CENTRAL FEDERAL CORP
Form 10-Q
August 14, 2012
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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 June 30, 2012

or

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

For the transition period from to

Commission File Number 0-25045

CENTRAL FEDERAL CORPORATION

(Exact name of registrant as specified in its charter)

Delaware	**34-1877137**
(State or other jurisdiction of incorporation or organization)	**(IRS Employer Identification No.)**
2923 Smith Road, Fairlawn, Ohio	**44333**
(Address of principal executive offices)	**(Zip Code)**

(330) 666-7979

(Registrant s telephone number, including area code)

(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 x 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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨

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

Large accelerated filer	¨	Accelerated filer	¨
Non-accelerated filer	¨	Smaller reporting company	x

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

As of July 31, 2012, there were 825,710 shares of the registrant s Common Stock outstanding.

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FORM 10-Q

QUARTER ENDED JUNE 30, 2012

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CENTRAL FEDERAL CORPORATION

CONSOLIDATED BALANCE SHEETS

(Dollars in thousands except per share data)

	June 30, 2012 (unaudited)	December 31, 2011
ASSETS		
Cash and cash equivalents	$ 55,209	$ 61,436
Interest-bearing deposits in other financial institutions	1,984	1,984
Securities available for sale	17,312	18,516
Loans held for sale	1,573	1,210
Loans, net of allowance of $5,434 and $6,110	132,352	151,160
FHLB stock	1,942	1,942
Loan servicing rights	31	37
Foreclosed assets, net	2,345	2,370
Premises and equipment, net	5,423	5,534
Assets held for sale	167	167
Other intangible assets	69	89
Bank owned life insurance	4,338	4,273
Accrued interest receivable and other assets	2,870	2,202
	$ 225,615	$ 250,920
LIABILITIES AND STOCKHOLDERS EQUITY		
Deposits		
Noninterest bearing	$ 15,042	$ 18,409
Interest bearing	183,310	198,640
Total deposits	198,352	217,049
Long-term FHLB advances	10,000	15,742
Advances by borrowers for taxes and insurance	55	159
Accrued interest payable and other liabilities	3,771	2,871
Subordinated debentures	5,155	5,155
Total liabilities	217,333	240,976
Stockholders equity		
Preferred stock, Series A, $.01 par value; aggregate liquidation value $7,886 in 2012, $7,691 in 2011 1,000,000 shares authorized; 7,225 shares issued	7,147	7,120
Common stock, $.01 par value, shares authorized; 50,000,000 in 2012 and 2011 shares issued; 937,417 in 2012 and 2011	9	9
Additional paid-in capital	27,847	27,837
Accumulated deficit	(23,807)	(22,163)
Accumulated other comprehensive income	331	386
Treasury stock, at cost; 111,707 shares	(3,245)	(3,245)
Total stockholders equity	8,282	9,944
	$ 225,615	$ 250,920

See accompanying notes to consolidated financial statements.

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CENTRAL FEDERAL CORPORATION

CONSOLIDATED STATEMENTS OF OPERATIONS

(Dollars in thousands except per share data)

(Unaudited)

	Three months ended June 30, 2012	Three months ended June 30, 2011	Six months ended June 30, 2012	Six months ended June 30, 2011
Interest and dividend income				
Loans, including fees	$ 1,769	$ 2,350	$ 3,660	$ 4,792
Securities	58	156	121	311
FHLB stock dividends	21	21	43	43
Federal funds sold and other	41	41	81	71
	1,889	2,568	3,905	5,217
Interest expense				
Deposits	557	750	1,150	1,452
Long-term FHLB advances and other debt	81	141	190	308
Subordinated debentures	45	42	92	83
	683	933	1,432	1,843
Net interest income	1,206	1,635	2,473	3,374
Provision for loan losses	200	432	400	1,851
Net interest income after provision for loan losses	1,006	1,203	2,073	1,523
Noninterest income				
Service charges on deposit accounts	58	69	117	130
Net gains on sales of loans	92	24	135	64
Loan servicing fees, net	5	4	13	12
Net gains on sales of securities	143		143	
Earnings on bank owned life insurance	32	33	65	65
Other	10	12	25	27
	340	142	498	298
Noninterest expense				
Salaries and employee benefits	953	1,033	1,944	2,074
Occupancy and equipment	59	69	133	154
Data processing	137	145	279	289
Franchise taxes	46	64	101	130
Professional fees	199	258	417	559
Director fees	46	45	91	91
Postage, printing and supplies	56	39	104	87
Advertising and promotion	4	14	7	24
Telephone	16	18	33	40
Loan expenses	23	20	31	30
Foreclosed assets, net	188	1,152	206	1,185
Depreciation	62	104	129	218
FDIC premiums	142	175	298	350

Amortization of intangibles	10	10	20	20
Regulatory assessment	21	38	66	75
Other insurance	38	34	80	51
Other	30	44	55	75
	2,030	3,262	3,994	5,452
Net loss	(684)	(1,917)	(1,423)	(3,631)
Preferred stock dividends and accretion of discount on preferred stock	(111)	(106)	(221)	(210)
Net loss attributable to common stockholders	$ (795)	$ (2,023)	$ (1,644)	$ (3,841)
Loss per common share:				
Basic	$ (0.96)	$ (2.45)	$ (1.99)	$ (4.65)
Diluted	$ (0.96)	$ (2.45)	$ (1.99)	$ (4.65)

See accompanying notes to consolidated financial statements.

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CENTRAL FEDERAL CORPORATION

CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

(Dollars in thousands except per share data)

(Unaudited)

	Three months ended June 30,		Six months ended June 30,	
	2012	2011	2012	2011
Net loss	$ (684)	$ (1,917)	$ (1,423)	$ (3,631)
Other comprehensive income (loss):				
Change in unrealized holding gains (losses) on securities available for sale	(305)	149	(198)	84
Reclassification adjustment for gains realized in income	143		143	
Net change in unrealized gains (losses)	(162)	149	(55)	84
Tax effect				
Other comprehensive income (loss)	(162)	149	(55)	84
Comprehensive loss	$ (846)	$ (1,768)	$ (1,478)	$ (3,547)

See accompanying notes to consolidated financial statements.

