CHEVIOT FINANCIAL CORP
Form 10-Q
May 12, 2011

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D. C. 20549
FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2011

OR

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

For the transition period from ____________ to _______________

Commission File No. 0-50529

CHEVIOT FINANCIAL CORP.
(Exact name of registrant as specified in its charter)

Federal	56-2423720
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

3723 Glenmore Avenue, Cincinnati, Ohio 45211
(Address of principal executive office)

Registrant’s telephone number, including area code: (513) 661-0457

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Sections 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days.

Yes x No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of “accelerated filer and large accelerated filer” in Rule 12b-2 of the Exchange Act. (Check one.)

Large accelerated filer o	Accelerated filer o	Non-accelerated filer o

Small business issuer x

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

Yes o No x

As of May 12, 2011, the latest practicable date, 8,864,908 shares of the registrant's common stock, $.01 par value, were issued and outstanding.

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 o No o

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Cheviot Financial Corp.

CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION

(In thousands, except share data)

ASSETS	March 31, 2011 (Unaudited)	December 31, 2010
Cash and due from banks	$5,505	$ 5,776
Federal funds sold	5,229	5,924
Interest-earning deposits in other financial institutions	12,944	6,449
Cash and cash equivalents	23,678	18,149
Investment securities available for sale – at fair value	99,523	88,382
Mortgage-backed securities available for sale - at fair value	8,609	4,279
Mortgage-backed securities held to maturity - at cost, approximate market value of $5,128 and $4,916 at March 31, 2011 and December 31, 2010, respectively	4,619	4,779
Loans receivable - net	409,230	220,998
Loans held for sale - at lower of cost or market	5,148	4,440
Real estate acquired through foreclosure - net	4,519	2,007
Office premises and equipment - at depreciated cost	9,569	4,610
Federal Home Loan Bank stock - at cost	8,366	3,375
Accrued interest receivable on loans	1,784	925
Accrued interest receivable on mortgage-backed securities	37	23
Accrued interest receivable on investments and interest-earning deposits	463	392
Goodwill	10,244	-
Core deposit intangible	1,298	-
Prepaid expenses and other assets	4,731	1,510
Bank-owned life insurance	10,079	3,791
Prepaid federal income taxes	749	409
Deferred federal income taxes	4,790	-
Total assets	$607,436	$ 358,069
LIABILITIES AND SHAREHOLDERS’ EQUITY		
Deposits	$481,052	$ 257,852
Advances from the Federal Home Loan Bank	46,997	27,300
Other borrowings	1,490	-
Advances by borrowers for taxes and insurance	2,217	1,440
Accrued interest payable	195	99
Accounts payable and other liabilities	5,725	1,955
Deferred federal income taxes	-	4
Total liabilities	537,676	288,650
Commitments and contingencies		
Shareholders’ equity		

Preferred stock - authorized 5,000,000 shares, $.01 par value; none issued		
Common stock - authorized 30,000,000 shares, $.01 par value;		
9,918,751 shares issued at March 31, 2011 and December 31, 2010	99	99
Additional paid-in capital	43,875	43,878
Shares acquired by stock benefit plans	(1,302)	(1,302)
Treasury stock - at cost, 1,053,843 shares at March 31, 2011 and December 31, 2010	(12,859)	(12,860)
Retained earnings - restricted	40,798	40,655
Accumulated comprehensive loss, unrealized losses on securities available for sale, net of related tax benefits	(851)	(1,051)
Total shareholders' equity	69,760	69,419
Total liabilities and shareholders' equity	$607,436	$ 358,069

See accompanying notes to consolidated financial statements.

Cheviot Financial Corp.

CONSOLIDATED STATEMENTS OF EARNINGS (UNAUDITED)

For the three months ended March 31, 2011 and 2010
(In thousands, except per share data)

	2011	2010
Interest income		
Loans	$3,390	$3,508
Mortgage-backed securities	50	86
Investment securities	457	373
Interest-earning deposits and other	50	40
Total interest income	3,947	4,007
Interest expense		
Deposits	926	915
Borrowings	279	366
Total interest expense	1,205	1,281
Net interest income	2,742	2,726
Provision for losses on loans	150	40
Net interest income after provision for losses on loans	2,592	2,686
Other income		
Rental	20	16
Loss on sale of real estate acquired through foreclosure	(12)	-
Gain on sale of loans	46	36
Earnings on bank-owned life insurance	39	35
Other operating	167	95
Total other income	260	182
General, administrative and other expense		
Employee compensation and benefits	1,135	1,160
Occupancy and equipment	162	164
Property, payroll and other taxes	278	245
Data processing	79	61
Legal and professional	223	129
Advertising	77	50
FDIC expense	127	71
Other operating	219	218
Total general, administrative and other expense	2,300	2,098
Earnings before federal income taxes	552	770
Federal income taxes		

Current	166	302
Deferred	(166)	(35)
Total federal income taxes	-	267
NET EARNINGS	$552	$503
EARNINGS PER SHARE		
Basic	$.06	$.06
Diluted	$.06	$.06
Dividends declared per share	$.12	$.11

See accompanying notes to consolidated financial statements.

