,404	8,914
Church	34,449	37,826
Construction	950	837
Commercial other	344	308
Consumer	4	6
Gross loans receivable before deferred loan costs and premiums	352,631	382,264
Unamortized net deferred loan costs and premiums	1,923	1,793
Gross loans receivable	354,554	384,057
Allowance for loan losses	(4,246)	(4,603)
Loans receivable, net	$ 350,308	$ 379,454

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(1) Includes $77.0 million and $81.9 million of non-impaired purchased loans at June 30, 2017 and December 31, 2016, respectively, with no allowance for loan losses.

The following tables present the activity in the allowance for loan losses by loan type for the periods indicated:

	Three Months Ended June 30, 2017							
	Single family	Multi-family	Real Estate Commercial real estate	Church	Construction	Commercial - other	Consumer	Total
				(In thousands)				
Beginning balance	$ 330	$ 2,711	$ 75	$ 1,250	$ 9	$ 16	$ 1	$ 4,392
Provision for (recapture of) loan losses	(40)	8	2	(270)	-	1	(1)	(300)
Recoveries	30	-	-	124	-	-	-	154

Loans charged off	-	-	-	-	-	-	-	-
Ending balance	$ 320	$ 2,719	$ 77	$ 1,104	$ 9	$ 17	$ -	$ 4,246

Three Months Ended June 30, 2016

	Single family	Multi-family	Real Estate Commercial real estate	Church	Construction	Commercial - other	Consumer	Total
				(In thousands)				
Beginning balance	$ 528	$ 1,866	$ 444	$ 1,676	$ 3	$ 17	$ -	$ 4,534
Provision for (recapture of) loan losses	(87)	381	(452)	(86)	-	(7)	1	(250)
Recoveries	-	-	248	6	-	7	-	261
Loans charged off	-	-	-	-	-	-	-	-
Ending balance	$ 441	$ 2,247	$ 240	$ 1,596	$ 3	$ 17	$ 1	$ 4,545

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BROADWAY FINANCIAL CORPORATION AND SUBSIDIARY

Notes to Unaudited Consolidated Financial Statements (continued)

	Six Months Ended June 30, 2017							
	Single family	Multi-family	Real Estate Commercial real estate	Church	Construction	Commercial - other	Consumer	Total
	(In thousands)							
Beginning balance	$ 367	$ 2,659	$ 215	$ 1,337	$ 8	$ 17	$ -	$ 4,603
Provision for (recapture of) loan losses	(77)	60	(138)	(496)	1	-	-	(650)
Recoveries	30	-	-	263	-	-	-	293
Loans charged off	-	-	-	-	-	-	-	-
Ending balance	$ 320	$ 2,719	$ 77	$ 1,104	$ 9	$ 17	$ -	$ 4,246

	Six Months Ended June 30, 2016							
	Single family	Multi-family	Real Estate Commercial real estate	Church	Construction	Commercial - other	Consumer	Total
	(In thousands)							
Beginning balance	$ 597	$ 1,658	$ 469	$ 2,083	$ 3	$ 18	$ -	$ 4,828
Provision for (recapture of) loan losses	(156)	589	(477)	(499)	-	(8)	1	(550)
Recoveries	-	-	248	12	-	7	-	267
Loans charged off	-	-	-	-	-	-	-	-
Ending balance	$ 441	$ 2,247	$ 240	$ 1,596	$ 3	$ 17	$ 1	$ 4,545

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 and for the periods indicated:

	June 30, 2017							
	Single family	Multi-family	Real Estate Commercial real estate	Church	Construction	Commercial - other	Consumer	Total
	(In thousands)							
Allowance for loan losses:								
Ending allowance balance attributable to loans:								
Individually evaluated for impairment	$ 117	$ -	$ -	$ 452	$ -	$ 14	$ -	$ 583
Collectively evaluated for impairment	203	2,719	77	652	9	3	-	3,663
Total ending allowance balance	$ 320	$ 2,719	$ 77	$ 1,104	$ 9	$ 17	$ -	$ 4,246