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CENTRAL FEDERAL CORPORATION

CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS EQUITY

(Dollars in thousands except per share data)

(Unaudited)

	Preferred Stock	Common Stock	Additional Paid-In Capital	Accumulated Deficit	Accumulated Other Comprehensive Income	Treasury Stock	Total Stockholders Equity
Balance at January 1, 2012	$ 7,120	$ 9	$ 27,837	$ (22,163)	$ 386	$ (3,245)	$ 9,944
Net loss				(1,423)			(1,423)
Other comprehensive loss					(55)		(55)
Accretion of discount on preferred stock	27			(27)			
Release of 1,200 stock-based incentive plan shares			7				7
Stock option expense, net of forfeitures			3				3
Preferred stock dividends				(194)			(194)
Balance at June 30, 2012	$ 7,147	$ 9	$ 27,847	$ (23,807)	$ 331	$ (3,245)	$ 8,282

See accompanying notes to consolidated financial statements.

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CENTRAL FEDERAL CORPORATION

CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS EQUITY

(Dollars in thousands except per share data)

(Unaudited)

	Preferred Stock	Common Stock	Additional Paid-In Capital	Accumulated Deficit	Accumulated Other Comprehensive Income	Treasury Stock	Total Stockholders Equity
Balance at January 1, 2011	$ 7,069	$ 47	$ 27,759	$ (16,313)	$ 672	$ (3,245)	$ 15,989
Net loss				(3,631)			(3,631)
Other comprehensive loss					84		84
Accretion of discount on preferred stock	25			(25)			
Release of 1,227 stock-based incentive plan shares, net of forfeitures			16				16
Stock option expense, net of forfeitures			9				9
Preferred stock dividends				(185)			(185)
Balance at June 30, 2011	$ 7,094	$ 47	$ 27,784	$ (20,154)	$ 756	$ (3,245)	$ 12,282

See accompanying notes to consolidated financial statements.

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CENTRAL FEDERAL CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Dollars in thousands)

(Unaudited)

	Six months ended June 30, 2012	2011
Net loss	$ (1,423)	$ (3,631)
Adjustments to reconcile net loss to net cash from operating activities:		
Provision for loan losses	400	1,851
Provision for losses on foreclosed assets	182	1,139
Valuation gain on mortgage servicing rights	(1)	(3)
Depreciation	129	218
Amortization, net	357	367
Net gains on sales of securities	(143)	
Originations of loans held for sale	(11,697)	(18,927)
Proceeds from sale of loans held for sale	11,360	19,133
Net gains on sales of loans	(135)	(64)
Loss on disposal of premises and equipment	4	
Loss on sale of assets held for sale		2
Stock based compensation expense	10	25
Net change in:		
Bank owned life insurance	(65)	(65)
Accrued interest receivable and other assets	(667)	(94)
Accrued interest payable and other liabilities	705	572
Net cash from (used by) operating activities	(984)	523
Cash flows from investing activities		
Available-for-sale securities:		
Sales	2,144	
Maturities, prepayments and calls	5,854	4,737
Purchases	(7,000)	(3,491)
Loan originations and payments, net	18,338	17,445
Additions to premises and equipment	(22)	(53)
Proceeds from the sale of assets held for sale		533
Proceeds from the sale of foreclosed assets		1,000
Proceeds from mortgage insurance on foreclosed assets	29	
Net cash from investing activities	19,343	20,171
Cash flows from financing activities		
Net change in deposits	(18,740)	10,801
Repayments on long-term FHLB advances and other debt	(5,742)	(5,200)
Net change in advances by borrowers for taxes and insurance	(104)	(134)
Net cash from (used by) financing activities	(24,586)	5,467
Net change in cash and cash equivalents	(6,227)	26,161
Beginning cash and cash equivalents	61,436	34,275
Ending cash and cash equivalents	$ 55,209	$ 60,436

Supplemental cash flow information:		
Interest paid	$ 1,344	$ 1,727
Supplemental noncash disclosures:		
Transfers from loans to repossessed assets	$ 186	$
Loans transferred from held for sale to portfolio	(109)	

See accompanying notes to consolidated financial statements.

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CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands except per share data)

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation:

The consolidated financial statements include Central Federal Corporation (the Holding Company) and its wholly owned subsidiaries, CFBank, Ghent Road, Inc., and Smith Ghent LLC, together with the Holding Company referred to as the Company. The accompanying unaudited interim consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (the SEC) and in compliance with U.S. generally accepted accounting principles (GAAP). Because this report is based on an interim period, certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted.

In the opinion of the management of the Company, the accompanying unaudited interim consolidated financial statements include all adjustments necessary for a fair presentation of the Company s financial condition and the results of operations for the periods presented. These adjustments are of a normal recurring nature, unless otherwise disclosed in this Form 10-Q. The financial performance reported for the Company for the six months ended June 30, 2012 is not necessarily indicative of the results that may be expected for the full year. This information should be read in conjunction with the Company s latest Annual Report to Stockholders and Form 10-K. Reference is made to the accounting policies of the Company described in Note 1 of the Notes to Consolidated Financial Statements contained in the Company s 2011 Annual Report that was filed as Exhibit 13.1 to the Company s Form 10-K for the year ended December 31, 2011. The Company has consistently followed those policies in preparing this Form 10-Q.

Reclassifications and Reverse Stock Split: Some items in the prior period financial statements were reclassified to conform to the current presentation. Reclassifications did not impact prior period net loss or total stockholders equity. On May 4, 2012, the Company completed a 1-for-5 reverse stock split, whereby each 5 shares of the Company s common stock were reclassified into one share of common stock. All share and per share amounts for all periods presented have been adjusted to reflect the reverse split as though it had occurred prior to the earliest period presented.