Cheviot Financial Corp.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (UNAUDITED)

For the three months ended March 31, 2011 and 2010
(In thousands)

	2011	2010
Net earnings for the period	$552	$503
Other comprehensive income, net of related tax expense:		
Unrealized holding gains on securities during the period, net of tax expense of $103 and $86 for the periods ended March 31, 2011 and 2010, respectively	200	167
Comprehensive income	$752	$670
Accumulated comprehensive loss	$(851)	$(213)

See accompanying notes to consolidated financial statements.

Cheviot Financial Corp.

CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

For the three months ended March 31, 2011 and 2010
(In thousands)

	2011	2010
Cash flows from operating activities:		
Net earnings for the period	$552	$503
Adjustments to reconcile net earnings to net cash (used in) provided by operating activities:		
Amortization of premiums and discounts on investment and mortgage-backed securities, net	5	10
Depreciation	69	80
Amortization of deferred loan origination costs (fees) - net	55	(3)
Proceeds from sale of loans in the secondary market	9,524	2,756
Loans originated for sale in the secondary market	(5,925)	(2,720)
Gain on sale of loans	(46)	(36)
Amortization of expense related to stock benefit plans	(8)	(11)
Provision for losses on loans	150	40
Federal Home Loan Bank stock dividends	-	(6)
Loss on real estate acquired through foreclosure	12	-
Impairment on real estate acquired through foreclosure	-	81
Net increase in cash surrender value of bank-owned life insurance, net of acquisition	(39)	(34)
Increase (decrease) in cash, net of acquisition, due to changes in:		
Accrued interest receivable on loans	(142)	(1)
Accrued interest receivable on mortgage-backed securities	11	3
Accrued interest receivable on investments and interest-earning deposits	57	(95)
Prepaid expenses and other assets	(151)	(268)
Accrued interest payable	(660)	3
Accounts payable and other liabilities	(828)	65
Federal income taxes		
Current	831	207
Deferred	(166)	(35)
Net cash flows provided by operating activities	3,301	539
Cash flows provided by (used in) investing activities:		
Principal repayments on loans	11,522	10,112
Loan disbursements	(8,038)	(5,697)
Purchase of investment securities – available for sale	-	(32,196)
Proceeds from maturity of investment securities – available for sale	5,000	14,901
Principal repayments on mortgage-backed securities – available for sale	337	151
Principal repayments on mortgage-backed securities – held to maturity	159	261
Proceeds from the sale of real estate acquired through foreclosure	314	-
Purchase of office premises and equipment	(102)	-
Cash paid for acquisition, net of cash received	(4,200)	-
Net cash flows provided by (used in) investing activities	4,992	(12,468)

Cash flows provided by (used in) financing activities:		
Net increase in deposits, net of acquisition	1,673	3,046
Proceeds from Federal Home Loan Bank advances	11,000	10,000
Repayments on Federal Home Loan Bank advances	(14,519)	(5,451)
Advances by borrowers for taxes and insurance, net of acquisition	(515)	(493)
Stock option expense, net	5	62
Dividends paid on common stock	(408)	(374)
Net cash flows provided by (used in) financing activities	(2,764)	6,790
Net increase (decrease) in cash and cash equivalents	5,529	(5,139)
Cash and cash equivalents at beginning of period	18,149	11,283
Cash and cash equivalents at end of period	$23,678	$6,144

See accompanying notes to consolidated financial statements.

Cheviot Financial Corp.

CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED) (CONTINUED)

For the three months ended March 31, 2011 and 2010
(In thousands)

	2011	2010
Supplemental disclosure of cash flow information:		
Cash paid during the period for:		
Federal income taxes	$120	$95
Interest on deposits and borrowings	$1,109	$1,279
Supplemental disclosure of non-cash investing activities:		
Transfer from loans to real estate acquired through foreclosure	$435	$23
Recognition of mortgage servicing rights	$62	$22

See accompanying notes to consolidated financial statements.