Loans:								
Loans individually evaluated for impairment	$ 636	$ 632	$ -	$ 9,399	$ -	$ 65	$ -	$ 10,732
Loans collectively evaluated for impairment	95,682	215,788	6,410	24,712	947	279	4	343,822
Total ending loans balance	$ 96,318	$ 216,420	$ 6,410	$ 34,111	$ 947	$ 344	$ 4	$ 354,554

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BROADWAY FINANCIAL CORPORATION AND SUBSIDIARY

Notes to Unaudited Consolidated Financial Statements (continued)

	December 31, 2016							
	Single family	Multi-family	Real Estate Commercial real estate	Church	Construction	Commercial - other	Consumer	Total
	(In thousands)							
Allowance for loan losses:								
Ending allowance balance attributable to loans:								
Individually evaluated for impairment	$ 125	$ -	$ -	$ 516	$ -	$ 15	$ -	$ 656
Collectively evaluated for impairment	242	2,659	215	821	8	2	-	3,947
Total ending allowance balance	$ 367	$ 2,659	$ 215	$ 1,337	$ 8	$ 17	$ -	$ 4,603
Loans:								
Loans individually evaluated for impairment	$ 644	$ 642	$ -	$ 10,545	$ -	$ 66	$ -	$ 11,897
Loans collectively evaluated for impairment	104,688	230,798	8,921	26,678	827	242	6	372,160
Total ending loans balance	$ 105,332	$ 231,440	$ 8,921	$ 37,223	$ 827	$ 308	$ 6	$ 384,057

The following table presents information related to loans individually evaluated for impairment by loan type as of the periods indicated:

	June 30, 2017			December 31, 2016		
	Unpaid Principal Balance	Recorded Investment	Allowance for Loan Losses Allocated	Unpaid Principal Balance	Recorded Investment	Allowance for Loan Losses Allocated
	(In thousands)					
With no related allowance recorded:						
Multi-family	$ 632	$ 632	$ -	$ 642	$ 642	$ -
Church	6,068	3,819	-	5,946	3,589	-
With an allowance recorded:						
Single family	636	636	117	644	644	125
Church	5,739	5,580	452	7,330	6,956	516
Commercial - other	65	65	14	66	66	15
Total	$ 13,140	$ 10,732	$ 583	$ 14,628	$ 11,897	$ 656

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.

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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 periods indicated.

	Three Months Ended June 30, 2017		Six Months Ended June 30, 2017	
	Average Recorded Investment	Cash Basis Interest Income Recognized	Average Recorded Investment	Cash Basis Interest Income Recognized
	(In thousands)			
Single family	$ 638	$ 7	$ 640	$ 14
Multi-family	635	12	638	23
Commercial real estate	992	104	567	104
Church	9,625	109	9,998	336
Commercial other	66	1	66	2
Total	$ 11,956	$ 233	$ 11,909	$ 479

	Three Months Ended June 30, 2016		Six Months Ended June 30, 2016	
	Average Recorded Investment	Cash Basis Interest Income Recognized	Average Recorded Investment	Cash Basis Interest Income Recognized
	(In thousands)			
Single family	$ 927	$ 7	$ 939	$ 14
Multi-family	966	11	1,102	52
Commercial real estate	1,746	211	1,825	267
Church	10,915	121	11,061	247
Commercial -other	66	2	67	2
Total	$ 14,620	$ 352	$ 14,994	$ 582

Cash-basis interest income recognized represents cash received for interest payments on accruing impaired loans and interest recoveries on non-accrual loans that were paid off. 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 or paid off. When a loan is returned to accrual status, the interest payments that were previously applied to principal are deferred and amortized over the remaining life of the loan. Foregone interest income that would have been recognized had loans performed in accordance with their original terms amounted to $28 thousand and $0 for the three months ended June 30, 2017 and 2016, respectively, and $74 thousand and $97 thousand for the six months ended June 30, 2017 and 2016, 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 by loan type as of the periods indicated:

	June 30, 2017				
	30-59 Days Past Due	60-89 Days Past Due	Greater than 90 Days Past Due	Total Past Due	Current
	(In thousands)				
Loans receivable held for investment:					
Single family	$ -	$ 57	$ -	$ 57	$ 96,261
Multi-family	-	-	-	-	216,420
Commercial real estate	-	-	-	-	6,410
Church	371	-	1,242	1,613	32,498
Construction	-	-	-	-	947
Commercial - other	-	-	-	-	344
Consumer	-	-	-	-	4
Total	$ 371	$ 57	$ 1,242	$ 1,670	$ 352,884

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	December 31, 2016				
	30-59 Days Past Due	60-89 Days Past Due	Greater than 90 Days Past Due	Total Past Due	Current
			(In thousands)		
Loans receivable held for investment:					
Single family	$ -	$ 64	$ -	$ 64	$ 105,268
Multi-family	-	-	-	-	231,440
Commercial real estate	1,324	-	-	1,324	7,597
Church	-	-	-	-	37,223
Construction	-	-	-	-	827
Commercial - other	-	-	-	-	308
Consumer	-	-	-	-	6
Total	$ 1,324	$ 64	$ -	$ 1,388	$ 382,669

As of June 30, 2017 and December 31, 2016, the recorded investment in non-accrual loans totaled $2.8 million and $2.9 million, respectively, and consisted entirely of church loans. There were no loans 90 days or more delinquent that were accruing interest as of June 30, 2017 or December 31, 2016.

Troubled Debt Restructurings

At June 30, 2017, loans classified as troubled debt restructurings (TDRs) totaled $10.3 million, of which $2.4 million were included in non-accrual loans and $7.9 million were on accrual status. At December 31, 2016, loans classified as TDRs totaled $11.5 million, of which $2.5 million were included in non-accrual loans and $9.0 million were on accrual status. The Company has allocated $583 thousand and $656 thousand of specific reserves for accruing TDRs as of June 30, 2017 and December 31, 2016, respectively. 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 June 30, 2017 and December 31, 2016, 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 or six months ended June 30, 2017 and 2016.

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.

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- ***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 and/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 categories of loans by loan type as of the periods indicated were as follows:

	June 30, 2017					
	Pass	Watch	Special Mention	Substandard	Doubtful	Loss
	(In thousands)					
Single family	$ 96,318	$ -	$ -	$ -	$ -	$ -
Multi-family	215,138	-	-	1,282	-	-
Commercial real estate	6,287	123	-	-	-	-
Church	26,998	446	269	6,398	-	-
Construction	947	-	-	-	-	-
Commercial - other	279	-	-	65	-	-
Consumer	4	-	-	-	-	-
Total	$ 345,971	$ 569	$ 269	$ 7,745	$ -	$ -

	December 31, 2016					
	Pass	Watch	Special Mention	Substandard	Doubtful	Loss
	(In thousands)					
Single family	$ 105,332	$ -	$ -	$ -	$ -	$ -
Multi-family	228,522	1,274	342	1,302	-	-
Commercial real estate	6,965	-	-	1,956	-	-
Church	27,560	1,143	823	7,697	-	-

Construction	827	-	-	-	-	-
Commercial - other	242	-	-	66	-	-
Consumer	6	-	-	-	-	-
Total	$ 369,454	$ 2,417	$ 1,165	$ 11,021	$ -	$ -

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BROADWAY FINANCIAL CORPORATION AND SUBSIDIARY

Notes to Unaudited Consolidated Financial Statements (continued)

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 3.81% at June 30, 2017. 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 through March 2019 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 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.

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).

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.

Appraisals for collateral-dependent impaired loans 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.

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BROADWAY FINANCIAL CORPORATION AND SUBSIDIARY

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Assets Measured on a Recurring Basis

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

	Fair Value Measurement			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
	(In thousands)			
At June 30, 2017:				
Securities available-for-sale - residential mortgage-backed	$ -	$ 10,040	$ -	$ 10,040
Securities available-for-sale - U.S. Government and federal agency	1,989	-	-	1,989
At December 31, 2016:				
Securities available-for-sale - residential mortgage-backed	$ -	$ 11,214	$ -	$ 11,214
Securities available-for-sale - U.S. Government and federal agency	1,988	-	-	1,988

There were no transfers between Level 1, Level 2, or Level 3 during the three and six months ended June 30, 2017 and 2016.

