

BankFinancial CORP
Form 10-Q
April 26, 2017

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

For the Quarterly Period ended March 31, 2017

or

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

For transition period from _____ to _____
Commission File Number 0-51331

BANKFINANCIAL CORPORATION
(Exact Name of Registrant as Specified in Charter)

Maryland 75-3199276
(State or Other Jurisdiction (I.R.S. Employer
of Incorporation) Identification No.)

15W060 North Frontage Road, Burr Ridge,
Illinois 60527

(Address of Principal Executive Offices)

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

Not Applicable

(Former name, former address and former fiscal year, if changed since last report)

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

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

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

Large accelerated filer Accelerated filer
Non-accelerated filer Smaller reporting company
Emerging growth company

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

Edgar Filing: BankFinancial CORP - Form 10-Q

Exchange Act. "

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock as of the latest practicable date. At April 24, 2017, there were 18,379,256 shares of Common Stock, \$0.01 par value, outstanding.

BANKFINANCIAL CORPORATION

Form 10-Q

March 31, 2017

Table of Contents

	Page Number
<u>PART I</u>	
Item 1. <u>Financial Statements</u>	<u>1</u>
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>27</u>
Item 3. <u>Quantitative and Qualitative Disclosure about Market Risk</u>	<u>39</u>
Item 4. <u>Controls and Procedures</u>	<u>40</u>
<u>PART II</u>	
Item 1. <u>Legal Proceedings</u>	<u>41</u>
Item 1A. <u>Risk Factors</u>	<u>41</u>
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	<u>41</u>
Item 3. <u>Defaults Upon Senior Securities</u>	<u>41</u>
Item 4. <u>Mine Safety Disclosures</u>	<u>41</u>
Item 5. <u>Other Information</u>	<u>41</u>
Item 6. <u>Exhibits</u>	<u>41</u>
<u>Signatures</u>	<u>43</u>

Table of Contents

BANKFINANCIAL CORPORATION
CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION
(In thousands, except share and per share data) - Unaudited

	March 31, 2017	December 31, 2016
Assets		
Cash and due from other financial institutions	\$10,247	\$13,053
Interest-bearing deposits in other financial institutions	65,219	83,631
Cash and cash equivalents	75,466	96,684
Securities, at fair value	110,230	107,212
Loans receivable, net of allowance for loan losses: March 31, 2017, \$7,971 and December 31, 2016, \$8,127	1,319,287	1,312,952
Other real estate owned, net	5,301	3,895
Stock in Federal Home Loan Bank and Federal Reserve Bank, at cost	8,147	11,650
Premises and equipment, net	31,149	31,413
Accrued interest receivable	4,478	4,381
Core deposit intangible	653	782
Bank owned life insurance	22,657	22,594
Deferred taxes	22,103	22,411
Other assets	4,002	6,063
Total assets	\$1,603,473	\$1,620,037
Liabilities		
Deposits		
Noninterest-bearing	\$234,415	\$249,539
Interest-bearing	1,094,867	1,089,851
Total deposits	1,329,282	1,339,390
Borrowings	52,046	51,069
Advance payments by borrowers for taxes and insurance	9,068	11,041
Accrued interest payable and other liabilities	11,056	13,757
Total liabilities	1,401,452	1,415,257
Stockholders' equity		
Preferred Stock, \$0.01 par value, 25,000,000 shares authorized, none issued or outstanding	—	—
Common Stock, \$0.01 par value, 100,000,000 shares authorized; 18,440,440 shares issued at March 31, 2017 and 19,233,760 issued at December 31, 2016	184	192
Additional paid-in capital	161,265	173,047
Retained earnings	40,209	39,483
Unearned Employee Stock Ownership Plan shares	—	(8,318)
Accumulated other comprehensive income	363	376
Total stockholders' equity	202,021	204,780
Total liabilities and stockholders' equity	\$1,603,473	\$1,620,037

See accompanying notes to the consolidated financial statements.

Table of Contents

BANKFINANCIAL CORPORATION
CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except share and per share data) - Unaudited

	Three Months Ended March 31,	
	2017	2016
Interest and dividend income		
Loans, including fees	\$12,760	\$ 12,347
Securities	349	314
Other	253	98
Total interest income	13,362	12,759
Interest expense		
Deposits	1,180	787
Borrowings	96	69
Total interest expense	1,276	856
Net interest income	12,086	11,903
Provision for (recovery of) loan losses	161	(490)
Net interest income after provision for (recovery of) loan losses	11,925	12,393
Noninterest income		
Deposit service charges and fees	529	567
Other fee income	481	495
Insurance commissions and annuities income	77	55
Gain on sale of loans, net	7	18
Gain on sale of securities (includes \$46 accumulated other comprehensive income reclassifications for unrealized net gains on available for sale securities for the three months ended March 31, 2016)	—	46
Loan servicing fees	68	73
Amortization and impairment of servicing assets	(31)	(31)
Earnings on bank owned life insurance	63	51
Trust income	172	160
Other	178	160
Total noninterest income	1,544	1,594
Noninterest expense		
Compensation and benefits	6,352	5,993
Office occupancy and equipment	1,622	1,647
Advertising and public relations	381	222
Information technology	753	724
Supplies, telephone, and postage	332	376
Amortization of intangibles	129	136
Nonperforming asset management	104	84
Operations of other real estate owned	213	376
FDIC insurance premiums	187	217
Other	1,193	1,155
Total noninterest expense	11,266	10,930
Income before income taxes	2,203	3,057
Income tax expense	322	1,153
Net income	\$1,881	\$ 1,904
Basic earnings per common share	\$0.10	\$ 0.10

Edgar Filing: BankFinancial CORP - Form 10-Q

Diluted earnings per common share	\$0.10	\$0.10
Weighted average common shares outstanding	18,642,054	19,428,551
Diluted weighted average common shares outstanding	18,647,516	19,431,490

See accompanying notes to the consolidated financial statements.

2

Table of Contents

BANKFINANCIAL CORPORATION
 CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
 (In thousands) - Unaudited

	Three Months Ended March 31,	
	2017	2016
Net income	\$1,881	\$1,904
Unrealized holding loss arising during the period	(20)	(22)
Tax effect	7	8
Net of tax	(13)	(14)
Reclassification adjustment for gain included in net income	—	(46)
Tax effect, included in income tax expense	—	18
Reclassification adjustment for gain included in net income, net of tax	—	(28)
Other comprehensive loss	(13)	(42)
Comprehensive income	\$1,868	\$1,862

See accompanying notes to the consolidated financial statements.

Table of Contents

BANKFINANCIAL CORPORATION

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

(In thousands, except per share data) - Unaudited

	Common Stock	Additional Paid-in Capital	Retained Earnings	Unearned Employee Stock Ownership Plan Shares	Accumulated Other Comprehen-sive Income	Total
Balance at January 1, 2016	\$ 203	\$ 184,797	\$ 36,114	\$ (9,297)	\$ 547	\$ 212,364
Net income	—	—	1,904	—	—	1,904
Other comprehensive loss, net of tax	—	—	—	—	(42)	(42)
Repurchase and retirement of common stock (357,817 shares)	(4)	(4,389)	—	—	—	(4,393)
Nonvested stock awards-stock-based compensation expense	—	377	—	—	—	377
Cash dividends declared on common stock (\$0.05 per share)	—	—	(1,010)	—	—	(1,010)
ESOP shares earned	—	45	—	243	—	288
Balance at March 31, 2016	\$ 199	\$ 180,830	\$ 37,008	\$ (9,054)	\$ 505	\$ 209,488
Balance at January 1, 2017	\$ 192	\$ 173,047	\$ 39,483	\$ (8,318)	\$ 376	\$ 204,780
Net income	—	—	1,881	—	—	1,881
Other comprehensive loss, net of tax	—	—	—	—	(13)	(13)
Net exercise of stock options (192,215 shares)	2	(1,220)	—	—	—	(1,218)
Prepayment of ESOP Share Acquisition Loan	(8)	(7,185)	—	8,318	—	1,125
Repurchase and retirement of common stock (232,045 shares)	(2)	(3,377)	—	—	—	(3,379)
Cash dividends declared on common stock (\$0.06 per share)	—	—	(1,155)	—	—	(1,155)
Balance at March 31, 2017	\$ 184	\$ 161,265	\$ 40,209	\$ —	\$ 363	\$ 202,021

See accompanying notes to the consolidated financial statements.

Table of Contents

BANKFINANCIAL CORPORATION
 CONSOLIDATED STATEMENTS OF CASH FLOWS
 (In thousands) - Unaudited

	Three Months Ended March 31,	
	2017	2016
Cash flows from operating activities		
Net income	\$1,881	\$1,904
Adjustments to reconcile to net income to net cash from operating activities		
Provision for (recovery of) loan losses	161	(490)
Prepayment of ESOP Share Acquisition Loan	1,125	—
ESOP shares earned	—	288
Stock-based compensation expense	—	377
Depreciation and amortization	958	939
Amortization of premiums and discounts on securities and loans	(65)	(37)
Amortization of core deposit intangible	129	136
Amortization of servicing assets	31	31
Net change in net deferred loan origination costs	129	(40)
Net loss on sale of other real estate owned	16	38
Net gain on sale of loans	(7)	(18)
Net gain on sale of securities	—	(46)
Loans originated for sale	(239)	(360)
Proceeds from sale of loans	246	378
Other real estate owned valuation adjustments	20	119
Net change in:		
Accrued interest receivable	(97)	(120)
Earnings on bank owned life insurance	(63)	(51)
Other assets	1,834	2,198
Accrued interest payable and other liabilities	(2,701)	(218)
Net cash from operating activities	3,358	5,028
Cash flows from investing activities		
Securities		
Proceeds from maturities	13,623	17,453
Proceeds from principal repayments	637	1,126
Proceeds from sales of securities	—	46
Purchases of securities	(17,302)	(15,293)
Loans receivable		
Loan participations sold	1,615	—
Principal payments on loans receivable	136,090	106,840
Purchase of loans	(20,406)	—
Originated for investment	(125,813)	(106,884)
Proceeds of redemption of Federal Home Loan Bank of Chicago stock	3,514	—
Purchase of Federal Home Loan Bank and Federal Reserve Bank stock	(11)	—
Proceeds from sale of other real estate owned	494	1,290
Purchase of premises and equipment, net	(179)	(96)
Net cash from (used in) investing activities	(7,738)	4,482

Continued

5

Table of Contents

BANKFINANCIAL CORPORATION
 CONSOLIDATED STATEMENTS OF CASH FLOWS
 (In thousands) - Unaudited

	Three Months Ended March 31,	
	2017	2016
Cash flows from financing activities		
Net change in deposits	\$(10,108)	\$51,770
Net change in borrowings	977	(46,697)
Net change in advance payments by borrowers for taxes and insurance	(1,973)	(2,614)
Repurchase and retirement of common stock	(3,379)	(4,393)
Cash dividends paid on common stock	(1,155)	(1,010)
Shares retired for tax liability	(1,200)	—
Net cash used in financing activities	(16,838)	(2,944)
Net change in cash and cash equivalents	(21,218)	6,566
Beginning cash and cash equivalents	96,684	59,377
Ending cash and cash equivalents	\$75,466	\$65,943
Supplemental disclosures of cash flow information:		
Interest paid	\$1,243	\$766
Income taxes paid	1	60
Loans transferred to other real estate owned	1,936	65

See accompanying notes to the consolidated financial statements.