Cheviot Financial Corp.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

For the three months ended March 31, 2011 and 2010

1. Basis of Presentation

Cheviot Financial Corp. ("Cheviot Financial" or the "Corporation") is a financial holding company, the principal asset of which consists of its ownership of Cheviot Savings Bank (the "Savings Bank"). The Savings Bank conducts a general banking business in southwestern Ohio which consists of attracting deposits and applying those funds primarily to the origination of real estate loans. The Corporation is 62% owned by Cheviot Mutual Holding Company. Earnings per share is reported including all shares held by Cheviot Mutual Holding Company. Cheviot Mutual Holding Company has to date waived the receipt of dividends declared by the Corporation. Cheviot Savings' profitability is significantly dependent on net interest income, which is the difference between interest income from interest-earning assets and the interest expense paid on interest-bearing liabilities. Net interest income is affected by the relative amount of interest-earning assets and interest-bearing liabilities and the interest received or paid on these balances.

On March 16, 2011, the Corporation completed the acquisition of First Franklin Corporation ("First Franklin") and its wholly-owned subsidiary, The Franklin Savings and Loan Company ("Franklin Savings"). Accordingly, the Corporation's unaudited consolidated financial statements for the three months ended March 31, 2011 includes the accounts of First Franklin for the period March 17, 2011 to March 31, 2011.

The accompanying unaudited consolidated financial statements were prepared in accordance with instructions for Form 10-Q and, therefore, do not include information or footnotes necessary for a complete presentation of financial position, results of operations and cash flows in conformity with accounting principles generally accepted in the United States of America. Accordingly, these consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto of Cheviot Financial included in the Annual Report on Form 10-K for the year ended December 31, 2010. However, in the opinion of management, all adjustments (consisting of only normal recurring accruals) which are necessary for a fair presentation of the consolidated financial statements have been included. The results of operations for the three month period ended March 31, 2011 are not necessarily indicative of the results which may be expected for the entire year.

Cheviot Financial evaluates subsequent events through the date of filing with the Securities and Exchange Commission.

2. Principles of Consolidation

The accompanying consolidated financial statements as of and for the three months ended March 31, 2011 and 2010 include the accounts of the Corporation and its wholly-owned subsidiary, the Savings Bank. All significant intercompany items have been eliminated.

3. Liquidity and Capital Resources

Liquidity describes our ability to meet the financial obligations that arise in the ordinary course of business. Liquidity is primarily needed to meet the borrowing and deposit withdrawal requirements of our customers and to fund current and planned expenditures. Our primary sources of funds are deposits, scheduled amortization and prepayments of loan principal and mortgage-backed securities, maturities and calls of securities and funds provided by our operations. In addition, we may borrow from the Federal Home Loan Bank of Cincinnati. At March 31, 2011 and December 31, 2010, we had $47.0 million and $27.3 million, respectively, in outstanding borrowings from the Federal

Home Loan Bank of Cincinnati and had the capacity to increase such borrowings at those dates by approximately $125.0 million and $115.3 million, respectively.

Loan repayments and maturing securities are a relatively predictable source of funds. However, deposit flows, calls of securities and prepayments of loans and mortgage-backed securities are strongly influenced by interest rates, general and local economic conditions and competition in the marketplace. These factors reduce the predictability of these sources of funds.

Cheviot Financial Corp.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

For the three months ended March 31, 2011 and 2010

3. Liquidity and Capital Resources (continued)

Our primary investing activities are the origination of one- to four-family real estate loans, commercial real estate, construction and consumer loans, and the purchase of securities. For the three months ended March 31, 2011, loan originations totaled $14.0 million, compared to $8.4 million for the three months ended March 31, 2010.

Total deposits increased $223.2 million and $3.0 million during the three months ended March 31, 2011 and 2010, respectively. Deposit flows are affected by the level of interest rates, the interest rates and products offered by competitors and other factors.

The following table sets forth information regarding the Corporation's obligations and commitments to make future payments under contracts as of March 31, 2011.