Earnings (Loss) Per Common Share: The two-class method is used in the calculation of basic and diluted earnings per share. Under the two-class method, earnings available to common stockholders for the period are allocated between common stockholders and participating securities (unvested share-based payment awards) according to dividends declared (or accumulated) and participation rights in undistributed earnings. The factors used in the earnings per share computation follow:

	Three months ended June 30, 2012	Three months ended June 30, 2011	Six months ended June 30, 2012	Six months ended June 30, 2011
Basic				
Net loss	$ (684)	$ (1,917)	$ (1,423)	$ (3,631)
Less: Preferred dividends and accretion of discount on preferred stock	(111)	(106)	(221)	(210)
Less: Net loss allocated to unvested share-based payment awards	3	13	6	25
Net loss allocated to common stockholders	$ (792)	$ (2,010)	$ (1,638)	$ (3,816)
Weighted average common shares outstanding including unvested share-based payment awards	825,491	825,366	825,469	825,363
Less: Unvested share-based payment awards	(2,700)	(5,100)	(3,000)	(5,402)
Average shares	822,791	820,266	822,469	819,961

Basic loss per common share	$ (0.96)	$ (2.45)	$ (1.99)	$ (4.65)
Diluted				
Net loss allocated to common stockholders	$ (792)	$ (2,010)	$ (1,638)	$ (3,816)
Weighted average common shares outstanding for basic loss per common share	822,791	820,266	822,469	819,961
Add: Dilutive effects of assumed exercises of stock options				
Add: Dilutive effects of assumed exercises of stock warrant				
Average shares and dilutive potential common shares	822,791	820,266	822,469	819,961
Diluted loss per common share	$ (0.96)	$ (2.45)	$ (1.99)	$ (4.65)

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CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands except per share data)

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

The following potential average common shares were anti-dilutive and not considered in computing diluted loss per common share because the Company reported a net loss for the periods presented.

	Three months ended June 30,		Six months ended June 30,	
	2012	2011	2012	2011
Stock options	42,116	44,756	42,116	44,756
Stock warrant	67,314	67,314	67,314	67,314

Adoption of New Accounting Standards:

In May 2011, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2011-04 to Fair Value Measurement (ASC 820), *Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs.* This ASU amends existing guidance to achieve common fair value measurement and disclosure requirements between U.S. and international accounting principles. Overall, the guidance is consistent with existing U.S. accounting principles; however, there are some amendments that change a particular principle or requirement for measuring fair value or for disclosing information about fair value measurements. The amendments in this guidance are effective for interim and annual reporting periods beginning after December 15, 2011. The adoption of this ASU did not have a material impact on the Company s consolidated financial statements, but the additional disclosures are included in Note 6.

In June 2011, the FASB issued ASU No. 2011-05 to Comprehensive Income (ASC 220), *Presentation of Comprehensive Income.* This ASU amended existing guidance and eliminated the option to present the components of other comprehensive income as part of the statement of changes in stockholder s equity. The amendment requires that comprehensive income be presented in either a single continuous statement or in two separate consecutive statements. The amendments in this update are effective for fiscal years, and interim periods within those years, beginning after December 15, 2011 and are to be applied retrospectively. The adoption of this amendment changed the presentation of the statement of comprehensive income for the Company to two consecutive statements instead of presented as part of the consolidated statement of stockholders equity.

In December 2011, the FASB issued ASU No. 2011-12 to Comprehensive Income (ASC 220), *Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in ASU 2011-05.* This ASU amended the guidance in ASU 2011-05 related to the presentation of the effects of reclassifications out of accumulated other comprehensive income on the components of net income and other comprehensive income. The amendments in this ASU are effective at the same time as the amendments in ASU 2011-05 so that entities will not be required to comply with the presentation requirements in ASU 2011-05 that this ASU is deferring. The amendments in this ASU are effective for public entities for fiscal years, and interim periods within those years, beginning after December 15, 2011. The adoption of this ASU did not have a material impact on the Company s consolidated financial statements.

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CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands except per share data)

NOTE 2 GOING CONCERN CONSIDERATIONS AND MANAGEMENT S PLANS

Going Concern Considerations:

The consolidated financial statements have been prepared on a going concern basis, which contemplates the realization of assets and the satisfaction of liabilities in the normal course of business for the foreseeable future. However, the events and circumstances described in this Note create substantial doubt about the Company s ability to continue as a going concern.

On May 25, 2011, the Holding Company and CFBank each consented to the issuance of an Order to Cease and Desist (the Holding Company Order and the CFBank Order, respectively, and collectively, the Orders) by the Office of Thrift Supervision (OTS), the primary regulator of the Holding Company and CFBank at the time the Orders were issued. In July 2011, in accordance with the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act), the Board of Governors of the Federal Reserve System (FED) replaced the OTS as the primary regulator of the Holding Company and the Office of the Comptroller of the Currency (OCC) replaced the OTS as the primary regulator of CFBank.

The Holding Company Order requires it, among other things, to: (i) submit by June 30, 2011 (and update by December 31, 2011 and every December 31 thereafter) a capital plan to regulators that establishes a minimum tangible capital ratio commensurate with the Holding Company s consolidated risk profile, reduces the risk from current debt levels and addresses the Holding Company s cash flow needs; (ii) not pay cash dividends, redeem stock or make any other capital distributions without prior regulatory approval; (iii) not pay interest or principal on any debt or increase any Holding Company debt or guarantee the debt of any entity without prior regulatory approval; (iv) obtain prior regulatory approval for changes in directors and senior executive officers; and (v) not enter into any new contractual arrangement related to compensation or benefits with any director or senior executive officer without prior notification to regulators.

The CFBank Order requires it, among other things, to: (i) have by September 30, 2011, and maintain thereafter, 8% core capital and 12% total risk-based capital, after establishing an adequate allowance for loan and lease losses; (ii) submit by June 30, 2011 (and update by December 31, 2011 and every December 31 thereafter) a capital and business plan to regulators that describes strategies to meet these required capital ratios and contains operating strategies to achieve realistic core earnings; (iii) submit a contingency plan providing for a merger or voluntary dissolution of CFBank if capital does not reach the required levels, which requirement was extended by the OCC until the earlier of 15 days after termination of the stock offering or January 31, 2012, and a further extension of this date has been requested of the OCC; (iv) not originate, participate in or acquire any nonresidential real estate loans or commercial loans without regulatory approval, which prohibition was waived by OCC on November 9, 2011 subject to certain Board approval conditions, loan policies and credit administration procedures; (v) adopt a revised credit administration policy, problem asset reduction plan, management succession plan and liquidity management policy; (vi) limit asset growth to net interest credited on deposit liabilities absent prior regulatory approval for additional growth; (vii) not pay cash dividends or make any other capital distributions without prior regulatory approval; (viii) obtain prior regulatory approval for changes in directors and senior executive officers; (ix) not enter into any new contractual arrangement related to compensation or benefits with any director or senior executive officer without prior notification to regulators; (x) not enter into any significant arrangement or contract with a third party service provider without prior regulatory approval; and (xi) comply with the Federal Deposit Insurance Corporation (FDIC) limits on brokered deposits. As a result of the CFBank Order, CFBank is considered adequately capitalized for regulatory purposes.