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 statement of condition. 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 as of the periods indicated. The fair value measurement for all of these assets falls within Level 3 of the fair value hierarchy.

	June 30, 2017	December 31, 2016
	(In thousands)	
Impaired loans carried at fair value of collateral	$ 1,652	$ 1,744

There were no losses recognized on assets measured at fair value on a non-recurring basis for the three and six months ended June 30, 2017 and 2016.

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Notes to Unaudited Consolidated Financial Statements (continued)

The following table presents the valuation methodology and unobservable inputs for Level 3 assets measured at fair value on a nonrecurring basis as of June 30, 2017 and December 31, 2016:

	Valuation Technique(s)	Unobservable Input(s)	Range	Weighted Average
June 30, 2017:				
Impaired loans	Third Party Appraisals	Adjustment for differences between the comparable sales	-16% to 0%	-3%
December 31, 2016:				
Impaired loans	Third Party Appraisals	Adjustment for differences between the comparable sales	-2% to 0%	-1%

Fair Values of Financial Instruments

The carrying amounts and estimated fair values of financial instruments as of the periods indicated were as follows:

	Carrying Value	Fair Value Measurements at June 30, 2017			
		Level 1	Level 2 (In thousands)	Level 3	Total
Financial Assets:					
Cash and cash equivalents	$ 16,835	$ 16,835	$ -	$ -	$ 16,835
Securities available-for-sale	12,029	1,989	10,040	-	12,029
Loans receivable held for sale	39,037	-	39,597	-	39,597
Loans receivable held for investment	350,308	-	-	351,238	351,238
Accrued interest receivable	1,103	57	71	975	1,103
Federal Home Loan Bank stock	2,916	2,916	-	-	2,916
Financial Liabilities:					
Deposits	$ 273,847	$ -	$ 264,619	$ -	$ 264,619
Federal Home Loan Bank advances	104,000	-	104,418	-	104,418
Junior subordinated debentures	5,100	-	-	4,458	4,458
Accrued interest payable	105	-	98	7	105

	Carrying Value	Fair Value Measurements at December 31, 2016			
		Level 1	Level 2 (In thousands)	Level 3	Total
Financial Assets:					

Cash and cash equivalents	$ 18,430	$ 18,430	$ -	$ -	$ 18,430
Securities available-for-sale	13,202	1,988	11,214	-	13,202
Loans receivable held for investment	379,454	-	-	382,717	382,717
Accrued interest receivable	1,178	64	29	1,085	1,178
Federal Home Loan Bank stock	2,573	2,573	-	-	2,573
Financial Liabilities:					
Deposits	$ 287,427	$ -	$ 278,254	$ -	$ 278,254
Federal Home Loan Bank advances	85,000	-	85,748	-	85,748
Junior subordinated debentures	5,100	-	-	4,414	4,414
Accrued interest payable	154	-	147	7	154

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Notes to Unaudited Consolidated Financial Statements (continued)

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.

(c) Loans Receivable Held For investment

Fair values of loans 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.

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BROADWAY FINANCIAL CORPORATION AND SUBSIDIARY

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NOTE (8) Stock-based Compensation

The Company issues stock-based compensation awards to its directors and employees under the 2008 Long-Term Incentive Plan (2008 LTIP). The 2008 LTIP permits the grant of non-qualified and incentive stock options, stock appreciation rights, full value awards and cash incentive awards for up to 2,000,000 shares of common stock. As of June 30, 2017, there were 1,308,890 shares available for future awards under the 2008 LTIP.

No stock options were granted during the six months ended June 30, 2017, compared to 450,000 stock options granted to senior executive officers under the 2008 LTIP during the six months ended June 30, 2016. These options have an exercise price of $1.62 per share, vest over five years and expire ten years from the grant date. The Company estimated the compensation costs and fair value per share of these stock options to be $194 thousand and $0.43 per share, respectively, using the Black-Scholes option pricing model and the following assumptions: (i) expected volatility of 27.36%; (ii) risk free interest rate of 1.21%; (iii) expected option term of five years; and (iv) 0% dividend yield.