	Payments due by period				
	Less than 1 year	More than 1-3 years	More than 4-5 years	More than 5 years	Total
			(In thousands)		
Contractual obligations:					
Advances from the Federal Home Loan Bank	$9,758	$2,662	$8,505	$26,072	$46,997
Certificates of deposit	153,177	69,691	59,653	9	282,530
Amount of loan commitments and expiration per period:					
Commitments to originate one- to four-family loans	516	-	-	-	516
Home equity lines of credit	32,450	-	-	-	32,450
Commercial lines of credit	526	-	-	-	526
Undisbursed loans in process	3,029	-	-	-	3,029
Lease obligations	132	276	290	1,518	2,216
Total contractual obligations	$199,588	$72,629	$68,448	$27,599	$368,264

We are committed to maintaining a strong liquidity position. We monitor our liquidity position on a daily basis. We anticipate that we will have sufficient funds to meet our current funding commitments. Based on our deposit retention experience and current pricing strategy, we anticipate that a significant portion of maturing time deposits will be retained.

At March 31, 2011 and 2010, we exceeded all of the applicable regulatory capital requirements. Our core (Tier 1) capital was $56.6 million and $55.2 million, or 9.5% and 16.0% of total assets at March 31, 2011 and 2010, respectively. In order to be classified as "well-capitalized" under federal banking regulations, we were required to have core capital of at least $36.4 million, or 6.0% of assets as of March 31, 2011. To be classified as a well-capitalized bank, we must also have a ratio of total risk-based capital to risk-weighted assets of at least 10.0%. At March 31, 2011 and 2010, we had a total risk-based capital ratio of 17.3% and 33.2%, respectively.

Cheviot Financial Corp.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

For the three months ended March 31, 2011 and 2010

4. Earnings Per Share

Basic earnings per share is computed based upon the weighted-average common shares outstanding during the period, less shares in the ESOP that are unallocated and not committed to be released plus shares in the ESOP that have been allocated. Weighted-average common shares deemed outstanding gives effect to 107,126 and 142,833 unallocated shares held by the ESOP for the three months ended March 31, 2011 and 2010, respectively.

	For the three months ended March 31,	
	2011	2010
Weighted-average common shares outstanding (basic)	8,757,782	8,725,873
Dilutive effect of assumed exercise of stock options	7,927	7,919
Weighted-average common shares outstanding (diluted)	8,765,709	8,733,792

5. Stock Option Plan

On April 26, 2005, the Corporation approved a Stock Incentive Plan that provides for grants of up to 486,018 stock options. During 2010, 2009 and 2008 approximately 8,860, 8,060 and 8,060 stock options were granted subject to a five year vesting period.

The Corporation follows FASB Accounting Standard Codification Topic 718 (ASC 718), "Compensation – Stock Compensation," for its stock option plans, and accordingly, the Corporation recognizes the expense of these grants as required. Stock-based employee compensation costs pertaining to stock options is reflected as a net increase in equity, for both any new grants, as well as for all unvested options outstanding at December 31, 2005, in both cases using the fair values established by usage of the Black-Scholes option pricing model, expensed over the vesting period of the underlying option.

The Corporation elected the modified prospective transition method in applying ASC 718. Under this method, the provisions of ASC 718 apply to all awards granted or modified after the date of adoption, as well as for all unvested options outstanding at December 31, 2005. The compensation cost recorded for unvested equity-based awards is based on their grant-date fair value. For the three months ended March 31, 2011, the Corporation recorded $5,000 in after-tax compensation cost for equity-based awards that vested during the three months ended March 31, 2011. The Corporation has $62,000 unrecognized pre-tax compensation cost related to non-vested equity-based awards granted under its stock incentive plan as of March 31, 2011, which is expected to be recognized over a weighted-average vesting period of approximately 0.2 years.

Cheviot Financial Corp.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

For the three months ended March 31, 2011 and 2010

5. Stock Option Plan (continued)

A summary of the status of the Corporation's stock option plan as of March 31, 2011, and changes during the period then ended is presented below:

	Three months ended March 31, 2011		Year ended December 31, 2010	
	Shares	Weighted-average exercise price	Shares	Weighted-average exercise price
Outstanding at beginning of period	421,200	$11.05	412,340	$11.17
Granted	-	-	8,860	8.07
Exercised	-	-	-	-
Forfeited	-	-	-	-
Outstanding at end of period	421,200	$11.05	421,200	$11.05
Options exercisable at period-end	397,260	$11.16	397,260	$11.16
Options expected to be exercisable at year-end				
Fair value of options granted		NA		$4.83

The following information applies to options outstanding at March 31, 2011:	
Number outstanding	421,200
Exercise price	$8.07 - $13.63
Weighted-average exercise price	$11.05
Weighted-average remaining contractual life	4.4 years

The expected term of options is based on evaluations of historical and expected future employee exercise behavior. The risk free interest rate is based upon the U.S. Treasury rates at the date of grant with maturity dates approximately equal to the expected life at the grant date. Volatility is based upon the historical volatility of the Corporation's stock.