The Company has been unprofitable for over the past three years and, unless additional capital is infused into the Holding Company and CFBank, it is unlikely that we will be able to generate profits in the future. This would cause our capital levels to continue to erode. If that happens, the regulators could take additional enforcement action against us, including the imposition of further operating restrictions. The regulators could also direct us to seek a merger partner, liquidate CFBank or be placed into receivership.

The Holding Company is significantly dependent on dividends from CFBank to provide the liquidity necessary to meet its obligations. As of June 30, 2012, pursuant to the CFBank Order, CFBank may not declare or pay dividends or make any other capital distributions without receiving the prior written approval of the OCC. Future dividend payments by CFBank to the Holding Company would be based on future earnings and the approval of the OCC. The payment of dividends from CFBank to the Holding Company is not likely to be approved by the

OCC while CFBank is suffering significant losses.

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CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands except per share data)

NOTE 2 GOING CONCERN CONSIDERATIONS AND MANAGEMENT S PLANS (continued)

The significant directives contained in the Orders, including higher capital requirements, requirements to reduce the level of our criticized and classified assets, growth and operating restrictions, restrictions on brokered deposits, restrictions on certain types of lending and restrictions on dividend payments have impeded and may further impede our ability to operate our business and to effectively compete in our markets. In addition, the regulators must approve any deviation from our business plan, which could limit our ability to make any changes to our business and could negatively impact the scope and flexibility of our business activities.

The requirements of the Orders will remain in effect until terminated, modified or suspended by regulators.

Management s Plans:

The Company announced the terms of a registered common stock offering of up to $30,000 on August 9, 2011. The registered common stock offering consisted of a $24,965 rights offering and a $5,035 offering to a group of standby purchasers. Under the terms of the rights offering, all record holders of the Company s common stock as of February 8, 2012 received, at no charge, one subscription right for each share of common stock held as of the record date, which was prior to the 1 for 5 reverse stock split effective May 4, 2012. Each subscription right entitled the holder of the right to purchase 6.0474 shares of Company common stock (pre-split) at a subscription price of $1.00 per share (pre-split). Shares were also available to the public at $1.00 per share. In addition, for each three shares of company stock purchased, purchasers were to receive, at no charge, one warrant to purchase one additional share of common stock at a purchase price of $1.00 per share. The warrants were to be exercisable for three years. The Company had separately entered into a series of standby purchase agreements with a group of investors led by Timothy T. O Dell, Thad R. Perry and Robert E. Hoeweler. Under the standby purchase agreements, the standby purchasers were to acquire 5.0 million shares of Company common stock at a price of $1.00 per share and receive warrants with the same terms and conditions as all purchasers in the rights offering. The standby purchasers had conditioned their purchase of shares of common stock upon the receipt by the Company of at least $16,500 in net proceeds from the rights offering. The registration statement related to the rights offering is on file with the SEC and became effective on February 8, 2012.

The Company suspended this offering and returned all subscriptions received. The Company modified the terms of the offering and filed post-effective amendments to its registration statement with the SEC, which was declared effective on June 14, 2012.

The terms of the restructured registered common stock offering were as follows: a rights offering of up to $18,000 and a $4,500 offering to a group of standby purchasers, as well as a public offering of any unsold shares. Under the terms of the rights offering, all holders of the Company s common stock as of the record date, June 14, 2012, received, at no charge, one subscription right for each share of common stock held as of the record date, which was after the 1 for 5 reverse stock split effective May 4, 2012. Each subscription right entitled the holder of the right to purchase 14.5329 shares of Company common stock (post-split) at a subscription price of $1.50 per share (post-split). The rights offering period expired on July 16, 2012, and unsubscribed shares were made available to the public beginning on July 17, 2012 at $1.50 per share. The public offering of unsubscribed shares of common stock will end on or before August 14, 2012. The Company separately entered into a series of standby purchase agreements with a group of investors led by Timothy T. O Dell, Thad R. Perry and Robert E. Hoeweler. Under the standby purchase agreements, the standby purchasers will acquire 3.0 million shares of Company common stock at a price of $1.50 per share. The standby purchasers have conditioned their purchase of shares of common stock upon the receipt by the Company of at least $13,500 in net proceeds from the rights offering and public offering.

A portion of the proceeds from the restructured registered common stock offering is expected to be retained by the Holding Company for general corporate purposes and is estimated to be sufficient to support the Holding Company s cash requirements. Given the uncertainty surrounding CFBank s future ability to pay dividends to the Holding Company, the current levels of problem assets, the continuing depressed economy and the longer periods of time necessary to work out problem assets in the current economy, the Board of Directors and management are relying on completion of the restructured registered common stock offering to provide additional funding to support the Holding Company s working capital needs. Should the restructured registered common stock offering be unsuccessful, there can be no assurance that additional funding sources will be available, which would have a material adverse impact on our financial condition.

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CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands except per share data)

NOTE 2 GOING CONCERN CONSIDERATIONS AND MANAGEMENT S PLANS (continued)

Without additional capital, it is unlikely that the Holding Company will have sufficient liquidity to continue to meet its operating expenses as they become due. This could result in the Holding Company being subject to additional regulatory restrictions which could ultimately result in the Holding Company being instructed to seek a merger partner, liquidate CFBank or be placed into receivership.

The Holding Company s available cash at June 30, 2012 is believed by management to be sufficient to cover operating expenses and expenses in connection with the restructured registered common stock offering, at their current projected levels, through approximately December 31, 2012. No assurance can be given that operating expenses, including expenses in connection with the registered common stock offering, will not increase from their current projected levels. As a result, there can be no assurance of the sufficiency of the Holding Company s cash through December 31, 2012. The Board of Directors elected to defer scheduled dividend payments related to the Preferred Stock, as defined in Note 11 to these consolidated financial statements, beginning with the November 15, 2010 payment, and the interest payments on the subordinated debentures beginning with the December 30, 2010 payment, in order to preserve cash at the Holding Company. The Company expects that the Board will also elect to defer future payments until the Company is recapitalized. Pursuant to the Holding Company Order, the Holding Company may not pay dividends on the Preferred Stock or interest on the subordinated debentures without the prior written notice to and written non-objection from the FED.