The following table summarizes stock option activity during the six months ended June 30, 2017 and 2016:

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (years)	Aggregate Intrinsic Value
Six Months Ended June 30, 2017:				
Outstanding at January 1, 2017	540,625	$ 2.18		
Granted	-	-		
Exercised	-	-		
Forfeited	-	-		
Outstanding at June 30, 2017	540,625	$ 2.18	7.50	$ 225,000
Exercisable at June 30, 2017	180,625	$ 3.29	5.19	$ 45,000
Six Months Ended June 30, 2016:				
Outstanding at January 1, 2016	90,625	$ 4.95		
Granted	450,000	1.62		
Exercised	-	-		
Forfeited	-	-		
Outstanding at June 30, 2016	540,625	$ 2.18	8.50	$ 86,000
Exercisable at June 30, 2016	90,625	$ 4.95	2.75	$ -

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BROADWAY FINANCIAL CORPORATION AND SUBSIDIARY

Notes to Unaudited Consolidated Financial Statements (continued)

The Company recorded $10 thousand of stock-based compensation expense related to stock options during the three months ended June 30, 2017 and 2016, respectively, and $19 thousand and $13 thousand during the six months ended June 30, 2017 and 2016, respectively. As of June 30, 2017, unrecognized compensation cost related to non-vested stock options granted under the plan was $142 thousand. The cost is expected to be recognized over a period of 3.65 years.

In March 2016, the Company awarded 120,483 shares of restricted stock to its Chief Executive Officer (CEO) under the 2008 LTIP. A restricted stock award is valued at the closing price of the Company s stock on the date of such award. Subject to certain performance restrictions, 100,000 shares of restricted stock shall vest over a two-year period and the remaining 20,483 shares shall vest over a three-year period. Stock-based compensation expense is recognized on a straight-line basis over the vesting period. The Company recorded $27 thousand and $26 thousand of stock-based compensation expense related to this award during the three months ended June 30, 2017 and 2016, respectively, and $53 thousand and $26 thousand during the six months ended June 30, 2017 and 2016, respectively. As of June 30, 2017, unrecognized compensation cost related to non-vested restricted stock award was $92 thousand, of which $79 thousand is expected to be recognized over a period of 9 months and $13 thousand is expected to be recognized over a period of 12 months.

In April 2017, the Company awarded 30,002 shares of common stock to its directors under the 2008 LTIP, all of which are fully vested. The Company recorded $52 thousand of compensation expense based on the fair value of the stock, which was determined using the average of the high and the low price of the stock on the date of the award.

In April 2017, the Company also awarded 129,270 of cash-settled restricted stock units (RSUs) to its CEO under the 2008 LTIP. The RSUs cliff vest at the end of two years from the date of the grant and are subject to forfeiture until vested. Each RSU entitles the CEO to receive cash equal to the fair market value of one share of common stock on the applicable payout date. Compensation expense is determined based on the fair value of the award and is re-measured at each reporting period. The Company recorded $23 thousand of compensation expense related to this award during the three months ended June 30, 2017.

NOTE (9) ESOP Plan

Employees participate in an Employee Stock Option Plan (ESOP) after attaining certain age and service requirements. In December 2016, the ESOP purchased 1,493,679 shares of the Company s common stock at $1.59 per share, for a total cost of $2.4 million, of which $1.2 million was funded with a loan from the Company. The loan will be repaid from the Bank s annual discretionary contributions to the ESOP, net of dividends paid, over a period of 20 years. Shares of the Company s common stock purchased by the ESOP are held in a suspense account until released for allocation to participants. When loan payments are made, shares are allocated to each eligible participant based on the ratio of each such participant s compensation, as defined in the ESOP, to the total compensation of all eligible plan participants. As the unearned shares are released from the suspense account, the Company recognizes compensation expense equal to the fair value of the ESOP shares during the periods in which they become committed to be released. To the extent that the fair value of the ESOP shares released differs from the cost of such shares, the difference is charged or credited to equity as additional paid-in capital. Dividends on allocated shares increase participant accounts. At the end of employment, participants will receive shares for their vested balance. Compensation expense related to the ESOP was $25 thousand and $19 thousand for the three months ended June 30, 2017 and 2016, respectively, and $47 thousand and $45 thousand for the six months ended June 30, 2017 and 2016, respectively.