The fair value of each option was estimated on the date of grant using the modified Black-Scholes options pricing model with the following weighted-average assumptions used for grants in 2010: dividend yield of 5.45%, expected volatility of 44.55%, risk-free interest rate of 3.38% and an expected life of 10 years for each grant.

The effects of expensing stock options are reported in “cash provided by financing activities” in the Consolidated Statements of Cash Flows.

Cheviot Financial Corp.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

For the three months ended March 31, 2011 and 2010

6. Investment and Mortgage-backed Securities

The amortized cost, gross unrealized gains, gross unrealized losses and estimated fair values of investment securities at March 31, 2011 and December 31, 2010 are shown below.

	March 31, 2011			
	Amortized cost	Gross unrealized gains	Gross unrealized losses	Estimated fair value
	(In thousands)			
Available for Sale:				
U.S. Government agency securities	$97,818	$112	$1,430	$96,500
Municipal obligations	3,143	41	161	3,023
	$100,961	$153	$1,591	$99,523

	December 31, 2010			
	Amortized cost	Gross unrealized gains	Gross unrealized losses	Estimated fair value
	(In thousands)			
Available for Sale:				
U.S. Government agency securities	$88,529	$102	$1,622	$87,009
Municipal obligations	1,545	5	177	1,373
	$90,074	$107	$1,799	$88,382

The amortized cost of investment securities at March 31, 2011, by contractual term to maturity, are shown below.

	March 31, 2011 (In thousands)
Less than one year	$ 24,136
One to five years	49,245
Five to ten years	15,684
More than ten years	11,896
	$ 100,961

Cheviot Financial Corp.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

For the three months ended March 31, 2011 and 2010

6. Investment and Mortgage-backed Securities (continued)

The amortized cost, gross unrealized gains, gross unrealized losses and estimated fair values of mortgage-backed securities at March 31, 2011 and December 31, 2010 are shown below.

	March 31, 2011			
	Amortized cost	Gross unrealized gains	Gross unrealized losses	Estimated fair value
	(In thousands)			
Available for sale:				
Federal Home Loan Mortgage Corporation adjustable-rate participation certificates	$1,276	$32	$-	$1,308
Federal National Mortgage Association adjustable-rate participation certificates	3,305	15	3	3,317
Government National Mortgage Association adjustable-rate participation certificates	3,878	106	-	3,984
	$8,459	$153	$3	$8,609
Held to maturity:				
Federal Home Loan Mortgage Corporation adjustable-rate participation certificates	$441	$57	$-	$498
Federal National Mortgage Association adjustable-rate participation certificates	489	62	-	551
Government National Mortgage Association adjustable-rate participation certificates	3,689	395	5	4,079
	$4,619	$514	$5	$5,128

	December 31, 2010			
	Amortized cost	Gross unrealized gains	Gross unrealized losses	Estimated fair value
	(In thousands)			
Available for sale:				
Federal Home Loan Mortgage Corporation adjustable-rate participation certificates	$723	$13	$-	$736
Federal National Mortgage Association adjustable-rate participation certificates	548	17	-	565
Government National Mortgage Association adjustable-rate participation certificates	2,908	70	-	2,978

	$4,179	$100	$-	$4,279

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Cheviot Financial Corp.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

For the three months ended March 31, 2011 and 2010

6. Investment and Mortgage-backed Securities (continued)

	December 31, 2010			
	Amortized cost	Gross unrealized gains	Gross unrealized losses	Estimated fair value
	(In thousands)			
Held to maturity:				
Federal Home Loan Mortgage Corporation adjustable-rate participation certificates	$464	$10	$1	$473
Federal National Mortgage Association adjustable-rate participation certificates	515	7	-	522
Government National Mortgage Association adjustable-rate participation certificates	3,800	121	-	3,921
	$4,779	$138	$1	$4,916

The amortized cost of mortgage-backed securities, including those designated as available for sale, at March 31, 2011, by contractual terms to maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may generally prepay obligations without prepayment penalties.