As of June 30, 2012, the Company had incurred and paid $1.2 million in costs related to the registered common stock offering that are included in other assets in the consolidated balance sheet. Costs related to the registered common stock offering incurred and paid by the Holding Company totaled $452,000 and those incurred and paid by CFBank totaled $768,000 as of June 30, 2012. The Company expects to incur additional costs prior to completion of the restructured stock offering. In the event the restructured registered common stock offering is not successful, these costs will be charged against current operations and will have a negative impact on earnings.

Because CFBank is no longer considered to be well-capitalized for regulatory purposes, it is prohibited from accepting or renewing brokered deposits, including reciprocal deposits in the Certificate of Deposit Account Registry Service® (CDARS) program, without FDIC approval. CFBank received limited waivers from the prohibition on renewal of reciprocal CDARS deposits from the FDIC, each for 90 day periods which expired on September 20, 2011, December 19, 2011, March 18, 2012, June 16, 2012 and a current limited waiver which expires on September 14, 2012. The current limited waiver allows CFBank to roll over or renew core deposits in the reciprocal CDARS program that have yet to mature or have matured and remained with CFBank between June 17, 2012 and September 14, 2012. Management intends to submit additional requests for waivers in the future; however, there can be no assurance that the requests will be granted by the FDIC or that customers will roll over or renew their CDARS deposits even if CFBank is granted additional waivers.

The prohibition on brokered deposits significantly limits CFBank s ability to participate in the CDARS program and impacts CFBank s liquidity management. As a result of the losses in 2009, 2010 and the first quarter of 2011, management had been concerned that CFBank would be restricted from accepting or renewing brokered deposits, in addition to other regulatory restrictions, and moved aggressively in 2011, prior to receipt of the CFBank Order, to build on-balance-sheet liquidity to deal with scheduled brokered deposit maturities and the potential impact of other regulatory restrictions on liquidity. At June 30, 2012, CFBank had $43,335 in brokered deposits with maturity dates from July 2012 through August 2016. At June 30, 2012, cash, unpledged securities and deposits in other financial institutions totaled $56,194, which was sufficient to cover all brokered deposit maturities. Brokered deposit maturities over the next five years are as follows:

June 30, 2013	$ 18,942
June 30, 2014	14,367
June 30, 2015	3,412
June 30, 2016	6,415

June 30, 2017	199
	$ 43,335

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CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands except per share data)

NOTE 2   GOING CONCERN CONSIDERATIONS AND MANAGEMENT S PLANS (continued)

We have taken such actions as we believe are necessary to comply with all requirements of the Orders which are currently effective, except the higher capital requirements, and we are continuing to work toward compliance with the provisions of the Orders having future compliance dates.

These financial statements do not include any adjustments that may result should the Company be unable to continue as a going concern.

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CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands except per share data)

NOTE 3 SECURITIES

The following table summarizes the amortized cost and fair value of the available-for-sale securities portfolio at June 30, 2012 and December 31, 2011 and the corresponding amounts of unrealized gains and losses recognized in accumulated other comprehensive income (loss):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
June 30, 2012				
Issued by U.S. government-sponsored entities and agencies:				
Mortgage-backed securities residential	$ 1,655	$ 100	$	$ 1,755
Collateralized mortgage obligations	15,326	231		15,557
Total	$ 16,981	$ 331	$	$ 17,312

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
December 31, 2011				
Issued by U.S. government-sponsored entities and agencies:				
Mortgage-backed securities residential	$ 1,475	$ 198	$	$ 1,673
Collateralized mortgage obligations	16,655	204	16	16,843
Total	$ 18,130	$ 402	$ 16	$ 18,516

There was no other-than-temporary impairment recognized in accumulated other comprehensive income (loss) for securities available for sale at June 30, 2012 or December 31, 2011.

The proceeds from the sales of securities for the three and six months ended June 30, 2012 are listed below. There were no proceeds from sales for the three and six months ended June 30, 2011.

	Three months ended June 30, 2012	Six months ended June 30, 2012
Proceeds	$ 2,144	$ 2,144
Gross gains	143	143
Gross losses		
Tax effect expense	$	$

At June 30, 2012 and December 31, 2011, there were no debt securities contractually due at a single maturity date. The amortized cost and fair value of mortgage-backed securities and collateralized mortgage obligations which are not due at a single maturity date, totaled $16,981 and

$17,312 at June 30, 2012, respectively, and $18,130 and $18,516 at December 31, 2011, respectively.

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CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands except per share data)

NOTE 3 SECURITIES (continued)

Fair value of securities pledged was as follows:

	June 30, 2012	December 31, 2011
Pledged as collateral for:		
FHLB advances	$ 5,994	$ 9,336
Public deposits	1,917	2,820
Customer repurchase agreements	5,330	3,557
Interest-rate swaps	1,770	1,464
Total	$ 15,011	$ 17,177

At June 30, 2012 and December 31, 2011, there were no holdings of securities of any one issuer, other than U.S. government-sponsored entities and agencies, in an amount greater than 10% of stockholders equity.

There were no securities with unrealized losses at June 30, 2012. The following table summarizes securities with unrealized losses at December 31, 2011 aggregated by major security type and length of time in a continuous unrealized loss position.

December 31, 2011	Less than 12 Months		12 Months or More		Total	
Description of Securities	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
Issued by U.S. government-sponsored entities and agencies:						
Collateralized mortgage obligations	$ 2,882	$ 16	$	$	$ 2,882	$ 16
Total temporarily impaired	$ 2,882	$ 16	$	$	$ 2,882	$ 16

The unrealized loss at December 31, 2011 is related to two Ginnie Mae collateralized mortgage obligations. These securities carry the full faith and credit guarantee of the U.S. government. Because the decline in fair value is attributable to changes in market conditions, and not credit quality, and because the Company does not have the intent to sell these securities and it is likely that it will not be required to sell these securities before their anticipated recovery, the Company did not consider these securities to be other-than-temporarily impaired at December 31, 2011.

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CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands except per share data)

NOTE 4 LOANS

The following table presents the recorded investment in loans by portfolio segment. The recorded investment in loans includes the principal balance outstanding adjusted for purchase premiums and discounts, deferred loan fees and costs and includes accrued interest.