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Shares held by the ESOP were as follows:

	June 30, 2017	December 31, 2016
	(Dollars in thousands)	
Allocated to participants	1,114,683	1,114,683
Suspense shares	739,748	739,748
Total ESOP shares	1,854,431	1,854,431
Fair value of unearned shares	$ 1,512	$ 1,213

The outstanding balance of unallocated shares at June 30, 2017 and December 31, 2016, was $1.1 million and $1.2 million, respectively, which is shown as Unearned ESOP shares in the equity section of the consolidated statements of financial condition. As of June 30, 2017, 26,750 shares were committed to be released.

NOTE (10) Regulatory Matters

The Bank s capital requirements are administered by the Office of the Comptroller of the Currency (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.

The federal banking regulators approved final capital rules (Basel III Capital Rules) in July 2013 implementing the Basel III framework as well as certain provisions of the Dodd-Frank Act. The Basel III Capital Rules prescribe a standardized approach for calculating risk-weighted assets and revised the definition and calculation of Tier 1 capital and Total capital, and include a new Common Equity Tier 1 capital (CET1) measure. Under the Basel III Capital Rules, the currently effective minimum capital ratios are:

- 4.5% CET1 to risk-weighted assets;
- 6.0% Tier 1 capital (that is, CET1 plus Additional Tier 1 capital) to risk-weighted assets;
- 8.0% Total capital (that is, Tier 1 capital plus Tier 2 capital) to risk-weighted assets; and
- 4.0% Tier 1 capital to average consolidated assets (known as the leverage ratio).

A new capital conservation buffer was also established above the regulatory minimum capital requirements. This capital conservation buffer was 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 it reaches its final level of 2.5% on January 1, 2019.

The Basel III Capital rules also contain revisions to the prompt corrective action framework, which is designed to place restrictions on insured depository institutions if their capital levels begin to show signs of weakness. Under the prompt corrective action requirements, which are designed to complement the capital conservation buffer, insured depository institutions are now required to meet the following increased capital level requirements in order to qualify as well capitalized : (i) a CET1 capital ratio of 6.5%; (ii) a Tier 1 capital ratio of 8% (increased from 6%); (iii) a total capital ratio of 10% (unchanged from previous rules); and (iv) a Tier 1 leverage ratio of 5% (unchanged from previous rules).

The Basel III Capital Rules became effective for the Bank on January 1, 2015 (subject to a phase-in period for certain provisions). At June 30, 2017 and December 31, 2016, the Bank s level of capital exceeded all regulatory capital requirements and its regulatory capital ratios were above the minimum levels required to be considered well capitalized for regulatory purposes. Actual and required capital amounts and ratios as of the periods indicated are presented below.

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Notes to Unaudited Consolidated Financial Statements (continued)

	Actual		Minimum Capital Requirements		Minimum Required To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
			(Dollars in thousands)			
June 30, 2017:						
Tier 1 (Leverage)	$ 47,009	10.51%	$ 17,884	4.0%	$ 22,356	5.0%
Common Equity Tier 1	$ 47,009	15.87%	$ 13,333	4.5%	$ 19,258	6.5%
Tier 1	$ 47,009	15.87%	$ 17,777	6.0%	$ 23,703	8.0%
Total Capital	$ 50,720	17.12%	$ 23,703	8.0%	$ 29,628	10.0%
December 31, 2016:						
Tier 1 (Leverage)	$ 43,954	10.60%	$ 16,594	4.0%	$ 20,742	5.0%
Common Equity Tier 1	$ 43,954	15.36%	$ 12,875	4.5%	$ 18,597	6.5%
Tier 1	$ 43,954	15.36%	$ 17,166	6.0%	$ 22,888	8.0%
Total Capital	$ 47,544	16.62%	$ 22,888	8.0%	$ 28,610	10.0%

Effective as of May 15, 2015, the Federal Reserve Board (FRB) adopted a final rule that exempts bank holding companies and savings and loan holding companies with less than $1 billion in consolidated assets, such as the Company, from FRB s consolidated regulatory capital requirements.