Table of Contents

BANKFINANCIAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation: BankFinancial Corporation, a Maryland corporation headquartered in Burr Ridge, Illinois (the “Company”), is the owner of all of the issued and outstanding capital stock of BankFinancial, NA (the “Bank”). The interim unaudited consolidated financial statements include the accounts of and transactions of BankFinancial Corporation, the Bank, and the Bank’s wholly-owned subsidiaries, Financial Assurance Services, Inc. and BF Asset Recovery Corporation (collectively, “the Company”), and reflect all normal and recurring adjustments that are, in the opinion of management, considered necessary for a fair presentation of the financial condition and results of operations for the periods presented. All significant intercompany accounts and transactions have been eliminated. The results of operations for the three month period ended March 31, 2017 are not necessarily indicative of the results of operations that may be expected for the year ending December 31, 2017.

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

Use of Estimates: To prepare financial statements in conformity with GAAP, management makes estimates and assumptions based on available information. These estimates and assumptions affect the amounts reported in the financial statements and the disclosures provided, and future results could differ.

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

These unaudited consolidated financial statements should be read in conjunction with the Company’s Annual Report on Form 10-K for the year ended December 31, 2016, as filed with the Securities and Exchange Commission.

Recent Accounting Pronouncements

In May 2014, the FASB issued an update (ASU No. 2014-09, Revenue from Contracts with Customers) creating FASB Topic 606, Revenue from Contracts with Customers. The guidance in this update affects any entity that either enters into contracts with customers to transfer goods or services or enters into contracts for the transfer of nonfinancial assets unless those contracts are within the scope of other standards (for example, insurance contracts or lease contracts). The core principle of the guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The guidance provides steps to follow to achieve the core principle. An entity should disclose sufficient information to enable users of financial statements to understand the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers. Qualitative and quantitative information is required about contracts with customers, significant judgments and changes in judgments, and assets recognized from the costs to obtain or fulfill a contract. The amendments in this update become effective for annual periods and interim periods within those annual periods beginning after December 15, 2017. We are currently evaluating the impact of adopting the new guidance on the consolidated financial statements. Our preliminary finding is that the new pronouncement will not have a significant impact on the consolidated financial statements as the majority of our business transactions will not be subject to this pronouncement.

On January 5, 2016, the FASB issued an update (ASU No. 2016-01, Financial Instruments - Recognition and Measurement of Financial Assets and Liabilities). The new guidance is intended to improve the recognition and measurement of financial instruments by requiring: equity investments (other than equity method or consolidation) to be measured at fair value with changes in fair value recognized in net income; public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes; separate presentation of financial assets and financial liabilities by measurement category and form of financial assets (i.e. securities or loans and receivables) on the balance sheet or the accompanying notes to the financial statements; eliminating the requirement to disclose the fair value of financial instruments measured at amortized cost for organizations that are not public business entities; eliminating the requirement for non-public business entities to disclose the method(s) and

significant assumptions used to estimate the fair value that is to be required to be disclosed for financial instruments measured at amortized cost on the balance sheet; and requiring a reporting organization to present separately in other comprehensive income the portion of the total change in fair value of a liability resulting from the change in the instrument-specific credit risk (also referred to as “own credit”) when the organization has elected to measure the liability at fair value in accordance with the fair value option for financial instruments. The new guidance is effective for public business entities for fiscal years beginning after December 15, 2017. We are currently evaluating the impact of adopting the new guidance on the consolidated financial statements. Our preliminary finding is that the new pronouncement will not have a significant impact on our Statement of Operations.

Table of Contents

BANKFINANCIAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

The pronouncement will require some revision to our disclosures within the consolidated financial statements and we are currently evaluating the impact.

In February 2016, the FASB issued ASU No. 2016-02, "Leases (Topic 842)" ("ASU 2016-02"). The standard requires a lessee to recognize assets and liabilities on the balance sheet for leases with lease terms greater than 12 months. ASU 2016-02 is effective for fiscal years, and interim periods within those years, beginning after December 15, 2018, and early adoption is permitted. We are currently evaluating the impact that the standard will have on our consolidated financial statements. Our preliminary finding is that the new pronouncement will not have a significant impact on our consolidated financial statements as the projected minimum lease payments under existing leases subject to the new pronouncement are less than one percent of our current total assets.

In March 2016, the FASB issued ASU No. 2016-09, "Compensation - Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting" ("ASU 2016-09"). The standard is intended to simplify several areas of accounting for share-based compensation arrangements, including the income tax impact, classification on the statement of cash flows and forfeitures. ASU 2016-09 was effective January 1, 2017. This new pronouncement reduces the effective tax rate reported as existing vested stock options are exercised. The amount of the impact on the effective tax rate is determined by the number of stock options exercised and the stock price of the Company when the stock options are exercised. Excess tax benefits and deficiencies are recorded in the tax expense.

In June 2016, the FASB issued ASU No. 2016-13, "Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments" ("ASU 2016-13"). These amendments require the measurement of 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 better inform 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. In addition, the ASU amends the accounting for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. ASU 2016-13 is effective for SEC filers for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019 (i.e., January 1, 2020, for calendar year entities). Early application will be permitted for all organizations for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. We are currently evaluating the impact that the standard will have on our consolidated financial statements. Our initial review indicates that we have maintained sufficient historical loan data to support the requirements of this pronouncement. We are currently evaluating various loss methodologies to determine their correlation to our various loan categories historical performance.

In March of 2017, the FASB issued ASU No. 2017-08, "Receivables-Nonrefundable Fees and Other Costs (Subtopic 310-20): Premium Amortization on Purchased Callable Debt Securities" ("ASU 2017-08"). This guidance shortens the amortization period for premiums on certain callable debt securities to the earliest call date (with an explicit, noncontingent call feature that is callable at a fixed price and on a preset dates), rather than contractual maturity date as currently required under GAAP. The ASU does not impact instruments without preset call dates such as mortgage-backed securities. For instruments with contingent call features, once the contingency is resolved and the security is callable at a fixed price and preset date, the security is within the scope of the ASU. ASU 2017-08 is effective for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years, and early adoption is permitted. Accordingly, effective January of 2017, we early adopted the pronouncement. Adoption of the new pronouncement was immaterial to the consolidated financial statements.

Table of Contents

BANKFINANCIAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

NOTE 2 - EARNINGS PER SHARE

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

	Three Months Ended March 31,	
	2017	2016
Net income available to common stockholders	\$1,881	\$ 1,904
Average common shares outstanding	19,243,940	20,155,541
Less:		
Unearned ESOP shares	(600,947)	(719,109)
Unvested restricted stock shares	(940)	(7,881)
Weighted average common shares outstanding	18,642,053	19,428,551
Add - Net effect of dilutive unvested restricted stock	5,462	2,939
Diluted weighted average common shares outstanding	18,647,515	19,431,490
Basic earnings per common share	\$0.10	\$ 0.10
Diluted earnings per common share	\$0.10	\$ 0.10
Number of antidilutive stock options excluded from the diluted earnings per share calculation	—	1,752,156
Weighted average exercise price of anti-dilutive option shares	\$—	\$ 12.30

NOTE 3 - SECURITIES

The fair value of securities and the related gross unrealized gains and losses recognized in accumulated other comprehensive income are shown below.

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
March 31, 2017				
Certificates of deposit	\$ 89,926	\$ —	\$ —	\$89,926
Equity mutual fund	500	—	(1)	499
Mortgage-backed securities - residential	13,907	622	(20)	14,509
Collateralized mortgage obligations - residential	5,293	15	(27)	5,281
SBA-guaranteed loan participation certificates	15	—	—	15
	\$ 109,641	\$ 637	\$ (48)	\$ 110,230
December 31, 2016				
Certificates of deposit	\$ 85,938	\$ —	\$ —	\$85,938
Equity mutual fund	500	—	(1)	499
Mortgage-backed securities - residential	14,561	644	(21)	15,184
Collateralized mortgage obligations - residential	5,587	15	(28)	5,574
SBA-guaranteed loan participation certificates	17	—	—	17
	\$ 106,603	\$ 659	\$ (50)	\$ 107,212

Table of Contents

BANKFINANCIAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

NOTE 3 - SECURITIES (continued)

The mortgage-backed securities and collateralized mortgage obligations reflected in the preceding table were issued by U.S. government-sponsored entities or agencies, Freddie Mac, Fannie Mae and Ginnie Mae, and are obligations which the government has affirmed its commitment to support. All securities reflected in the preceding table were classified as available-for-sale at March 31, 2017 and December 31, 2016.

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

	March 31, 2017	
	Amortized Cost	Fair Value
Due in one year or less	\$89,926	\$89,926
Equity mutual fund	500	499
Mortgage-backed securities - residential	13,907	14,509
Collateralized mortgage obligations - residential	5,293	5,281
SBA-guaranteed loan participation certificates	15	15
	\$109,641	\$110,230

Sales of securities were as follows:

Three
Months
Ended
March
31,
2016

Proceeds \$— \$46

Gross gains — 46

Securities with unrealized losses not recognized in income are as follows:

	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
March 31, 2017						
Equity Mutual Fund	\$499	\$ (1)	\$—	\$ —	\$499	\$ (1)
Mortgage-backed securities - residential	1,179	(20)	—	—	1,179	(20)
Collateralized mortgage obligations - residential	2,720	(17)	976	(10)	3,696	(27)
	\$4,398	\$ (38)	\$976	\$ (10)	\$5,374	\$ (48)
December 31, 2016						
Equity Mutual Fund	\$499	\$ (1)	\$—	\$ —	\$499	\$ (1)
Mortgage-backed securities - residential	1,187	(21)	—	—	1,187	(21)
Collateralized mortgage obligations - residential	3,691	(18)	1,028	(10)	4,719	(28)
	\$5,377	\$ (40)	\$1,028	\$ (10)	\$6,405	\$ (50)

The Company evaluates marketable investment securities with significant declines in fair value on a quarterly basis to determine whether they should be considered other-than-temporarily impaired under current accounting guidance, which generally provides

Table of Contents

BANKFINANCIAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

NOTE 3 - SECURITIES (continued)

that if a marketable security is in an unrealized loss position, whether due to general market conditions or industry or issuer-specific factors, the holder of the securities must assess whether the impairment is other-than-temporary. Certain mortgage-backed securities and collateralized mortgage obligations that the Company holds in its investment portfolio were in an unrealized loss position at March 31, 2017, but the unrealized losses were not considered significant under the Company's impairment testing methodology. In addition, the Company does not intend to sell these securities, and it is likely that the Company will not be required to sell these securities before their anticipated recovery occurs.