	June 30, 2012	December 31, 2011
Commercial	$ 20,599	$ 25,994
Real estate:		
Single-family residential	17,710	18,214
Multi-family residential	23,070	27,163
Commercial	61,632	69,757
Consumer:		
Home equity lines of credit	13,662	14,921
Other	1,113	1,221
Subtotal	137,786	157,270
Less: ALLL	(5,434)	(6,110)
Loans, net	$ 132,352	$ 151,160

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CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands except per share data)

NOTE 4 LOANS (continued)

The ALLL is a valuation allowance for probable incurred credit losses in the loan portfolio based on management s evaluation of various factors including past loan loss experience, the nature and volume of the portfolio, information about specific borrower situations and estimated collateral values, economic conditions and other factors. A provision for loan losses is charged to operations based on management s periodic evaluation of these and other pertinent factors described in Note 1 of the Notes to Consolidated Financial Statements contained in the Company s 2011 Annual Report that was filed as Exhibit 13.1 to the Company s Form 10-K for the year ended December 31, 2011.

The following tables present the activity in the ALLL by portfolio segment for the three and six months ended June 30, 2012:

	Three months ended June 30, 2012						
		Real Estate			Consumer		
	Commercial	Single-family	Multi-family	Commercial	Home equity lines of credit	Other	Total
Beginning balance	$ 1,802	$ 190	$ 1,446	$ 1,912	$ 274	$ 17	$ 5,641
Addition to (reduction in) provision for loan losses	(589)	58	(58)	712	45	32	200
Charge-offs	(84)	(7)	(18)	(496)	(40)	(34)	(679)
Recoveries	248	4		2	7	2	263
Reclass of ALLL on loan-related commitments [1]	9						9
Ending balance	$ 1,386	$ 245	$ 1,370	$ 2,130	$ 286	$ 17	$ 5,434

(1) Reclassified from (to) accrued interest payable and other liabilities in the consolidated balance sheet

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CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands except per share data)

NOTE 4 LOANS (continued)

	Six months ended June 30, 2012						
		Real Estate			Consumer		
					Home equity lines of		
	Commercial	Single-family	Multi-family	Commercial	credit	Other	Total
Beginning balance	$ 2,281	$ 207	$ 1,470	$ 1,863	$ 272	$ 17	$ 6,110
Addition to (reduction in) provision for loan losses	(1,097)	39	312	1,059	64	23	400
Charge-offs	(99)	(7)	(434)	(930)	(60)	(34)	(1,564)
Recoveries	292	6	22	138	10	11	479
Reclass of ALLL on loan-related commitments [1]	9						9
Ending balance	$ 1,386	$ 245	$ 1,370	$ 2,130	$ 286	$ 17	$ 5,434

[1] Reclassified from (to) accrued interest payable and other liabilities in the consolidated balance sheet

The following tables present the activity in the ALLL by portfolio segment for the three and six months ended June 30, 2011:

	Three months ended June 30, 2011							
		Real Estate				Consumer		
						Home equity lines of		
	Commercial	Single-family	Multi-family	Commercial	Construction	credit	Other	Total
Beginning balance	$ 3,141	$ 233	$ 1,939	$ 3,848	$ 34	$ 201	$ 21	$ 9,417
Addition to (reduction in) provision for loan losses	240	14	693	(488)	(34)	16	(9)	432
Charge-offs	(640)	(7)	(450)	(850)				(1,947)
Recoveries		2	1	122		3	7	135
Reclass of ALLL on loan-related commitments [1]	13							13
Ending balance	$ 2,754	$ 242	$ 2,183	$ 2,632	$	$ 220	$ 19	$ 8,050

[1] Reclassified from (to) accrued interest payable and other liabilities in the consolidated balance sheet

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CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands except per share data)

NOTE 4 LOANS (continued)

	Six months ended June 30, 2011							
		Real Estate				Consumer		
	Commercial	Single-family	Multi-family	Commercial	Construction	Home equity lines of credit	Other	Total
Beginning balance	$ 1,879	$ 241	$ 2,520	$ 4,719	$ 74	$ 303	$ 22	$ 9,758
Addition to (reduction in) provision for loan losses	1,945	11	911	(860)	(74)	(88)	6	1,851
Charge-offs	(1,140)	(14)	(1,250)	(1,350)			(18)	(3,772)
Recoveries	71	4	2	123		5	9	214
Reclass of ALLL on loan-related commitments [1]	(1)							(1)
Ending balance	$ 2,754	$ 242	$ 2,183	$ 2,632	$	$ 220	$ 19	$ 8,050

[1] Reclassified from (to) accrued interest payable and other liabilities in the consolidated balance sheet

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CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands except per share data)

NOTE 4 LOANS (continued)

The following table presents the balance in the ALLL and the recorded investment in loans by portfolio segment and based on the impairment method as of June 30, 2012:

			Real Estate		Consumer		
	Commercial	Single-family	Multi-family	Commercial	Home equity lines of credit	Other	Total
ALLL:							
Ending allowance balance attributable to loans:							
Individually evaluated for impairment	$ 569	$ 49	$ 12	$ 285	$	$	$ 915
Collectively evaluated for impairment	817	196	1,358	1,845	286	17	4,519
Total ending allowance balance	$ 1,386	$ 245	$ 1,370	$ 2,130	$ 286	$ 17	$ 5,434
Loans:							
Individually evaluated for impairment	$ 809	$ 130	$ 4,032	$ 5,815	$	$	$ 10,786
Collectively evaluated for impairment	19,790	17,580	19,038	55,817	13,662	1,113	127,000
Total ending loan balance	$ 20,599	$ 17,710	$ 23,070	$ 61,632	$ 13,662	$ 1,113	$ 137,786

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CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands except per share data)

NOTE 4 LOANS (continued)

The following table presents the balance in the ALLL and the recorded investment in loans by portfolio segment and based on the impairment method as of December 31, 2011:

		Real Estate			Consumer		
	Commercial	Single-family	Multi-family	Commercial	Home equity lines of credit	Other	Total
ALLL:							
Ending allowance balance attributable to loans:							
Individually evaluated for impairment	$ 624	$	$ 11	$ 262	$	$	$ 897
Collectively evaluated for impairment	1,657	207	1,459	1,601	272	17	5,213
Total ending allowance balance	$ 2,281	$ 207	$ 1,470	$ 1,863	$ 272	$ 17	$ 6,110
Loans:							
Individually evaluated for impairment	$ 821	$	$ 5,090	$ 6,085	$ 135	$	$ 12,131
Collectively evaluated for impairment	25,173	18,214	22,073	63,672	14,786	1,221	145,139
Total ending loan balance	$ 25,994	$ 18,214	$ 27,163	$ 69,757	$ 14,921	$ 1,221	$ 157,270

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CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands except per share data)

NOTE 4 LOANS (continued)

The following table presents loans individually evaluated for impairment by class of loans at June 30, 2012. The unpaid principal balance is the contractual principal balance outstanding. The recorded investment is the unpaid principal balance adjusted for partial charge-offs, purchase premiums and discounts, deferred loan fees and costs and includes accrued interest. There was no cash-basis interest income recognized during the three and six months ended June 30, 2012.