NOTE (11) Income Taxes

The Company and its subsidiary 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 evaluated 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. Based on this analysis, the Company determined that as of June 30, 2017, no valuation allowance was required on its deferred tax assets, which totaled $6.0 million. As of December 31, 2016, the Company recorded no valuation allowance on its deferred tax assets of $6.9 million.

NOTE (12) Concentration of Credit Risk

The Bank has a significant concentration of deposits with a long-time customer that accounted for approximately 12% of its deposits as of June 30, 2017. The Bank expects to maintain this relationship with the customer.

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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, 2016. Certain statements herein are forward-looking statements within the meaning of Section 21E of the U.S. Securities Exchange Act of 1934, as amended (the Exchange Act) and Section 27A of the U.S. Securities Act of 1933, as amended, that reflect our current views with respect to future events and financial performance. Forward-looking statements typically include the words anticipate, believe, estimate, expect, project, plan, forecast, intend, and other similar expressions. These forward-looking statements are subject t uncertainties, which could cause actual future results to differ materially from historical results or from those anticipated or implied by such statements. Readers should not place undue reliance on these forward-looking statements, which speak only as of their dates or, if no date is provided, then as of the date of this Form 10-Q. We undertake no obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, except to the extent required by law.

Critical Accounting Policies and Estimates

Our significant accounting policies, which are essential to understanding Management s Discussion and Analysis of Financial Condition and Results of Operations, are described in the Notes to Consolidated Financial Statements and in the Critical Accounting Policies section of Management s Discussion and Analysis of Financial Condition and Results of Operations in our Annual Report on Form 10-K for the year ended December 31, 2016. There have been no material changes to our critical accounting policies.

Overview

Total assets increased by $6.4 million during the first half of 2017, primarily reflecting an increase of $39.0 million in loans receivable held for sale, which was partially offset by a decrease of $29.1 million in loans receivable held for investment, a decrease of $1.6 million in cash and cash equivalents, a decrease of $1.2 million in securities available-for-sale and a decrease of $932 thousand in deferred tax assets.

During the first half of 2017, total deposits decreased by $13.6 million and FHLB advances increased by $19.0 million.

We recorded net income of $533 thousand and $1.8 million for the three and six months ended June 30, 2017, respectively, compared to $319 thousand and $952 thousand for the three and six months ended June 30, 2016, respectively. The increase in net income during the three months ended June 30, 2017 compared to the second quarter of 2016 primarily resulted from higher net interest income, higher recaptures of loan loss provisions, higher non-interest income (primarily from gains on sales of loans), and lower non-interest expense, which were partially offset by higher income tax expense.

The increase in net income for the six months ended June 30, 2017 compared to the first half of 2016 primarily reflected higher non-interest income, which reflected an insurance litigation settlement and higher gains on sales of loans. In addition, net income increased during the first half of 2017 because of higher net interest income, higher recaptures of loan loss provisions, and lower non-interest expense, partially offset by higher income tax expense.

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Results of Operations

Net Interest Income

Net interest income for the second quarter of 2017 totaled $3.0 million, compared to $2.8 million for the second quarter of 2016. The slight increase in net interest income of $161 thousand primarily resulted from an increase in the average balance of loans receivable (including loans held for sale), which was partially offset by a decrease in net interest margin.

During the second quarter of 2017, the average balance of loans receivable increased by $64.1 million, which increased interest income by $654 thousand. However, the average yield on loans decreased by 34 basis points compared to the second quarter of 2016, which reduced interest income by $301 thousand. The decrease in the average yield on loans primarily resulted from the payoff of loans with higher interest rates than those originated over the last year. The lower interest rates on loan originations primarily reflect the overall continued low interest rate environment and competitive market conditions.

The increase of $353 thousand in interest income on loans was partially offset by higher interest expense on deposits and FHLB advances for the second quarter of 2017 compared to the second quarter of 2016. Interest expense on deposits increased by $86 thousand, primarily due to an increase of $34.2 million in the average balance of deposits and an increase of 2 basis points in the average cost of deposits compared to the second quarter of 2016. The higher average balance of deposits increased interest expense by $71 thousand and the higher average cost of deposits increased interest expense by $15 thousand. Interest expense on FHLB advances increased by $109 thousand, primarily due to an increase of $29.4 million in the average balance of FHLB advances, which increased interest expense by $148 thousand, offset in part by a decrease of 20 basis points in the average cost of FHLB advances, which reduced interest expense by $39 thousand.