NOTE 4 - LOANS RECEIVABLE

Loans receivable are as follows:

	March 31, 2017	December 31, 2016
One-to-four family residential real estate	\$122,310	\$135,218
Multi-family mortgage	549,829	542,887
Nonresidential real estate	179,896	182,152
Construction and land	1,354	1,302
Commercial loans	105,671	103,063
Commercial leases	364,768	352,539
Consumer	1,896	2,255
	1,325,724	1,319,416
Net deferred loan origination costs	1,534	1,663
Allowance for loan losses	(7,971)	(8,127)
Loans, net	\$1,319,287	\$1,312,952

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

	Allowance for loan losses		Loan Balances		
	Individually evaluated for impairment	Collectively evaluated for impairment	Individually evaluated for impairment	Collectively evaluated for impairment	Total
March 31, 2017					
One-to-four family residential real estate	\$—	\$993	\$4,869	\$117,441	\$122,310
Multi-family mortgage	—	3,704	703	549,126	549,829
Nonresidential real estate	—	1,732	—	179,896	179,896
Construction and land	—	33	—	1,354	1,354
Commercial loans	—	807	—	105,671	105,671
Commercial leases	—	685	—	364,768	364,768
Consumer	—	17	—	1,896	1,896
	\$—	\$7,971	\$5,572	\$1,320,152	1,325,724
Net deferred loan origination costs					1,534
Allowance for loan losses					(7,971)
Loans, net					\$1,319,287

Table of Contents

BANKFINANCIAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

NOTE 4 - LOANS RECEIVABLE (continued)

	Allowance for loan losses			Loan Balances		
	Individually evaluated for impairment	Collectively evaluated for impairment	Total	Individually evaluated for impairment	Collectively evaluated for impairment	Total
December 31, 2016						
One-to-four family residential real estate	\$—	\$ 1,168	\$ 1,168	\$ 4,962	\$ 130,256	\$ 135,218
Multi-family mortgage	—	3,647	3,647	787	542,100	542,887
Nonresidential real estate	26	1,768	1,794	260	181,892	182,152
Construction and land	—	32	32	—	1,302	1,302
Commercial loans	—	733	733	—	103,063	103,063
Commercial leases	—	714	714	—	352,539	352,539
Consumer	—	39	39	—	2,255	2,255
	\$ 26	\$ 8,101	\$ 8,127	\$ 6,009	\$ 1,313,407	1,319,416
Net deferred loan origination costs						1,663
Allowance for loan losses						(8,127)
Loans, net						\$ 1,312,952
Activity in the allowance for loan losses is as follows:						
		Three Months Ended March 31,				
		2017	2016			
Beginning balance		\$ 8,127	\$ 9,691			
Loans charged off:						
One-to-four family residential real estate	(171)	(52)				
Multi-family mortgage	(3)	(45)				
Nonresidential real estate	(165)	(3)				
Consumer	—	(16)				
	(339)	(116)				
Recoveries:						
One-to-four family residential real estate	6	81				
Multi-family mortgage	11	137				
Construction and land	—	35				
Commercial loans	5	77				
Consumer	—	1				
	22	331				
Net recoveries (charge-offs)	(317)	215				
Provision for (recovery of) loan losses	161	(490)				
Ending balance	\$ 7,971	\$ 9,416				

Table of Contents

BANKFINANCIAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

NOTE 4 - LOANS RECEIVABLE (continued)

Impaired loans

Several of the following disclosures are presented by “recorded investment,” which the FASB defines as “the amount of the investment in a loan, which is not net of a valuation allowance, but which does reflect any direct write-down of the investment.” The following represents the components of recorded investment:

Loan principal balance
 Less unapplied payments
 Plus negative unapplied balance
 Less escrow balance
 Plus negative escrow balance
 Plus unamortized net deferred loan costs
 Less unamortized net deferred loan fees
 Plus unamortized premium
 Less unamortized discount
 Less previous charge-offs
 Plus recorded accrued interest
 Less reserve for uncollected interest
 = Recorded investment

The following tables present loans individually evaluated for impairment by class of loans:

				Three months ended March 31, 2017		
	Loan Balance	Recorded Investment	Partial Charge-off	Allowance for Loan Losses Allocated	Average Investment in Impaired Loans	Interest Income Recognized
March 31, 2017						
With no related allowance recorded:						
One-to-four family residential real estate	\$ 5,146	\$ 4,250	\$ 871	\$ —	\$ 4,453	\$ 19
One-to-four family residential real estate - non-owner occupied	624	588	60	—	634	—
Multi-family mortgage - Illinois	704	706	—	—	727	10
	\$ 6,474	\$ 5,544	\$ 931	\$ —	\$ 5,814	\$ 29
Year ended December 31, 2016						
	Loan Balance	Recorded Investment	Partial Charge-off	Allowance for Loan Losses Allocated	Average Investment in Impaired Loans	Interest Income Recognized
December 31, 2016						
With no related allowance recorded:						
One-to-four family residential real estate	\$ 5,379	\$ 4,548	\$ 886	\$ —	\$ 2,947	\$ 70
One-to-four family residential real estate - non-owner occupied	503	386	119	—	251	9

Edgar Filing: BankFinancial CORP - Form 10-Q

Multi-family mortgage - Illinois	787	787	—	—	980	41
	6,669	5,721	1,005	—	4,178	120
With an allowance recorded:						
Nonresidential real estate	262	260	21	26	164	—
	262	260	21	26	164	—
	\$6,931	\$ 5,981	\$ 1,026	\$ 26	\$4,342	\$ 120

13

Table of Contents

BANKFINANCIAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

NOTE 4 - LOANS RECEIVABLE (continued)

Nonaccrual Loans

The following tables present the recorded investment in nonaccrual loans and loans past due over 90 days still on accrual by class of loans:

	Loan	Recorded	Loans Past
	Balance	Investment	Due Over 90
			Days, Still
			Accruing
March 31, 2017			
One-to-four family residential real estate	\$ 2,049	\$ 1,724	\$ —
One-to-four family residential real estate – non-owner occupied	550	572	—
Multi-family mortgage - Illinois	158	106	—
	\$ 2,757	\$ 2,402	\$ —
December 31, 2016			
One-to-four family residential real estate	\$ 2,861	\$ 2,483	\$ —
One-to-four family residential real estate – non-owner occupied	428	368	—
Multi-family mortgage - Illinois	187	185	—
Nonresidential real estate	262	260	—
	\$ 3,738	\$ 3,296	\$ —

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

The Company's reserve for uncollected loan interest was \$208,000 and \$199,000 at March 31, 2017 and December 31, 2016, respectively. When a loan is on nonaccrual status and the ultimate collectability of the total principal of an impaired loan is in doubt, all payments are applied to principal under the cost recovery method. Alternatively, when a loan is on non-accrual status but there is doubt concerning only the ultimate collectability of interest, contractual interest is credited to interest income only when received, under the cash basis method pursuant to the provisions of FASB ASC 310-10, as applicable. In all cases, the average balances are calculated based on the month-end balances of the financing receivables within the period reported pursuant to the provisions of FASB ASC 310-10, as applicable.

Table of Contents

BANKFINANCIAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

NOTE 4 - LOANS RECEIVABLE (continued)

Past Due Loans

The following tables present the aging of the recorded investment of loans at March 31, 2017 by class of loans:

	30-59 Days Past Due	60-89 Days Past Due	90 Days or Greater Past Due	Total Past Due	Loans Not Past Due	Total
One-to-four family residential real estate loans	\$ 881	\$ 51	\$ 1,597	\$ 2,529	\$ 88,704	\$ 91,233
One-to-four family residential real estate loans – non-owner occupied	471	3	573	1,047	29,452	30,499
Multi-family mortgage - Illinois	1,415	—	106	1,521	293,113	294,634
Multi-family mortgage - Other	—	—	—	—	252,197	252,197
Nonresidential real estate	—	—	—	—	177,998	177,998
Construction	—	—	—	—	1,025	1,025
Land	—	—	—	—	327	327
Commercial loans:						
Regional commercial banking	—	—	—	—	41,149	41,149
Health care	—	—	—	—	35,957	35,957
Direct commercial lessor	—	—	—	—	28,779	28,779
Commercial leases:						
Investment rated commercial leases	1,487	—	—	1,487	279,408	280,895
Other commercial leases	140	—	—	140	85,711	85,851
Consumer	5	—	—	5	1,899	1,904
	\$ 4,399	\$ 54	\$ 2,276	\$ 6,729	\$ 1,315,719	\$ 1,322,448

Table of Contents

BANKFINANCIAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

NOTE 4 - LOANS RECEIVABLE (continued)

The following tables present the aging of the recorded investment of loans at December 31, 2016 by class of loans:

	30-59 Days Past Due	60-89 Days Past Due	90 Days or Greater Past Due	Total Past Due	Loans Not Past Due	Total
One-to-four family residential real estate loans	\$ 984	\$ 335	\$ 2,235	\$ 3,554	\$ 92,665	\$ 96,219
One-to-four family residential real estate loans – non-owner occupied	664	114	368	1,146	37,179	38,325
Multi-family mortgage - Illinois	605	439	184	1,228	294,223	295,451
Multi-family mortgage - Other	—	—	—	—	243,944	243,944
Nonresidential real estate	—	—	260	260	178,644	178,904
Construction	—	—	—	—	950	950
Land	—	—	—	—	349	349
Commercial loans:						
Regional commercial banking	—	—	—	—	36,086	36,086
Health care	—	—	—	—	35,455	35,455
Direct commercial lessor	—	—	—	—	31,847	31,847
Commercial leases:						
Investment rated commercial leases	51	—	—	51	269,430	269,481
Other commercial leases	—	—	—	—	84,988	84,988
Consumer	—	—	—	—	2,263	2,263
	\$ 2,304	\$ 888	\$ 3,047	\$ 6,239	\$ 1,308,023	\$ 1,314,262

Troubled Debt Restructurings

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

The Company had \$17,000 of TDRs at March 31, 2017, compared to \$341,000 at December 31, 2016. No specific valuation reserves were allocated to those loans at March 31, 2017 and December 31, 2016. The Company had no outstanding commitments to borrowers whose loans were classified as TDRs at either date. During the first quarter of 2017, six loans totaling \$324,000 were declassified as TDRs as they successfully met the criteria for removal from TDR status.

The following table presents loans classified as TDRs:

	March 31, 2017	December 31, 2016
One-to-four family residential real estate	\$ —	\$ 205
Troubled debt restructured loans – accrual loans	—	205
One-to-four family residential real estate	17	136
Troubled debt restructured loans – nonaccrual loans	17	136

Edgar Filing: BankFinancial CORP - Form 10-Q

Total troubled debt restructured loans \$ 17 \$ 341

During the three months ended March 31, 2017, there were no loans modified and classified as TDRs. During the three months ended March 31, 2016, the terms of certain loans were modified and classified as TDRs. The modification of the terms of such

16

Table of Contents

BANKFINANCIAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

NOTE 4 - LOANS RECEIVABLE (continued)

loans included one or a combination of the following: a reduction of the stated interest rate of the loan; an extension of the maturity date at a stated rate of interest lower than the current market rate for new debt with similar risk; or a permanent reduction of the recorded investment in the loan.

The following tables present TDR activity:

	Three Months Ended March 31, 2017		2016	
	Pre-Modification Number of outstanding loans	Post-Modification outstanding recorded investment	Pre-Modification Number of outstanding loans	Post-Modification outstanding recorded investment
One-to-four family residential real estate	—	—	1	\$ 63
			Due to permanent reduction in investment	Total
			Due to extension of maturity date interest rate	

For the Three Months Ended March 31, 2016

One-to-four family residential real estate	\$	—	\$ 63	\$	—	\$ 63
--	----	---	-------	----	---	-------

The TDRs described above had no impact on interest income, resulted in no change to the allowance for loan losses allocated and resulted in no charge-offs for the three months ended March 31, 2016.

The following table presents TDRs for which there was a payment default during the three months ended March 31, 2017 and 2016 within twelve months following the modification.

	2017		2016	
	Number of Recorded of investment loans	Number of Recorded of investment loans	Number of Recorded of investment loans	Number of Recorded of investment loans
One-to-four family residential real estate	1	\$ 17	2	\$ 42

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

The TDRs for which there was a payment default resulted in no change to the allowance for loan losses allocated and resulted in no charge-offs during the three months ended March 31, 2017 and 2016.

There were certain other loan modifications during the three months ended March 31, 2017 that did not meet the definition of a TDR. These loans had a total recorded investment of \$133,000 at March 31, 2017. The modification of these loans involved either a modification of the terms of a loan to borrowers who were not experiencing financial difficulties or a delay in a payment that was considered to be insignificant. There were no other loan modifications for the three months ended March 31, 2016.