	As of June 30, 2012			Three months ended June 30, 2012		Six months ended June 30, 2012	
	Unpaid Principal Balance	Recorded Investment	ALLL Allocated	Average Recorded Investment	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:							
Commercial	$ 147	$ 132	$	$ 133	$	$ 89	$
Real estate:							
Multi-family residential	4,970	3,942		3,955	29	4,099	39
Commercial:							
Non-owner occupied	2,672	1,882		1,909		1,571	
Owner occupied	839	409		413		422	
Total with no allowance recorded	8,628	6,365		6,410	29	6,181	39
With an allowance recorded:							
Commercial	677	677	569	679	9	687	22
Real estate:							
Single-family residential	130	130	49	131		111	
Multi-family residential	90	90	12	90	2	91	3
Commercial:							
Non-owner occupied	2,684	2,684	261	2,411	36	2,404	87
Owner occupied	405	405	7	406	6	407	12
Land	480	435	17	438	6	461	13
Total with an allowance recorded	4,466	4,421	915	4,155	59	4,161	137
Total	$ 13,094	$ 10,786	$ 915	$ 10,565	$ 88	$ 10,342	$ 176

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CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands except per share data)

NOTE 4 LOANS (continued)

The following table presents loans individually evaluated for impairment by class of loans at December 31, 2011. The unpaid principal balance is the contractual principal balance outstanding. The recorded investment is the unpaid principal balance adjusted for partial charge-offs, purchase premiums and discounts, deferred loan fees and costs and includes accrued interest. There was no cash-basis interest income recognized during the three and six months ended June 30, 2011.

	As of December 31, 2011			Three months ended June 30, 2011		Six months ended June 30, 2011	
	Unpaid Principal Balance	Recorded Investment	ALLL Allocated	Average Recorded Investment	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:							
Commercial	$ 573	$ 47	$	$ 154	$	$ 149	$
Real estate:							
Multi-family residential	6,742	4,996				47	
Commercial:							
Non-owner occupied	2,177	1,755		75		76	
Owner occupied	876	446					
Land				686	11	690	21
Consumer:							
Home equity lines of credit:							
Originated for portfolio	135	135		136		136	
Total with no allowance recorded	10,503	7,379		1,051	11	1,098	21
With an allowance recorded:							
Commercial	796	774	624	1,112		1,487	
Real estate:							
Multi-family residential	94	94	11	3,147		3,433	
Commercial:							
Non-owner occupied	2,823	2,823	210	1,623		1,938	
Owner occupied	411	411	20	1,051		1,051	
Land	766	650	32				
Total with an allowance recorded	4,890	4,752	897	6,933		7,909	
Total	$ 15,393	$ 12,131	$ 897	$ 7,984	$ 11	$ 9,007	$ 21

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CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands except per share data)

NOTE 4 LOANS (continued)

The following table presents the recorded investment in nonaccrual loans by class of loans:

	June 30, 2012	December 31, 2011
Nonaccrual loans:		
Commercial	$ 132	$ 47
Real estate:		
Single-family residential	551	736
Multi-family residential	2,035	4,996
Commercial:		
Non-owner occupied	1,882	1,910
Owner occupied	409	446
Consumer:		
Home equity lines of credit:		
Originated for portfolio	66	157
Purchased for portfolio	81	9
Total nonaccrual and nonperforming loans	$ 5,156	$ 8,301

Nonaccrual loans include both smaller balance single-family mortgage and consumer loans that are collectively evaluated for impairment and individually classified impaired loans. There were no loans 90 days or more past due and still accruing interest at June 30, 2012 or December 31, 2011.

CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands except per share data)

NOTE 4 LOANS (continued)

The following table presents the aging of the recorded investment in past due loans by class of loans as of June 30, 2012:

	30 - 59 Days Past Due	60 - 89 Days Past Due	Greater than 90 Days Past Due	Total Past Due	Loans Not Past Due	Nonaccrual Loans Not > 90 days Past Due
Commercial	$	$	$ 132	$ 132	$ 20,467	$
Real estate:						
Single-family residential	348	248	91	687	17,023	460
Multi-family residential			2,035	2,035	21,035	
Commercial:						
Non-owner occupied	301		1,016	1,317	29,799	866
Owner occupied			409	409	25,405	
Land					4,702	
Consumer:						
Home equity lines of credit:						
Originated for portfolio	54		66	120	11,143	
Purchased for portfolio	132		81	213	2,186	
Other	20			20	1,093	
Total	$ 855	$ 248	$ 3,830	$ 4,933	$ 132,853	$ 1,326

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CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands except per share data)

NOTE 4 LOANS (continued)

The following table presents the aging of the recorded investment in past due loans by class of loans as of December 31, 2011:

	30 - 59 Days Past Due	60 - 89 Days Past Due	Greater than 90 Days Past Due	Total Past Due	Loans Not Past Due	Nonaccrual Loans Not > 90 Days Past Due
Commercial	$ 103	$	$	$ 103	$ 25,891	$ 47
Real estate:						
Single-family residential	714	474	491	1,679	16,535	245
Multi-family residential			3,065	3,065	24,098	1,931
Commercial:						
Non-owner occupied	173	275	68	516	35,899	1,842
Owner occupied					27,900	446
Land					5,442	
Consumer:						
Home equity lines of credit:						
Originated for portfolio	22		135	157	12,126	22
Purchased for portfolio			9	9	2,629	
Other		30		30	1,191	
Total	$ 1,012	$ 779	$ 3,768	$ 5,559	$ 151,711	$ 4,533

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CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands except per share data)

NOTE 4 LOANS (continued)

Troubled Debt Restructurings (TDRs):

The Company has allocated $915 and $897 of specific reserves to loans whose terms have been modified in TDRs as of June 30, 2012 and December 31, 2011. The Company has not committed to lend additional amounts as of June 30, 2012 or December 31, 2011 to customers with outstanding loans that are classified as nonaccrual TDRs.