For the six months ended June 30, 2017, net interest income increased by $569 thousand to $6.1 million from $5.5 million for the same period a year ago, as the impact of a higher average balance of loans receivable more than offset the impact of a lower net interest margin.

During the first half of 2017, the average balance of loans receivable increased by $71.2 million, which increased interest income by $1.5 million. However, the average yield on loans decreased by 33 basis points compared to the first half of 2016, which reduced interest income by $565 thousand.

The increase of $888 thousand in interest income on loans was partially offset by higher interest expense on deposits and borrowings for the first half of 2017 compared to the first half of 2016. Interest expense on deposits increased by $143 thousand, primarily due to an increase of $31.9 million in the average balance of deposits and an increase of one basis point in the average cost of deposits compared to the second quarter of 2016. The higher average balance of deposits increased interest expense by $132 thousand and the higher average cost of deposits increased interest expense by $11 thousand. Interest expense on borrowings increased by $173 thousand, primarily due to an increase of $24.6 million in the average balance of FHLB advances, which increased interest expense by $246 thousand, offset in part by a decrease of 22 basis points in the average cost of FHLB advances, which reduced interest expense by $86 thousand. Additionally, the cost of Debentures increased by 51 basis points and resulted in additional interest expense of $13 thousand.

Our net interest margin decreased by 9 basis points to 2.80% for the six months ended June 30, 2017 from 2.89% for the same period in 2016, primarily due to a lower average yield on interest earning assets.

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The following tables set forth average balances, 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					
	June 30, 2017			June 30, 2016		
(Dollars in Thousands)	Average Balance	Interest	Average Yield/ Cost	Average Balance	Interest	Average Yield/ Cost
Assets						
Interest-earning assets:						
Interest-earning deposits	$ 30,195	$ 83	1.10%	$ 6,480	$ 6	0.37%
Federal funds sold	-	-	-	24,325	29	0.48%
Securities	12,363	73	2.36%	15,057	84	2.23%
Loans receivable (1)	396,244	3,944	3.98%	332,184	3,591	4.32%
FHLB stock	2,878	36	5.00%	2,573	63	9.79%
Total interest-earning assets	441,680	$ 4,136	3.75%	380,619	$ 3,773	3.97%
Non-interest-earning assets	10,803			9,032		
Total assets	$ 452,483			$ 389,651		
Liabilities and Stockholders Equity						
Interest-bearing liabilities:						
Money market deposits	$ 33,143	$ 54	0.65%	$ 25,860	$ 36	0.56%
Passbook deposits	39,970	32	0.32%	36,444	29	0.32%
NOW and other demand deposits	31,718	3	0.04%	29,804	5	0.07%
Certificate accounts	189,647	508	1.07%	168,140	441	1.05%
Total deposits	294,478	597	0.81%	260,248	511	0.79%
FHLB advances	100,418	490	1.95%	71,044	381	2.15%
Junior subordinated debentures	5,100	47	3.69%	5,100	40	3.14%
Total interest-bearing liabilities	399,996	$ 1,134	1.13%	336,392	$ 932	1.11%
Non-interest-bearing liabilities	5,222			6,200		
Stockholders Equity	47,265			47,059		
Total liabilities and stockholders equity	$ 452,483			$ 389,651		
Net interest rate spread (2)		$ 3,002	2.62%		$ 2,841	2.86%
Net interest rate margin (3)			2.72%			2.99%
Ratio of interest-earning assets to interest-bearing liabilities			110.42%			113.15%

(1) Amount is net of deferred loan fees, loan discounts and loans in process, and includes deferred origination costs, loan premiums and loans receivable held for sale. The Company did not have any loans receivable held for sale during the three months ended June 30, 2016.

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

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

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	For the six months ended	
	June 30, 2017	June 30, 2016