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

Credit Quality Indicators

The Company categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt, including current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. The Company analyzes loans individually by classifying the loans based on credit risk. This analysis includes non-homogeneous loans, such as commercial and

commercial real estate loans. This analysis is performed on a monthly basis. The Company uses the following definitions for risk ratings:

Special Mention. A Special Mention asset has potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the asset or in the

Table of Contents

BANKFINANCIAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

NOTE 4 - LOANS RECEIVABLE (continued)

institution's credit position at some future date. Special Mention assets are not adversely classified and do not expose an institution to sufficient risk to warrant adverse classification.

Substandard. Loans categorized as Substandard continue to accrue interest, but exhibit a well-defined weakness or weaknesses that may jeopardize the liquidation of the debt. The loans continue to accrue interest because they are well secured and collection of principal and interest is expected within a reasonable time. The risk rating guidance published by the Office of the Comptroller of the Currency clarifies that a loan with a well-defined weakness does not have to present a probability of default for the loan to be rated Substandard, and that an individual loan's loss potential does not have to be distinct for the loan to be rated Substandard.

Nonaccrual. An asset classified Nonaccrual has all the weaknesses inherent in one classified Substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable. The loans were placed on nonaccrual status.

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

As of March 31, 2017, based on the most recent analysis performed, the risk categories of loans by class of loans are as follows:

	Pass	Special Mention	Substandard	Nonaccrual	Total
One-to-four family residential real estate loans	\$89,198	\$ —	\$ 685	\$ 1,724	\$91,607
One-to-four family residential real estate loans – non-owner occupied	30,089	—	41	573	30,703
Multi-family mortgage loans - Illinois	295,523	—	769	107	296,399
Multi-family mortgage loans - Other	253,430	—	—	—	253,430
Nonresidential real estate loans	179,788	—	108	—	179,896
Construction loans	1,022	—	—	—	1,022
Land loans	332	—	—	—	332
Commercial loans:					
Regional commercial banking	41,066	—	14	—	41,080
Health care	35,948	—	—	—	35,948
Direct commercial lessor	28,643	—	—	—	28,643
Commercial leases:					
Investment rated commercial leases	279,345	—	—	—	279,345
Other commercial leases	85,423	—	—	—	85,423
Consumer	1,896	—	—	—	1,896
	\$1,321,703	\$ —	\$ 1,617	\$ 2,404	\$1,325,724

Table of Contents

BANKFINANCIAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

NOTE 4 - LOANS RECEIVABLE (continued)

As of December 31, 2016, the risk categories of loans by class of loans are as follows:

	Pass	Special Mention	Substandard	Nonaccrual	Total
One-to-four family residential real estate loans	\$93,514	\$—	\$ 629	\$ 2,486	\$96,629
One-to-four family residential real estate loans – non-owner occupied	38,179	—	41	369	38,589
Multi-family mortgage loans - Illinois	297,826	122	1,048	187	299,183
Multi-family mortgage loans - Other	243,704	—	—	—	243,704
Nonresidential real estate loans	180,047	—	1,845	260	182,152
Construction loans	946	—	—	—	946
Land loans	356	—	—	—	356
Commercial loans:					
Regional commercial banking	35,944	—	66	—	36,010
Health care	35,372	—	—	—	35,372
Direct commercial lessor	30,881	800	—	—	31,681
Commercial leases:					
Investment rated commercial leases	268,022	—	—	—	268,022
Other commercial leases	84,356	161	—	—	84,517
Consumer	2,255	—	—	—	2,255
	\$1,311,402	\$ 1,083	\$ 3,629	\$ 3,302	\$1,319,416

NOTE 5 - OTHER REAL ESTATE OWNED

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

	March 31, 2017			December 31, 2016		
	Balance	Valuation Allowance	Net OREO Balance	Balance	Valuation Allowance	Net OREO Balance
One-to-four family residential	\$2,086	\$ (100)	\$ 1,986	\$1,702	\$ (137)	\$ 1,565
Multi-family mortgage	615	—	615	370	—	370
Nonresidential real estate	1,933	(125)	1,808	1,171	(105)	1,066
Land	1,077	(185)	892	1,101	(207)	894
	\$5,711	\$ (410)	\$ 5,301	\$4,344	\$ (449)	\$ 3,895

Table of Contents

BANKFINANCIAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

NOTE 5 - OTHER REAL ESTATE OWNED (continued)

The following represents the roll forward of OREO and the composition of OREO properties:

	For the Three Months Ended March 31,	
	2017	2016
Beginning balance	\$3,895	\$7,011
New foreclosed properties	1,936	65
Valuation adjustments	(20)	(119)
Sales and Payments	(510)	(1,328)
Ending balance	\$5,301	\$5,629

Activity in the valuation allowance is as follows:

	For the Three Months Ended March 31,	
	2017	2016
Beginning balance	\$449	\$1,042
Additions charged to expense	20	119
Reductions from sales of other real estate owned	(59)	(507)
Ending balance	\$410	\$654

At March 31, 2017 and December 31, 2016, the balance of OREO includes no foreclosed residential real estate properties recorded as a result of obtaining physical possession of the property without title. At March 31, 2017 and December 31, 2016, the recorded investment of consumer mortgage loans secured by residential real estate properties for which formal foreclosure proceeds are in process was \$1.5 million and \$1.6 million, respectively.

NOTE 6 - SECURITIES SOLD UNDER AGREEMENTS TO REPURCHASE

Securities sold under agreements to repurchase, included with borrowings on the consolidated balance sheet, are shown below.

	March 31, 2017			
	Overnight and Continued	30 - to 30 days	90 - 90 days	Greater Than 90 days
	Total	Total	Total	Total
Repurchase agreements and repurchase-to-maturity transactions	\$2,046	\$ —	\$ —	\$ —
Gross amount of recognized liabilities for repurchase agreements	\$2,046			
	in Statement of Condition December 31, 2016			
	Overnight and Continued	30 - to 30 days	90 - 90 days	Greater Than 90 days
	Total	Total	Total	Total
Repurchase agreements and repurchase-to-maturity transactions	\$1,069	\$ —	\$ —	\$ —
Gross amount of recognized liabilities for repurchase agreements	\$1,069			

Securities sold under agreements to repurchase were secured by mortgage-backed securities with a carrying amount of \$4.6 million and \$4.7 million at March 31, 2017 and December 31, 2016, respectively. Also included in total borrowings were advances from the FHLBC of \$50.0 million at March 31, 2017 and December 31, 2016.

Table of Contents

BANKFINANCIAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

NOTE 6 - SECURITIES SOLD UNDER AGREEMENTS TO REPURCHASE (continued)

Because security values fluctuate due to market conditions, the Company has no control over the market value of securities sold under agreements to repurchase. The Company is obligated to promptly transfer additional securities to the counterparty if the market value of the securities falls below the repurchase price, per the agreement.

NOTE 7 – EMPLOYEE BENEFIT PLAN

Employee Stock Ownership Plan. On March 29, 2017, the BankFinancial NA Employee Stock Ownership Plan (the "ESOP") was terminated and the ESOP repaid all amounts owing under the ESOP's Term Loan Agreement with the Company (the "Share Acquisition Loan"). The ESOP repaid the Share Acquisition Loan by transferring 753,490 unallocated shares of the Company's common stock to the Company in exchange for the full satisfaction of the Share Acquisition Loan, using the valuation method provided for in the ESOP. A total of 78,362 unallocated shares remained in the ESOP after the Share Acquisition Loan was repaid, and these shares were released and will be allocated to the accounts of eligible ESOP participants who were actively employed by the Bank as of March 29, 2017, based on their account balances, subject to the receipt of a favorable IRS determination letter. These transactions resulted in the recording of one-time, non-cash, non-tax deductible equity compensation expense of \$1.1 million in the first quarter of 2017. The Share Acquisition Loan had no outstanding principal balance at March 31, 2017 and \$10.8 million at December 31, 2016.

The Company made the Share Acquisition Loan to the ESOP in the original principal amount of \$19.6 million in connection with the Company's mutual to stock conversion in June of 2005. The proceeds of the Share Acquisition Loan were used by the ESOP to purchase 1,957,300 shares of the Company's common stock issued in the subscription offering price of \$10.00 per share. The Share Acquisition Loan was secured by a pledge of the acquired shares and the ESOP made annual loan payments with funds it received from the Bank's discretionary contributions to the ESOP in subsequent years and dividends it received on unallocated shares. As loan payments were made, the Company recorded compensation expense based on the allocation of shares released.

ESOP benefit expense is recorded based upon the fair value of the awarded shares, net of dividends and interest received on unallocated ESOP shares. ESOP benefit expense totaled \$1.3 million for the year ended December 31, 2016.

Shares held by the ESOP were as follows:

	March 31, December 31,	
	2017	2016
Allocated to participants	1,203,810	1,125,448
Distributed to participants	(314,062)	(313,223)
Unearned	—	831,852
Total ESOP shares	889,748	1,644,077
Fair value of unearned shares \$	—	\$ 12,328

NOTE 8 – EQUITY INCENTIVE PLAN

On June 27, 2006, the Company's stockholders approved the BankFinancial Corporation 2006 Equity Incentive Plan, which authorized the Human Resources Committee of the Board of Directors of the Company to grant a variety of cash- and equity-based incentive awards, including stock options, stock appreciation rights, restricted stock, performance shares and other incentive awards, to employees and directors aggregating up to 3,425,275 shares of the Company's common stock. The Plan provides that no awards may be granted under the Plan after the ten-year anniversary of the Effective Date. Consequently, no further awards will be granted under this Plan.

Table of Contents

BANKFINANCIAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

NOTE 8 – EQUITY INCENTIVE PLAN (continued)

As of December 31, 2016, there were 1,752,156 stock options outstanding. The Company recognized \$979,000 of equity-based compensation expense relating to the granting of stock options for the year ended December 31, 2016. There was no equity-based compensation expense for the three months ended March 31, 2017. A summary of the activity in the stock option plan for 2017 and 2016 follows:

Stock Options	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value ⁽¹⁾
Stock options outstanding at December 31, 2015	1,752,156	\$ 12.30	1.48	\$ 778
Stock options granted	—	—		
Stock options exercised	—	—		
Stock options outstanding at December 31, 2016	1,752,156	\$ 12.30	0.48	\$ 4,422
Stock options granted	—	—		
Stock options exercised	(1,717,817)	12.30		
Stock options outstanding at March 31, 2017	34,339	\$ 12.05	0.15	\$ 85
Stock options exercisable at March 31, 2017	34,339	12.05	0.15	85
Fully vested and expected to vest	34,339	12.05	0.15	85

Stock option aggregate intrinsic value represents the number of shares subject to options multiplied by the (1) difference (if positive) in the closing market price of the common stock underlying the options on the date shown and the weighted average exercise price.

During the three months ended March 31, 2017, 1,717,817 stock options were exercised. All stock options were exercised on a net settlement basis, using a portion of the shares obtained upon exercise in payment of the exercise price of the stock option. The net settlement resulted in the issuance of 273,514 of the Company's common stock. Certain employees chose to use a portion of the net shares received upon the exercise to pay required tax withholdings. This reduced the net shares issued by 81,299 shares to 192,215 shares.