	March 31, 2011 (In thousands)
Due in one year or less	$ 526
Due in one year through five years	2,287
Due in five years through ten years	3,312
Due in more than ten years	6,953
	$ 13,078

The table below indicates the length of time individual securities have been in a continuous unrealized loss position at March 31, 2011:

Description of securities	Less than 12 months			12 months or longer			Total		
	Number of investments	Fair value	Unrealized losses	Number of investments	Fair value	Unrealized losses	Number of investments	Fair value	Unrealized losses
	(Dollars in thousands)								
U.S. Government agency securities	28	$71,375	$ 1,430	-	$-	$ -	28	$71,375	$ 1,430
Municipal obligations	6	659	21	2	1,095	140	8	1,754	161
Mortgage-backed securities	25	360	8	-	-	-	25	360	8

Total temporarily impaired securities	59	$72,394	$ 1,459	2	$1,095	$ 140	61	$73,489	$ 1,599

Cheviot Financial Corp.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

For the three months ended March 31, 2011 and 2010

6. Investment and Mortgage-backed Securities (continued)

Management does not intend to sell any of the debt securities with an unrealized loss and does not believe that it is more likely than not that we will be required to sell a security in an unrealized loss position prior to a recovery in value. The decline in the fair value is primarily due to an increase in market interest rates. The fair values are expected to recover as securities approach maturity dates. The Company has evaluated these securities and has determined that the decline in their values is temporary.

7. Income Taxes

The Corporation uses an asset and liability approach to accounting for income taxes. The asset and liability approach requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the carrying amounts and the tax bases of assets and liabilities. Deferred tax assets are recognized if it is more likely than not that a future benefit will be realized. The Corporation accounts for income taxes in accordance with Financial Accounting Standards Board (“FASB”) Accounting Standards Codification (“ASC”) 740, Income Taxes, which prescribes the recognition and measurement criteria related to tax positions taken or expected to be taken in a tax return.

The Corporation’s principal temporary differences between financial income and taxable income result mainly from different methods of accounting for deferred loan origination fees and costs, Federal Home Loan Bank stock dividends, the general loan loss allowance, deferred compensation, stock benefit plans, goodwill and intangible assets. The Corporation has approximately $8.3 million of net operating losses to carryforward for the next 20 years. These losses are subject to the Internal Revenue Code section 382 limitations which allow approximately $1.1 million of the losses on an annual basis to offset current year taxable income.

The Corporation recognizes the financial statement benefit of a tax position only after determining that the relevant tax authority would more likely than not sustain the position following an audit. For tax positions meeting the more-likely-than-not threshold, the amount recognized in the financial statements is the largest benefit that has a greater than 50 percent likelihood of being realized upon ultimate settlement with the relevant tax authority. At adoption date, January 1, 2007 the Corporation applied the standard to all tax positions for which the statute of limitations remained open and was not required to record any liability for unrecognized tax benefits as that date. There have been no material changes in unrecognized tax benefits since January 1, 2007. The known tax attributes which can influence the Corporation’s effective tax rate is the utilization of net operating loss carryforwards subject to the limitations under Internal Revenue Code section 382.

The Corporation is subject to income taxes in the U.S. federal jurisdiction, as well as various state jurisdictions. Tax regulations within each jurisdiction are subject to the interpretation of the related tax laws and regulations and require significant judgment to apply. With few exceptions, the Corporation is no longer subject to U.S. federal, state and local, or non U.S. income tax examinations by tax authorities for the years before 2008.

The Corporation will recognize, if applicable, interest accrued related to unrecognized tax liabilities in interest expense and penalties in operating expenses.

Cheviot Financial Corp.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

For the three months ended March 31, 2011 and 2010

7. Income Taxes (continued)

Federal income tax on earnings differs from that computed at the statutory corporate tax rate for the periods ended March 31, 2011 and 2010:

	2011	2010
	(Dollars in thousands)	
Federal income taxes at statutory rate of 34%	$ 188	$ 262
Increase (decrease) in taxes resulting primarily from:		
Stock compensation	(4)	23
Nontaxable interest income	(6)	(5)
Cash surrender value of life insurance	(13)	(12)
Utilization of net operating loss carryforwards, previously reserved	(166)	-
Other	1	(1)
Federal income taxes per financial statements	$ -	$ 267
Effective tax rate	0 %	34.7 %

8. Disclosures About Fair Value of Assets and Liabilities

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. A three-level hierarchy exists for fair value measurements based upon the inputs to the valuation of an asset or liability.

Level 1 Quoted prices in active markets for identical assets or liabilities.

Level 2 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 for substantially the full term of the assets or liabilities.

Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

Fair value methods and assumptions are set forth below for each type of financial instrument.