NOTE 9 – FAIR VALUE

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

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

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

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

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

Securities: The fair values of marketable equity securities are generally determined by quoted prices, in active markets, for each specific security (Level 1). If Level 1 measurement inputs are not available for a marketable equity security, we determine its fair value based on the quoted price of a similar security traded in an active market (Level 2). The fair values of debt securities are generally determined by matrix pricing, which is a mathematical technique

widely used in the industry to value debt securities without relying exclusively on quoted prices for the specific securities, but rather by relying on the securities' relationship to other benchmark quoted securities (Level 2).

Table of Contents

BANKFINANCIAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

NOTE 9 - FAIR VALUE (continued)

Impaired Loans: The fair value of impaired loans with specific allocations of the allowance for loan losses is generally based on recent real estate appraisals. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the independent appraisers to adjust for differences between the comparable sales and income data available for similar loans and collateral underlying such loans. Non-real estate collateral may be valued using an appraisal, net book value per the borrower's financial statements, or aging reports, adjusted or discounted based on management's historical knowledge, changes in market conditions from the time of the valuation, and management's expertise and knowledge of the client and client's business, resulting in a Level 3 fair value classification. Impaired loans are evaluated on a quarterly basis for additional impairment and adjusted in accordance with the allowance policy.

Other Real Estate Owned: Assets acquired through or instead 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 lower of cost or fair value less estimated costs to sell. Fair value is commonly based on recent real estate appraisals which are updated no less frequently than annually. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach with data from comparable properties. Adjustments are routinely made in the appraisal process by the independent appraisers to adjust for differences between the comparable sales and income data available. Real estate owned properties are evaluated on a quarterly basis for additional impairment and adjusted accordingly.

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

	Fair Value Measurements Using			
	Quoted Prices in Active Markets for Identical Assets (Level 1)			Fair Value
	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)		
March 31, 2017				
Securities:				
Certificates of deposit	\$—	\$ 89,926	\$	—\$ 89,926
Equity mutual fund	499	—	—	499
Mortgage-backed securities – residential	—	14,509	—	14,509
Collateralized mortgage obligations – residential	—	5,281	—	5,281
SBA-guaranteed loan participation certificates	—	15	—	15
	\$ 499	\$ 109,731	\$	—\$ 110,230
December 31, 2016				
Securities:				
Certificates of deposit	\$—	\$ 85,938	\$	—\$ 85,938
Equity mutual fund	499	—	—	499
Mortgage-backed securities - residential	—	15,184	—	15,184
Collateralized mortgage obligations – residential	—	5,574	—	5,574

Edgar Filing: BankFinancial CORP - Form 10-Q

SBA-guaranteed loan participation certificates	—	17	—	17
	\$499	\$ 106,713	\$	—\$107,212

23

Table of Contents

BANKFINANCIAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

NOTE 9 - FAIR VALUE (continued)

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

	Fair Value Measurement			
	Using			
	Quoted			
	Prices in			
	Active	Significant	Significant	Fair
	Markets	Observable	Unobservable	Value
	for	Inputs	Inputs	
	Identical	(Level 2)	(Level 3)	
	Assets			
	(Level			
	1)			
March 31, 2017				
Other real estate owned:				
Nonresidential real estate	\$—	—\$ 49		\$49
	\$—	—\$ 49		\$49
December 31, 2016				
Impaired loans:				
Nonresidential real estate	—	234		234
	\$—	—\$ 234		\$234
Other real estate owned:				
One-to-four family residential real estate	\$—	—\$ 1,282		\$1,282
Nonresidential real estate	—	553		553
Land	—	47		47
	\$—	—\$ 1,882		\$1,882

At March 31, 2017 there were no impaired loans that were measured for impairment using the fair value of the collateral for collateral-dependent loans and which have specific valuation allowances, compared to a carrying amount of \$260,000 and a valuation allowance of \$26,000 at December 31, 2016. The decrease in the valuation allowance resulted in a decrease in the provision for loan losses of \$26,000 for the three months ended March 31, 2017. There was an increase in the provision for loan losses of \$13,000 for the three months ended March 31, 2016.

OREO, which is carried at the lower of cost or fair value less costs to sell, had a carrying value of \$86,000 less a valuation allowance of \$37,000, or \$49,000 at March 31, 2017, compared to a carrying value of \$2.3 million less a valuation allowance of \$434,000, or \$1.9 million at December 31, 2016. There were \$20,000 of valuation adjustments of OREO recorded for the three months ended March 31, 2017. There were \$119,000 of valuation adjustments of OREO recorded for the three months ended March 31, 2016.

The following table presents quantitative information, based on certain empirical data with respect to Level 3 fair value measurements for financial instruments measured at fair value on a non-recurring basis at March 31, 2017:

	Fair Value	Valuation	Significant	Range
		Technique(s)	Unobservable	(Weighted
			Input(s)	Average)
Other real estate owned:				
Nonresidential real estate loans	\$ 49	Sales comparison	Comparison	3.6%
			between sales	

and income
approaches

Other real estate owned \$ 49

24

Table of Contents

BANKFINANCIAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

NOTE 9 - FAIR VALUE (continued)

The following table presents quantitative information, based on certain empirical data with respect to Level 3 fair value measurements for financial instruments measured at fair value on a non-recurring basis at December 31, 2016:

	Fair Value	Valuation Technique(s)	Significant Unobservable Input(s)	Range (Weighted Average)
Impaired loans				
Nonresidential real estate	\$ 234	Sales comparison	Comparison between sales and income approaches	-10.2%
	\$ 234			
Other real estate owned				
One-to-four family residential real estate	\$ 1,282	Sales comparison	Discount applied to valuation	8.62% to 20.04% (11.9%)
Nonresidential real estate	553	Sales comparison	Comparison between sales and income approaches	-3.22% to 4.58(3.7%)
Land	47	Sales comparison	Discount applied to valuation	5.74% to 31.60% (25.2%)
	\$ 1,882			

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

	Carrying Amount	Fair Value Measurements at March 31, 2017 Using:			Total
		Level 1	Level 2	Level 3	
Financial assets					
Cash and cash equivalents	\$75,466	\$10,247	\$65,219	\$	-\$75,466
Securities	110,230	499	109,731	—	110,230
Loans receivable, net of allowance for loan losses	1,319,287	—	1,321,180	—	1,321,180
FHLBC and FRB stock	8,147	—	—	—	N/A
Accrued interest receivable	4,478	—	4,478	—	4,478
Financial liabilities					
Noninterest-bearing demand deposits	\$234,415	\$—	\$234,415	\$	-\$234,415
Savings deposits	161,938	—	161,938	—	161,938
NOW and money market accounts	571,138	—	571,138	—	571,138
Certificates of deposit	361,791	—	360,644	—	360,644
Borrowings	52,046	—	52,073	—	52,073
Accrued interest payable	135	—	135	—	135

Table of Contents

BANKFINANCIAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

NOTE 9 - FAIR VALUE (continued)

	Fair Value Measurements at December 31, 2016 Using:				
	Carrying Amount	Level 1	Level 2	Level 3	Total
Financial assets					
Cash and cash equivalents	\$96,684	\$13,053	\$83,631	\$	-\$96,684
Securities	107,212	499	106,713	—	107,212
Loans receivable, net of allowance for loan losses	1,312,952	—	1,322,713	234	1,322,947
FHLBC and FRB stock	11,650	—	—	—	N/A
Accrued interest receivable	4,381	—	4,381	—	4,381
Financial liabilities					
Noninterest-bearing demand deposits	\$249,539	\$—	\$249,539	\$	-\$249,539
Savings deposits	160,002	—	160,002	—	160,002
NOW and money market accounts	578,237	—	578,237	—	578,237
Certificates of deposit	351,612	—	350,593	—	350,593
Borrowings	51,069	—	50,015	—	50,015
Accrued interest payable	102	—	102	—	102

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

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

Loans: The estimated fair value for loans has been determined by calculating the present value of future cash flows based on the current rate the Company would charge for similar loans with similar maturities, applied for an estimated time period until the loan is assumed to be repriced or repaid.

FHLBC and FRB Stock: It is not practicable to determine the fair value of FHLBC and FRB stock due to the restrictions placed on its transferability.

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

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

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

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

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

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

Table of Contents

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

Cautionary Statement Regarding Forward-Looking Information

Forward Looking Statements

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

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

These risks and uncertainties, as well as the Risk Factors set forth in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2016 and this Quarterly Report on Form 10-Q, as well as other filings we make with the SEC, should be considered in evaluating forward-looking statements and undue reliance should not be placed on such statements. We do not undertake any obligation to update any forward-looking statement in the future, or to reflect circumstances and events that occur after the date on which the forward-looking statement was made.

Critical Accounting Policies

Critical accounting policies are defined as those that are reflective of significant judgments and uncertainties, and could potentially result in materially different results under different assumptions and conditions. We believe that the

most critical accounting policies upon which our financial condition and results of operation depend, and which involve the most complex subjective decisions or assessments, are included in the discussion entitled “Critical Accounting Policies” in Item 7, “Management's Discussion and Analysis of Financial Condition and Results of Operations,” in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2016, and all amendments thereto, as filed with the Securities and Exchange Commission.

Overview

Total loans increased in the first quarter of 2017 due to net growth in multi-family and commercial loans, and net growth in commercial leases related to the final installment of a \$20.4 million commercial lease portfolio purchase. Total commercial-related

Table of Contents

loan balances reached a new record level of \$1.2 billion, and now comprise 91% of total loans. New loan and lease opportunities continue to arise but it remains difficult to predict the quantity of new loan originations and net loan balances in future quarters due to the various competitive factors we encounter.

Our average yield on loans increased modestly due to the relative composition of new loan originations, partially offset by an increase in higher-yield loan payoffs. Accordingly, our net interest margin expanded modestly due to the higher average loan yield. The expansion of our net interest margin was partially offset by an increase in our cost of funds due to asset-liability duration management activities. Non-interest income decreased modestly due primarily to slightly lower deposit-account related fee income and reduced loan fee income.

Non-interest expense increased primarily due to equity-linked compensation and benefit expense, including the termination of our ESOP and the repayment of the ESOP loan in the first quarter of 2017. These transactions resulted in the recording of a non-tax deductible equity compensation expense of \$1.1 million during the first quarter and the elimination of future ESOP benefit expense for greater efficiency and flexibility in managing retirement benefits. Compared to the actual expense recorded for the first quarter of 2017, we expect that our compensation and benefits expense for each of the remaining three quarters of 2017 will be approximately \$1.3 million less than it was in the first quarter of 2017. In addition, exercises of stock options outstanding resulted in additional payroll tax and retirement benefit expense of approximately \$150,000, which was more than offset by a related income tax benefit of approximately \$950,000. We also expect that our marketing and information technology expenses will decline by an average of \$200,000 per quarter for the remainder of 2017. Other non-interest expenses remained well-contained. Past due and classified loan trends remain favorable. Our ratio of nonperforming loans to total loans was 0.18% and our ratio of non-performing assets to total assets was 0.48% at March 31, 2017. Non-performing commercial-related loans represented only 0.01% of total commercial-related loans. Non-performing asset and OREO expenses increased slightly in the first quarter due in part to real estate taxes and litigation expenses against a borrower and guarantor on a previously charged-off loan. We continue to focus on pro-active portfolio management and resolutions of non-performing loans and assets to maintain our strong asset quality ratios and reduce non-performing asset expense to the lowest practicable levels.

Table of Contents

SELECTED FINANCIAL DATA

The following summary information is derived from the consolidated financial statements of the Company. For additional information, reference is made to the Consolidated Financial Statements of the Company and related notes included elsewhere in this Quarterly Report.

	March 31, 2017	December 31, 2016	Change
(Dollars in thousands)			
Selected Financial Condition Data:			
Total assets	\$1,603,473	\$1,620,037	\$(16,564)
Loans, net	1,319,287	1,312,952	6,335
Securities, at fair value	110,230	107,212	3,018
Other real estate owned, net	5,301	3,895	1,406
Deposits	1,329,282	1,339,390	(10,108)
Borrowings	52,046	51,069	977
Equity	202,021	204,780	(2,759)
	Three Months Ended March 31, 2017 2016 Change (Dollars in thousands)		
Selected Operating Data:			
Interest income	\$13,362	\$12,759	\$603
Interest expense	1,276	856	420
Net interest income	12,086	11,903	183
Provision for (recovery of) loan losses	161	(490)	651
Net interest income after provision for (recovery of) loan losses	11,925	12,393	(468)
Noninterest income	1,544	1,594	(50)
Noninterest expense	11,266	10,930	336
Income before income tax expense	2,203	3,057	(854)
Income tax expense	322	1,153	(831)
Net income	\$1,881	\$1,904	\$(23)

Table of Contents

	Three Months Ended March 31, 2017		2016	
Selected Financial Ratios and Other Data:				
Performance Ratios:				
Return on assets (ratio of net income to average total assets) ⁽¹⁾	0.47	%	0.50	%
Return on equity (ratio of net income to average equity) ⁽¹⁾	3.66		3.59	
Average equity to average assets	12.87		14.03	
Net interest rate spread ^{(1) (2)}	3.15		3.30	
Net interest margin ^{(1) (3)}	3.26		3.39	
Efficiency ratio ⁽⁴⁾	82.66		80.98	
Noninterest expense to average total assets ⁽¹⁾	2.82		2.89	
Average interest-earning assets to average interest-bearing liabilities	132.57		136.26	
Dividends declared per share	\$0.06		\$0.05	
Dividend payout ratio	61.42	%	53.05	%
	At		At	
	March		December	
	31, 2017		31, 2016	
Asset Quality Ratios:				
Nonperforming assets to total assets ⁽⁵⁾	0.48	%	0.44	%
Nonperforming loans to total loans	0.18		0.25	
Allowance for loan losses to nonperforming loans	331.85		246.57	
Allowance for loan losses to total loans	0.60		0.62	
Capital Ratios:				
Equity to total assets at end of period	12.60	%	12.64	%
Tier 1 leverage ratio (Bank only)	10.94	%	10.27	%
Other Data:				
Number of full-service offices	19		19	
Employees (full-time equivalents)	242		246	

(1) Ratios annualized.

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

(3) The net interest margin represents net interest income divided by average total interest-earning assets for the period.

(4) The efficiency ratio represents noninterest expense, divided by the sum of net interest income and noninterest income.

(5) Nonperforming assets include nonperforming loans and other real estate owned.

Comparison of Financial Condition at March 31, 2017 and December 31, 2016

Total assets decreased \$16.6 million, or 1.0%, to \$1.603 billion at March 31, 2017, from \$1.620 billion at December 31, 2016. The decrease in total assets was primarily due to a decrease in cash and cash equivalents. Partially offsetting this decrease was a \$6.3 million, or 0.5%, increase in loans to \$1.319 billion at March 31, 2017, from \$1.313 billion at December 31, 2016 and a \$3.0 million, or 2.8%, increase in securities to \$110.2 million at March 31, 2017, from \$107.2 million at December 31, 2016.

Our loan portfolio consists primarily of investment and business loans (multi-family, nonresidential real estate, commercial, construction and land loans, and commercial leases), which together totaled 90.6% of gross loans at March 31, 2017. Commercial leases increased \$12.2 million, or 3.5%, due in part to the Company's acquisition of a portfolio of investment-grade commercial leases from a competitor exiting the sector. The Company closed \$20.4

million of the commercial lease portfolio acquisition late in the first quarter of 2017, consisting of commercial leases having an average rate of 2.13% and an average duration of approximately 26 months. Multi-family mortgage loans increased by \$6.9 million, or 1.3% and commercial loans increased by \$2.6 million, or 2.5%. The Bank's primary lending area consists of the counties in the State of Illinois where our branch offices are located, and contiguous counties. We derive the most significant portion of our revenues from these geographic areas. We also engage in multi-family lending activities in carefully selected metropolitan areas outside our primary lending area, and engage in certain types of

Table of Contents

commercial lending and leasing activities on a nationwide basis. At March 31, 2017, \$287.7 million, or 52.3%, of our multi-family loans were in the Metropolitan Statistical Area for Chicago, Illinois, while \$66.7 million, or 12.1%, were in the Metropolitan Statistical Area for Dallas, Texas; \$54.6 million, or 9.9%, were in the Metropolitan Statistical Area for Denver, Colorado; \$26.5 million, or 4.8%, were in the Metropolitan Statistical Area for Tampa, Florida and \$19.7 million, or 3.6%, were in the Metropolitan Statistical Area for Minneapolis, Minnesota. This information reflects the location of the collateral, but does not necessarily reflect the location of the borrower.

Total liabilities decreased \$13.8 million, or 1.0%, to \$1.401 billion at March 31, 2017, from \$1.415 billion at December 31, 2016, primarily due to decreases in noninterest-bearing and money market accounts. The decreases were partially offset by increases in savings deposits and certificates of deposit. Total deposits decreased \$10.1 million, or 0.8%, to \$1.329 billion at March 31, 2017, from \$1.339 billion at December 31, 2016. Certificates of deposit increased \$10.2 million, or 2.9%, to \$361.8 million at March 31, 2017, from \$351.6 million at December 31, 2016. This increase included a \$11.7 million increase in brokered certificates of deposit. Interest-bearing NOW accounts decreased \$897,000, or 0.34%, to \$266.2 million at March 31, 2017, from \$267.1 million at December 31, 2016. Savings accounts increased \$1.9 million, or 1.2%, to \$161.9 million at March 31, 2017, from \$160.0 million at December 31, 2016. Noninterest-bearing demand deposits decreased \$15.1 million, or 6.1%, to \$234.4 million at March 31, 2017, from \$249.5 million at December 31, 2016. Money market accounts decreased \$6.2 million, or 1.99%, to \$305.0 million at March 31, 2017, from \$311.2 million at December 31, 2016. Core deposits (which consists of savings, money market, noninterest-bearing demand and NOW accounts) were 72.8% and 73.7% of total deposits at March 31, 2017 and December 31, 2016, respectively.

Total stockholders' equity was \$202.0 million at March 31, 2017, compared to \$204.8 million at December 31, 2016. The decrease in total stockholders' equity was due to the combined impact of our repurchase of 232,045 shares of our common stock at a total cost of \$3.4 million, our declaration and payment of cash dividends totaling \$1.2 million, and the \$1.2 million net impact of exercise of stock options during the three months ended March 31, 2017. These items were partially offset by the net income of \$1.9 million that we recorded for the three months ended March 31, 2017 and the \$1.1 million impact of the ESOP loan repayment on March 29, 2017.

Operating Results for the Three Months Ended March 31, 2017 and 2016

Net Income. We had net income of \$1.9 million for each of the three months ended March 31, 2017 and March 31, 2016. Earnings per basic and fully diluted share of common stock were \$0.10 for both the three months ended March 31, 2017 and three months ended March 31, 2016.

Net Interest Income. Net interest income was \$12.1 million for the three months ended March 31, 2017, compared to \$11.9 million for the same period in 2016. The increase in net interest income reflected a \$603,000, or 4.7%, increase in interest income, which was partially offset by a \$420,000, or 49.1%, increase in interest expense.

The increase in interest income was primarily attributable to an increase in average interest-earning assets. Total average interest-earning assets increased \$88.1 million, or 6.23%, to \$1.502 billion for the three months ended March 31, 2017, from \$1.414 billion for the same period in 2016. Our net interest rate spread decreased by 15 basis points to 3.15% for the three months ended March 31, 2017, from 3.30% for the same period in 2016. Our net interest margin decreased by 13 basis points to 3.26% for the three months ended March 31, 2017, from 3.39% for the same period in 2016. The decreases in the net interest rate spread and net interest margin resulted from increased average balances and increased costs for interest-bearing liabilities. The yield on interest-earning assets decreased two basis points to 3.61% for the three months ended March 31, 2017 from 3.63% for the same period 2016, and the cost of interest-bearing liabilities increased 13 basis points to 0.46% for the three months ended March 31, 2017, from 0.33% for the same period in 2016.

Table of Contents

Average Balance Sheets

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

	For the Three Months Ended March 31,						
	2017				2016		
	Average	Interest	Yield/Rate	(1) Average	Interest	Yield/Rate	(1)
	Outstanding			Outstanding			
	Balance			Balance			
	(Dollars in thousands)						
Interest-earning assets:							
Loans	\$1,313,299	\$12,760	3.94 %	\$1,238,270	\$12,347	4.01 %	
Securities	113,756	349	1.24	118,557	314	1.07	
Stock in FHLBC and FRB	9,158	99	4.38	6,257	14	0.90	
Other	65,933	154	0.95	50,924	84	0.66	
Total interest-earning assets	1,502,146	13,362	3.61	1,414,008	12,759	3.63	
Noninterest-earning assets	93,045			99,675			
Total assets	\$1,595,191			\$1,513,683			
Interest-bearing liabilities:							
Savings deposits	\$160,456	43	0.11	\$158,320	42	0.11	
Money market accounts	307,121	273	0.36	324,516	249	0.31	
NOW accounts	263,286	121	0.19	245,115	90	0.15	
Certificates of deposit	352,929	743	0.85	234,872	406	0.70	
Total deposits	1,083,792	1,180	0.44	962,823	787	0.33	
Borrowings	49,306	96	0.79	74,907	69	0.37	
Total interest-bearing liabilities	1,133,098	1,276	0.46	1,037,730	856	0.33	
Noninterest-bearing deposits	235,167			242,290			
Noninterest-bearing liabilities	21,547			21,341			
Total liabilities	1,389,812			1,301,361			
Equity	205,379			212,322			
Total liabilities and equity	\$1,595,191			\$1,513,683			
Net interest income		\$12,086			\$11,903		
Net interest rate spread (2)			3.15 %			3.30 %	
Net interest-earning assets (3)	\$369,048			\$376,278			
Net interest margin (4)			3.26 %			3.39 %	
Ratio of interest-earning assets to interest-bearing liabilities	132.57 %			136.26 %			

(1) Annualized

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

(3) Net interest-earning assets represents total interest-earning assets less total interest-bearing liabilities.

(4) Net interest margin represents net interest income divided by average total interest-earning assets.

Table of Contents

Provision for Loan Losses

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

We recorded a provision for loan losses of \$161,000 for the three months ended March 31, 2017, compared to a recovery of loan losses of \$490,000 for the same period in 2016. The provision for or recovery of loan losses is a function of the allowance for loan loss methodology that we use to determine the appropriate level of the allowance for inherent loan losses after net charge-offs have been deducted. The portion of the allowance for loan losses attributable to loans collectively evaluated for impairment decreased \$130,000, or 1.6%, to \$8.0 million at March 31, 2017, from \$8.1 million at December 31, 2016. The reserve established for loans individually evaluated for impairment decreased \$26,000 to no reserve for the three months ended March 31, 2017. Net charge-offs were \$317,000 for the three months ended March 31, 2017.

The allowance for loan losses as a percentage of nonperforming loans was 331.85% at March 31, 2017, compared to 246.57% at December 31, 2016.