Securities available for sale: Fair value on available for sale securities were based upon a market approach. Securities which are fixed income instruments that are not quoted on an exchange, but are traded in active markets, are valued using prices obtained from our custodian, which used third party data service providers. Available for sale securities includes U.S. agency securities, municipal bonds and mortgage-backed agency securities.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

For the three months ended March 31, 2011 and 2010

8. Disclosures About Fair Value of Assets and Liabilities (continued)

Fair Value Measurements at March 31, 2011 and December 31, 2010

	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant other unobservable inputs (Level 3)
Securities available for sale at March 31, 2011:			
U.S. Government agency securities	-	$ 96,500	-
Municipal obligations	-	$ 3,023	-
Mortgage-backed securities	-	$ 8,609	-
Securities available for sale at December 31, 2010:			
U.S. Government agency securities	-	$ 87,009	-
Municipal obligations	-	$ 1,373	-
Mortgage-backed securities	-	$ 4,279	-

The Corporation is predominately an asset-based lender with real estate serving as collateral on a substantial majority of loans. Loans which are deemed to be impaired are primarily valued on a nonrecurring basis at the fair values of the underlying real estate collateral. In addition, on the acquisition date the Corporation independently fair valued $25.0 million of First Franklin's impaired loans, as well as $173.2 million of performing loans. First Franklin's impaired loans subject to fair value write-downs are not included in Cheviot Financial's non-performing loan totals. Such loans are considered performing under Topic ASC 310-30, even though the loans are contractually past due, as any nonpayment of contractual principal or interest is considered in the periodic re-estimation of expected cash flows and the resulting loss provisions or future period yield adjustments. The fair values were obtained using independent appraisals, which the Corporation considers to be Level 2 inputs. The aggregate carrying amount of the Corporation's impaired loans at March 31, 2011 was approximately $4.3 million, compared to approximately $4.9 million at December 31, 2010.

The Corporation has real estate acquired through foreclosure totaling $4.5 million and $2.0 million at March 31, 2011 and December 31, 2010, respectively. Real estate acquired through foreclosure is carried at the lower of the cost or fair value less estimated selling expenses at the date of acquisition. Fair values are obtained using independent appraisals, based on comparable sales which the Corporation considers to be Level 2 inputs. The aggregate amount of real estate acquired through foreclosure that is carried at fair value was approximately $3.7 million at March 31, 2011 and $1.1 million at December 31, 2010. The aggregate amount of real estate acquired through foreclosure which is carried at historic cost totaled $834,000 at March 31, 2011.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

For the three months ended March 31, 2011 and 2010

9. Effects of Recent Accounting Pronouncements

We adopted the following accounting guidance in 2011 none of which had a material effect, if any, on our consolidated financial position or results of operations.

In January 2010, the FASB issued ASU No. 2010-06 “Improving Disclosures About Fair Value Measurements,” which amends the guidance for fair value measurements and disclosures. The guidance in ASU 2010-06 requires a reporting entity to disclose separately the amounts of significant transfers in and out of Level 1 and Level 2 fair value measurements and to describe the reasons for the transfers. Furthermore, ASU 2010-06 requires a reporting entity to present separately information about purchases, sales, issuances, and settlements in the reconciliation for fair value measurements using significant unobservable inputs; clarifies existing fair value disclosures about the level of disaggregation and about inputs and valuation techniques used to measure fair value; and amends guidance on employers’ disclosures about postretirement benefit plan assets to require that disclosures be provided by classes of assets instead of by major categories of assets. The new guidance is effective for interim and annual reporting periods beginning January 1, 2010, except for the disclosures about purchases, sales, issuances, and settlements in the roll forward of activity in Level 3 fair value measurements. Those disclosures are effective January 1, 2011 and for interim periods thereafter. In the period of initial adoption, entities will not be required to provide the amended disclosures for any previous periods presented for comparative purposes. Early adoption is permitted. The adoption of this guidance did not have a significantly impact our annual and interim financial statement disclosures and did not have any impact on our consolidated financial statements.

In December 2010, the FASB issued ASU 2010-28, “When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units with Zero or Negative Carrying Amounts.” This ASU modifies Step 1 of the goodwill impairment test for reporting units with zero or negative carrying amounts. For those reporting units, an entity is required to perform Step 2 of the goodwill impairment test if it is more likely than not that a goodwill impairment exists. In determining whether it is more likely than not that a goodwill impairment exists, an entity should consider whether there are any adverse qualitative factors indicating an impairment may exist. The qualitative factors are consistent with the existing guidance, which requires that goodwill of a reporting unit be tested for impairment between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. For public entities, the amendments in this Update are effective for fiscal year, and interim periods within those years, beginning after December 15, 2010. Adoption of this guidance on January 1, 2011 did not have a material effect on the Corporation’s results of operation or financial position.

In December 2010, the FASB issued ASU 2010-29, “Disclosure of Supplementary Pro Forma Information for Business Combinations.” The amendments in this update specify that if a public entity presents comparative financial statements, the entity should disclose revenue and earnings of the combined entity as though the business combination(s) that occurred during the current year had occurred as of the beginning of the current and comparable prior annual reporting period. The amendments also expand the supplemental pro forma disclosures under Topic 805 to include a description of the nature and amount of material, nonrecurring pro forma adjustments directly attributable to the business combination included in the reported pro forma revenue and earnings. The amendments in this Update are effective prospectively for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2010. Management has provided the required pro forma disclosures related to the First Franklin acquisition in Note 11 herein.

Cheviot Financial Corp.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

For the three months ended March 31, 2011 and 2010

9. Effect of Recent Accounting Pronouncements (continued)

In April 2011, the FASB ASU No. 2011-02, "Receivables (Topic 310) - A Creditor's Determination of Whether a Restructuring Is a Troubled Debt Restructuring." ASU 2011-02 clarifies which loan modifications constitute troubled debt restructurings and is intended to assist creditors in determining whether a modification of the terms of a receivable meets the criteria to be considered a troubled debt restructuring, both for purposes of recording an impairment loss and for disclosure of troubled debt restructurings. In evaluating whether a restructuring constitutes a troubled debt restructuring, a creditor must separately conclude, under the guidance clarified by ASU 2011-02, that both of the following exist: (a) the restructuring constitutes a concession; and (b) the debtor is experiencing financial difficulties. ASU 2011-02 will be effective for the Corporation on July 1, 2011, and applies retrospectively to restructurings occurring on or after January 1, 2011. Adoption of ASU 2011-02 is not expected to have a significant impact on the Corporation's financial statements.

10. Fair Value of Financial Instruments

Fair value information about financial instruments, whether or not recognized in the balance sheet, for which it is practical to estimate the value, is based upon the characteristics of the instruments and relevant market information. Financial instruments include cash, evidence of ownership in an entity or contracts that convey or impose on an entity the contractual right or obligation to either receive or deliver cash for another financial instrument. These fair value estimates are based on relevant market information and information about the financial instruments. Fair value estimates are intended to represent the price for which an asset could be sold or liability could be settled. However, given there is no active market or observable market transactions for many of the Corporation's financial instruments, it has made estimates of many of these fair values which are subjective in nature, involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimated values.

The following methods and assumptions were used by the Corporation in estimating its fair value disclosures for financial instruments at March 31, 2011:

Cash and cash equivalents: The carrying amounts presented in the consolidated statements of financial condition for cash and cash equivalents are deemed to approximate fair value.

Investment and mortgage-backed securities: For investment and mortgage-backed securities, fair value is deemed to equal the quoted market price.

Loans receivable: The loan portfolio was segregated into categories with similar characteristics, such as one-to four-family residential, multi-family residential and commercial real estate. These loan categories were further delineated into fixed-rate and adjustable-rate loans. The fair values for the resultant loan categories were computed via discounted cash flow analysis, using current interest rates offered for loans with similar terms to borrowers of similar credit quality. For loans on deposit accounts, fair values were deemed to equal the historic carrying values. The historical carrying amount of accrued interest on loans is deemed to approximate fair value.

Federal Home Loan Bank stock: The carrying amount presented in the consolidated statements of financial condition is deemed to approximate fair value.

Cheviot Financial Corp.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

For the three months ended March 31, 2011 and 2010

10. Fair Value of Financial Instruments (continued)

Deposits: The fair value of NOW accounts, passbook accounts, and money market demand deposits is deemed to approximate the amount payable on demand at March 31, 2011. Fair values for fixed-rate certificates of deposit have been estimated using a discounted cash flow calculation using the interest rates currently offered for deposits of similar remaining maturities.

Advances from the Federal Home Loan Bank: The fair value of these advances is estimated using the rates currently offered for similar advances of similar remaining maturities or, when available, quoted market prices.

Advances by Borrowers for Taxes and Insurance: The carrying amount of advances by borrowers for taxes and insurance is deemed to approximate fair value.

Commitments to extend credit: For fixed-rate loan commitments, the fair value estimate considers the difference between current levels of interest rates and committed rates. At March 31, 2011, the fair value of the derivative loan commitments was not m