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

Noninterest Income

	Three Months Ended March 31, 2017 2016 Change		
	(Dollars in thousands)		
Deposit service charges and fees	\$529	\$567	\$ (38)
Other fee income	481	495	(14)
Insurance commissions and annuities income	77	55	22
Gain on sale of loans, net	7	18	(11)
Gain on sales of securities	—	46	(46)
Loan servicing fees	68	73	(5)
Amortization of servicing assets	(31)	(28)	(3)
Recovery of servicing assets	—	(3)	3
Earnings on bank owned life insurance	63	51	12
Trust income	172	160	12
Other	178	160	18
Total noninterest income	\$1,544	\$1,594	\$ (50)

Noninterest income decreased \$50,000, or 3.1%, to \$1.5 million for the three months ended March 31, 2017, compared to \$1.6 million for the three months ended March 31, 2016. Deposit service charges and fees decreased \$38,000, or 6.7%, to \$529,000 for the three months ended March 31, 2017, compared to \$567,000 for the three

Edgar Filing: BankFinancial CORP - Form 10-Q

months ended March 31, 2016. Other fee income decreased \$14,000, or 2.8%, to \$481,000 for the three months ended March 31, 2017, compared to \$495,000 for the three months ended March 31, 2016. Noninterest income for the three months ended March 31, 2017 included a \$7,000 gain on sale of loans. Earnings on bank owned life insurance and trust income each increased \$12,000 for the three months ended March 31, 2017. Other income increased \$18,000, or 11.3%, to \$178,000 for the three months ended March 31, 2017, compared to \$160,000 for the three

Table of Contents

months ended March 31, 2016. The results for the three months ended March 31, 2016 also included a \$46,000 gain on the sale of certain securities the Bank acquired in its acquisition of Downers Grove National Bank in 2011.

Noninterest Expense

	Three Months Ended March 31,		
	2017	2016	Change
	(Dollars in thousands)		
Compensation and benefits	\$6,352	\$5,993	\$ 359
Office occupancy and equipment	1,622	1,647	(25)
Advertising and public relations	381	222	159
Information technology	753	724	29
Supplies, telephone and postage	332	376	(44)
Amortization of intangibles	129	136	(7)
Nonperforming asset management	104	84	20
Loss on sale other real estate owned	16	38	(22)
Valuation adjustments of other real estate owned	20	119	(99)
Operations of other real estate owned	177	219	(42)
FDIC insurance premiums	187	217	(30)
Other	1,193	1,155	38
Total noninterest expense	\$11,266	\$10,930	\$ 336

Noninterest expense increased by \$336,000, or 3.1%, to \$11.3 million for the three months ended March 31, 2017, from \$10.9 million for the same period in 2016. Compensation and benefits increased \$359,000, primarily due to a one-time, non-cash, non-tax deductible equity compensation expense of \$1.1 million related to the termination of the ESOP and the repayment of the ESOP's Share Acquisition Loan on March 29, 2017 for greater efficiency and flexibility in managing retirement benefits. Compensation expense for the three months ended March 31, 2016 included \$245,000 in stock-based compensation and incentive compensation accruals. Advertising and public relations expense increased \$159,000, or 71.6%, to \$381,000 for the three months ended March 31, 2017, from \$222,000 for the same period in 2016. Nonperforming asset management expense increased \$20,000, or 23.8%, to \$104,000 for the three months ended March 31, 2017, from \$84,000 for the same period in 2016. Valuation adjustments of OREO decreased \$99,000, or 83.2%, to \$20,000 for the three months ended March 31, 2017, compared to \$119,000 for the same period in 2016.

Income Taxes

For the three months ended March 31, 2017, we recorded income tax expense of \$322,000, compared to \$1.2 million for the three months ended March 31, 2016. Our effective tax rate for the three months ended March 31, 2017 was 14.6%, which includes the impact of the stock option exercises and the ESOP termination charge, compared to 37.7% for the same period in 2016. Excluding the impact of the stock option exercises and the ESOP termination charge, the effective tax rate for the three months ended March 31, 2017 would have been comparable to the effective tax rate for the same period in 2016.

Nonperforming Loans and Assets

We review loans on a regular basis, and generally place loans on nonaccrual status when either principal or interest is 90 days or more past due. In addition, the Company places loans on nonaccrual status when we do not expect to receive full payment of interest or principal. Interest accrued and unpaid at the time a loan is placed on nonaccrual status is reversed from interest income. Interest payments received on nonaccrual loans are recognized in accordance with our significant accounting policies. Once a loan is placed on nonaccrual status, the borrower must generally demonstrate at least six months of payment performance before the loan is eligible to return to accrual status. We may have loans classified as 90 days or more delinquent and still accruing. Generally, we do not utilize this category of loan classification unless: (1) the loan is repaid in full shortly after the period end date; (2) the loan is well secured and

there are no asserted or pending legal barriers to its collection; or (3) the borrower has remitted all scheduled payments and is otherwise in substantial compliance with the terms of the loan, but the processing of loan payments actually received or the renewal of the loan has not occurred for administrative reasons. At March 31, 2017, we had no loans in this category.

Table of Contents

We typically obtain new third-party appraisals or collateral valuations when we place a loan on nonaccrual status, conduct impairment testing or conduct a TDR analysis unless the existing valuation information for the collateral is sufficiently current to comply with the requirements of our Appraisal and Collateral Valuation Policy (“ACV Policy”). We also obtain new third-party appraisals or collateral valuations when the judicial foreclosure process concludes with respect to real estate collateral, and when we otherwise acquire actual or constructive title to real estate collateral. In addition to third-party appraisals, we use updated valuation information based on Multiple Listing Service data, broker opinions of value, actual sales prices of similar assets sold by us and approved sales prices in response to offers to purchase similar assets owned by us to provide interim valuation information for consolidated financial statement and management purposes. Our ACV Policy establishes the maximum useful life of a real estate appraisal at 18 months. Because appraisals and updated valuations utilize historical or “ask-side” data in reaching valuation conclusions, the appraised or updated valuation may or may not reflect the actual sales price that we will receive at the time of sale. Real estate appraisals may include up to three approaches to value: the sales comparison approach, the income approach (for income-producing property) and the cost approach. Not all appraisals utilize all three approaches. Depending on the nature of the collateral and market conditions, we may emphasize one approach over another in determining the fair value of real estate collateral. Appraisals may also contain different estimates of value based on the level of occupancy or planned future improvements. “As-is” valuations represent an estimate of value based on current market conditions with no changes to the use or condition of the real estate collateral. “As-stabilized” or “as-completed” valuations assume the real estate collateral will be improved to a stated standard or achieve its highest and best use in terms of occupancy. “As-stabilized” or “as-completed” valuations may be subject to a present value adjustment for market conditions or the schedule of improvements.

As part of the asset classification process, we develop an exit strategy for real estate collateral or OREO by assessing overall market conditions, the current use and condition of the asset, and its highest and best use. For most income-producing real estate, we believe that investors value most highly a stable income stream from the asset; consequently, we perform a comparative evaluation to determine whether conducting a sale on an “as-is”, “as-stabilized” or “as-completed” basis is most likely to produce the highest net realizable value. If we determine that the “as-stabilized” or “as-completed” basis is appropriate, we then complete the necessary improvements or tenant stabilization tasks, with the applicable time value discount and improvement expenses incorporated into our estimates of the expected costs to sell. As of March 31, 2017, substantially all impaired real estate loan collateral and OREO were valued on an “as-is basis.” Estimates of the net realizable value of real estate collateral also include a deduction for the expected costs to sell the collateral or such other deductions from the cash flows resulting from the operation and liquidation of the asset as are appropriate. For most real estate collateral subject to the judicial foreclosure process, we generally apply a 10.0% deduction to the value of the asset to determine the expected costs to sell the asset. This estimate includes one year of real estate taxes, sales commissions and miscellaneous repair and closing costs. If we receive a purchase offer that requires unbudgeted repairs, or if the expected resolution period for the asset exceeds one year, we then include, on a case-by-case basis, the costs of the additional real estate taxes and repairs and any other material holding costs in the expected costs to sell the collateral. For OREO, we generally apply a 7.0% deduction to determine the expected costs to sell, as expenses for real estate taxes and repairs are expensed when incurred.

Table of Contents

Nonperforming Assets Summary

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

	March 31, December 31, Quarter		
	2017	2016	Change
	(Dollars in thousands)		
Nonaccrual loans:			
One-to-four family residential real estate	\$2,296	\$ 2,851	\$(555)
Multi-family mortgage	106	185	(79)
Nonresidential real estate	—	260	(260)
	2,402	3,296	(894)
Other real estate owned:			
One-to-four family residential	1,986	1,565	421
Multi-family mortgage	615	370	245
Nonresidential real estate	1,808	1,066	742
Land	892	894	(2)
	5,301	3,895	1,406
Total nonperforming assets	\$7,703	\$ 7,191	\$ 512
Ratios:			
Nonperforming loans to total loans	0.18	% 0.25	%
Nonperforming assets to total assets	0.48	0.44	

Nonperforming Assets

Nonperforming assets totaled \$7.7 million at March 31, 2017, and \$7.2 million at of December 31, 2016.

Nonperforming assets increased \$512,000 for the three months ended March 31, 2017. Although we experience occasional isolated instances of new nonaccrual loans, we believe that continuing our aggressive resolution posture will maintain the trends favoring very strong asset quality.

Four residential, one multi-family and two nonresidential real estate loans with a book balance of \$1.9 million were transferred from nonaccrual loans to OREO during the three months ended March 31, 2017. We continue to experience modest quantities of defaults on residential real estate loans principally due either to the borrower's personal financial condition or deteriorated collateral value.

Liquidity and Capital Resources

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

Our primary sources of funds are deposits, principal and interest payments on loans and securities, and, to a lesser extent, wholesale borrowings, the proceeds from maturing securities and short-term investments, and the proceeds from the sales of loans and securities and lease payments. The scheduled amortization of loans and securities, as well as proceeds from borrowings, are predictable sources of funds. Other funding sources, however, such as deposit inflows, mortgage prepayments and mortgage loan sales are greatly influenced by market interest rates, economic conditions and competition. We anticipate that we will have sufficient funds available to meet current loan commitments and lines of credit and maturing certificates of deposit that are not renewed or extended. We generally remain fully invested and utilize additional sources of funds through FHLBC advances. We had \$50.0 million of FHLBC advances at March 31, 2017 and December 31, 2016.

As of March 31, 2017, we were not aware of any known trends, events or uncertainties that had or were reasonably likely to have a material impact on our liquidity. As of March 31, 2017, we had no other material commitments for capital expenditures.

Table of Contents

Capital Management - Bank. The overall objectives of our capital management are to ensure the availability of sufficient capital to support loan, deposit and other asset and liability growth opportunities and to maintain capital to absorb unforeseen losses or write-downs that are inherent in the business risks associated with the banking industry. We seek to balance the need for higher capital levels to address such unforeseen risks and the goal to achieve an adequate return on the capital invested by our stockholders.

The Bank and the Company are subject to regulatory capital requirements administered by the federal banking agencies. The capital adequacy guidelines and, additionally for banks, prompt corrective action regulations, involve the quantitative measurement 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 regulators. The failure to meet minimum capital requirements can result in regulatory actions. The final rules implementing Basel Committee on Banking Supervision's capital guidelines for U.S. banks (Basel III rules) became effective for the Company on January 1, 2015, with full compliance with all of the requirements being phased in over a multi-year schedule, and fully phased in by January 1, 2019. The net unrealized gain or loss on available for sale securities is not included in computing regulatory capital.

Prompt corrective action regulations provide five classifications: well-capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized, although these terms are not used to represent overall financial condition. If only adequately capitalized, regulatory approval is required to accept brokered deposits. If undercapitalized, capital distributions are limited, as is asset growth and expansion, and capital restoration plans are required. As of March 31, 2017 and December 31, 2016, the OCC categorized the Bank as well-capitalized under the regulatory framework for prompt corrective action. There are no conditions or events since those notifications that management believes have changed the institution's well-capitalized status.

The Company and the Bank have each adopted Regulatory Capital Plans that require the Bank to maintain a Tier 1 leverage ratio of at least 7.5% and a total risk-based capital ratio of at least 10.5% (including the Capital Conservation Buffer ("CCB")). The minimum capital ratios set forth in the Regulatory Capital Plans will be increased and other minimum capital requirements will be established if and as necessary. In accordance with the Regulatory Capital Plans, neither the Company nor the Bank will pursue any acquisition or growth opportunity, declare any dividend or conduct any stock repurchase that would cause the Bank's total risk-based capital ratio and/or its Tier 1 leverage ratio to fall below the established minimum capital levels or the capital levels required for capital adequacy plus the CCB. The minimum CCB at March 31, 2017 is 1.25% and will increase 0.625% annually through 2019 to 2.5%. In addition, the Company will continue to maintain its ability to serve as a source of financial strength to the Bank by holding at least \$5.0 million of cash or liquid assets for that purpose. As of March 31, 2017, the Bank and the Company were well-capitalized, with all capital ratios exceeding the well-capitalized requirement. There are no conditions or events that management believes have changed the Bank's prompt corrective action capitalization category.

The Bank is subject to regulatory restrictions on the amount of dividends it may declare and pay to the Company without prior regulatory approval, and to regulatory notification requirements for dividends that do not require prior regulatory approval.

Table of Contents

Actual and required capital amounts and ratios were:

	Actual		Required for Capital Adequacy Purposes		To be Well-Capitalized under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
(Dollars in thousands)						
March 31, 2017						
Total capital (to risk-weighted assets):						
Consolidated	\$190,479	16.65 %	\$91,510	8.00 %	N/A	N/A
BankFinancial, NA	180,381	15.76	91,582	8.00	\$114,477	10.00 %
Tier 1 (core) capital (to risk-weighted assets):						
Consolidated	182,508	15.96	68,632	6.00	N/A	N/A
BankFinancial, NA	172,410	15.06	68,686	6.00	91,582	8.00
Common Tier 1 (CET1)						
Consolidated	182,508	15.96	51,474	4.50	N/A	N/A
BankFinancial, NA	172,410	15.06	51,515	4.50	74,410	6.50
Tier 1 (core) capital (to adjusted average total assets):						
Consolidated	182,508	11.58	63,808	4.00	N/A	N/A
BankFinancial, NA	172,410	10.94	63,029	4.00	78,786	5.00

	Actual		Required for Capital Adequacy Purposes		To be Well-Capitalized under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
(Dollars in thousands)						

December 31, 2016

Total capital (to risk-weighted assets):						
Consolidated	\$193,845	16.96 %	\$91,414	8.00 %	N/A	N/A
BankFinancial, NA	168,113	14.72	91,386	8.00	\$114,232	10.00 %
Tier 1 (core) capital (to risk-weighted assets):						
Consolidated	185,718	16.25	68,560	6.00	N/A	N/A
BankFinancial, NA	159,986	14.01	68,539	6.00	91,386	8.00
Common Tier 1 (CET1)						
Consolidated	185,718	16.25	51,420	4.50	N/A	N/A
BankFinancial, NA	159,986	14.01	51,404	4.50	74,251	6.50
Tier 1 (core) capital (to adjusted average total assets):						
Consolidated	185,718	11.92	62,306	4.00	N/A	N/A
BankFinancial, NA	159,986	10.27	62,303	4.00	77,879	5.00

Capital Management - Company. Total stockholders' equity was \$202.0 million at March 31, 2017, compared to \$204.8 million at December 31, 2016. The decrease in total stockholders' equity was due to the combined impact of our repurchase of 232,045 shares of our common stock at a total cost of \$3.4 million, our declaration and payment of cash dividends totaling \$1.2 million, and the net impact of exercise of stock options of \$1.2 million during the three months ended March 31, 2017. These items were partially offset by the net income of \$1.9 million that we recorded for the three months ended March 31, 2017 and the \$1.1 million impact of the ESOP loan repayment on March 29, 2017.

Quarterly Cash Dividends. The Company declared cash dividends of \$0.06 and \$0.05 per share for the three months ended March 31, 2017 and March 31, 2016, respectively.

Table of Contents

Stock Repurchase Program. On October 27, 2016, the Board extended the expiration date of the current repurchase authorization from December 31, 2016 to June 30, 2017, and increased the total number of shares authorized for repurchase by an additional 478,789 shares. During the quarter ending March 31, 2017, the Company repurchased 232,045 shares of its common stock. As of March 31, 2017, the Company had repurchased 2,100,251 shares of its common stock out of the 2,580,755 shares of common stock authorized under this repurchase authorization.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK

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

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

We actively evaluate interest rate risk in connection with our lending, investing and deposit activities. In an effort to better manage interest-rate risk, we have de-emphasized the origination of residential mortgage loans, and have increased our emphasis on the origination of nonresidential real estate loans, multi-family mortgage loans, commercial loans and commercial leases. In addition, depending on market interest rates and our capital and liquidity position, we generally sell all or a portion of our longer-term, fixed-rate residential loans, usually on a servicing-retained basis. Further, we primarily invest in shorter-duration securities, which generally have lower yields compared to longer-term investments. Shortening the average maturity of our interest-earning assets by increasing our investments in shorter-term loans and securities, as well as loans with variable rates of interest, helps to better match the maturities and interest rates of our assets and liabilities, thereby reducing the exposure of our net interest income to changes in market interest rates. Finally, we have classified all of our investment portfolio as available-for-sale so as to provide flexibility in liquidity management.

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

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

Our dynamic GAP analysis determines the relative balance between the repricing of assets and liabilities over multiple periods of time (ranging from overnight to five years). Dynamic GAP analysis includes expected cash flows from loans and mortgage-backed securities, applying prepayment rates based on the differential between the current interest

rate and the market interest rate for each loan and security type. This analysis identifies mismatches in the timing of asset and liability repricing but does not necessarily provide an accurate indicator of interest rate risk because it omits the factors incorporated into the net interest income analysis.

Table of Contents

Quantitative Analysis. The following table sets forth, as of March 31, 2017, the estimated changes in the Bank's NPV and net interest income that would result from the designated instantaneous parallel shift in the U.S. Treasury yield curve. Computations of prospective effects of hypothetical interest rate changes are based on numerous assumptions including relative levels of market interest rates, loan prepayments and deposit decay, and should not be relied upon as indicative of actual results.

Change in Interest Rates (basis points)	Estimated Decrease in NPV		Increase (Decrease) in Estimated Net Interest Income		
	Amount	Percent	Amount	Percent	
	(Dollars in thousands)				
+400	\$ (31,325)	(12.65)%	\$ 602	1.23	%
+300	(19,434)	(7.85)	556	1.13	
+200	(9,955)	(4.02)	527	1.07	
+100	(3,869)	(1.56)	337	0.69	
0					
-25	(314)	(0.13)	(310)	(0.63)	

The table set forth above indicates that at March 31, 2017, in the event of an immediate 25 basis point decrease in interest rates, the Bank would be expected to experience a 0.13% decrease in NPV and a \$310,000 decrease in net interest income. In the event of an immediate 200 basis point increase in interest rates, the Bank would be expected to experience a 4.02% decrease in NPV and a \$527,000 increase in net interest income. This data does not reflect any actions that we may undertake in response to changes in interest rates, such as changes in rates paid on certain deposit accounts based on local competitive factors, which could reduce the actual impact on NPV and net interest income, if any.

Certain shortcomings are inherent in the methodology used in the above interest rate risk measurements. Modeling changes in NPV and net interest income requires that we make certain assumptions that may or may not reflect the manner in which actual yields and costs respond to changes in market interest rates. The NPV and net interest income table presented above assumes that the composition of our interest-rate-sensitive assets and liabilities existing at the beginning of a period remains constant over the period being measured and, accordingly, the data does not reflect any actions that we may undertake in response to changes in interest rates, such as changes in rates paid on certain deposit accounts based on local competitive factors. The table also assumes that a particular change in interest rates is reflected uniformly across the yield curve regardless of the duration to maturity or the repricing characteristics of specific assets and liabilities. Because of the shortcomings mentioned above, management considers many additional factors such as projected changes in loan and deposit balances and various projected forward interest rate scenarios when evaluating strategies for managing interest rate risk. Accordingly, although the NPV and net interest income table provides an indication of our sensitivity to interest rate changes at a particular point in time, such measurements are not intended to and do not provide a precise forecast of the effect of changes in market interest rates on our net interest income and will differ from actual results.

ITEM 4. CONTROLS AND PROCEDURES

An evaluation was performed under the supervision and with the participation of the Company's management, including the Chairman, Chief Executive Officer and President and the Executive Vice President and Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in Rule 13a-15(e) promulgated under the Securities and Exchange Act of 1934, as amended) as of March 31, 2017. Based on that evaluation, the Company's management, including the Chairman, Chief Executive Officer, and President and the Executive Vice President and Chief Financial Officer, concluded that the Company's disclosure controls and procedures were effective.

During the quarter ended March 31, 2017, there have been no changes in the Company's internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II

ITEM 1. LEGAL PROCEEDINGS

The Company and its subsidiaries are subject to various legal actions arising in the normal course of business. In the opinion of management, based on currently available information, the resolution of these legal actions is not expected to have a material adverse effect on the Company's results of operations.

ITEM 1A. RISK FACTORS

There have been no material changes to the risk factors previously disclosed in the Company's filings with the Securities and Exchange Commission.

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

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

(b) Use of Proceeds. Not applicable.

(c) Repurchases of Equity Securities.

The following table sets forth information in connection with purchases of our common stock made by, or, on behalf of us, during the first quarter of 2017:

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet be Purchased under the Plans or Programs ⁽¹⁾
January 1, 2017 through January 31, 2017	—	\$ —	—	712,549
February 1, 2017 through February 28, 2017	79,228	14.29	79,228	633,321
March 1, 2017 through March 31, 2017	152,817	14.63	152,817	480,504
	232,045		232,045	

On October 27, 2016, the Board extended the expiration date of the current repurchase authorization from (1) December 31, 2016 to June 30, 2017, and increased the total number of shares authorized for repurchase by an additional 478,789 shares. As of March 31, 2017, the Company had repurchased 2,100,251 shares of its common stock out of the 2,580,755 shares of common stock authorized under this repurchase authorization.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

Edgar Filing: BankFinancial CORP - Form 10-Q

Exhibit Number	Description
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	Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002*
101	The following financial statements from the BankFinancial Corporation Quarterly Report on Form 10-Q for the quarter ended March 31, 2017, formatted in Extensive Business Reporting Language (XBRL): (i) consolidated statement of conditions, (ii) consolidated statements of operations, (iii) consolidated statements of cash flows and (iv) the notes to consolidated financial statements.

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

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

**BANKFINANCIAL
CORPORATION**

Dated: April 26, 2017 By: /s/ F. Morgan Gasior

F. Morgan Gasior
Chairman of the
Board, Chief
Executive Officer and
President

/s/ Paul A. Cloutier
Paul A. Cloutier
Executive Vice
President and Chief
Financial Officer