During the quarter ended June 30, 2012, the terms of one loan were modified as a TDR, where concessions were granted to a borrower experiencing financial difficulties. The modification of the terms of this non-owner occupied commercial real estate loan included an extension of the maturity date from May 31, 2012 to September 30, 2012 and required a $50 principal repayment at the date of modification.

During the six months ended June 30, 2012, the terms of 2 loans were modified as TDRs, where concessions were granted to borrowers experiencing financial difficulties. In addition to the loan described in the preceding paragraph, one single-family residential loan was modified as a TDR during the six months ended June 30, 2012 and included a reduction in the stated interest rate of the loan from 10% to 5%, a waiver of a portion of the accrued and unpaid interest, addition of the remaining accrued and unpaid interest to the principal balance and extension of the maturity date from 2034 to 2042. This modification involved a reduction in the stated interest rate of the loan for a period of 30 years.

The following table presents loans modified as TDRs by class of loans during the three and six months ended June 30, 2012:

	Three months ended June 30, 2012			Six months ended June 30, 2012		
	Number of Loans	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Number of Loans	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Real estate:						
Single-family residential		$	$	1	$ 132	$ 138
Commercial:						
Non-owner occupied	1	478	428	1	478	428
Total	1	$ 478	$ 428	2	$ 610	$ 566

The TDRs described resulted in a $46 increase in the ALLL during the three and six months ended June 30, 2012 and did not result in a charge-off during the three and six months ended June 30, 2012.

There were no TDRs in payment default or that became nonperforming during the period ended June 30, 2012, that had been modified within the twelve months ended June 30, 2012. A loan is considered to be in payment default once it is 90 days contractually past due under the modified terms, at which time the loan is re-evaluated to determine whether an impairment loss should be recognized, either through a write-off or specific valuation allowance, so that the loan is reported, net, at the present value of estimated future cash flows, or at the fair value of collateral, less cost to sell, if repayment is expected solely from the collateral.

The terms of certain other loans were modified during the six months ended June 30, 2012 that did not meet the definition of a TDR. These loans had a total recorded investment as of June 30, 2012 of $5,448. The modification of these loans involved either a modification of the terms of a loan to borrowers who were not experiencing financial difficulties, a delay in a payment that was considered to be insignificant or there were no concessions granted.

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CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands except per share data)

NOTE 4 LOANS (continued)

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.

There were no loans which were modified during the three or six months ended June 30, 2012 that did not meet the definition of a TDR due to a delay in payment that was considered to be insignificant.

Nonaccrual loans include loans that were modified and identified as TDRs and the loans are not performing. At June 30, 2012 and December 31, 2011, nonaccrual TDRs were as follows:

	June 30, 2012	December 31, 2011
Commercial	$	$ 47
Real estate:		
Single-family residential	130	
Multi-family residential		2,527
Commercial:		
Owner occupied	410	446
Total	$ 540	$ 3,020

Nonaccrual loans at June 30, 2012 and December 31, 2011 do not include $6,198 and $4,597, respectively, of TDRs where customers have established a sustained period of repayment performance, generally six months, loans are current according to their modified terms and repayment of the remaining contractual payments is expected. These loans are included in total impaired loans.

Credit Quality Indicators:

The Company categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt, such as current financial information, historical payment experience, credit documentation, public information and current economic trends, among other factors. Management analyzes loans individually by classifying the loans as to credit risk. This analysis includes commercial, commercial real estate and multi-family residential real estate loans. Internal loan reviews for these loan types are performed at least annually, and more often for loans with higher credit risk. Adjustments to loan risk ratings are made based on the reviews and at any time information is received that may affect risk ratings. The following definitions are used for risk ratings:

Special Mention. Loans classified as special mention have a potential weakness that deserves management s close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or of CFBank s credit position at some future date.

Substandard. Loans classified as substandard are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that there will be some loss if the deficiencies are not corrected.

Doubtful. Loans classified as doubtful have all the weaknesses inherent in those classified as substandard, with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable and improbable.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands except per share data)

NOTE 4 LOANS (continued)

Loans not meeting the criteria to be classified into one of the above categories are considered to be not rated or pass-rated loans. Loans listed as not rated are primarily groups of homogeneous loans. Past due information is the primary credit indicator for groups of homogenous loans. Loans listed as pass-rated loans are loans that are subject to internal loan reviews and are determined not to meet the criteria required to be classified as special mention, substandard or doubtful. The recorded investment in loans by risk category and by class of loans as of June 30, 2012 and based on the most recent analysis performed follows. There were no loans rated doubtful at June 30, 2012.

	Not Rated	Pass	Special Mention	Substandard	Total
Commercial	$ 356	$ 15,768	$ 3,194	$ 1,281	$ 20,599
Real estate:					
Single-family residential	17,159			551	17,710
Multi-family residential		12,418	5,840	4,812	23,070
Commercial:					
Non-owner occupied	342	22,071	3,043	5,660	31,116
Owner occupied		21,543	3,078	1,193	25,814
Land	905	251	436	3,110	4,702
Consumer:					
Home equity lines of credit:					
Originated for portfolio	11,197			66	11,263
Purchased for portfolio	1,873		445	81	2,399
Other	1,113				1,113
	$ 32,945	$ 72,051	$ 16,036	$ 16,754	$ 137,786

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands except per share data)

NOTE 4 LOANS (continued)

The recorded investment in loans by risk category and by class of loans as of December 31, 2011 follows.

	Not Rated	Pass	Special Mention	Substandard	Doubtful	Total
Commercial	$ 432	$ 19,591	$ 2,062	$ 3,909	$	$ 25,994
Real estate:						
Single-family residential	17,478			736		18,214
Multi-family residential		15,395	4,539	6,822	407	27,163
Commercial:						
Non-owner occupied	365	22,159	5,717	8,176		36,417
Owner occupied		22,526	3,474	1,898		27,898
Land	954	1,123		3,365		5,442
Consumer:						
Home equity lines of credit:						
Originated for portfolio	12,126			157		12,283
Purchased for portfolio	2,182		447	9		2,638
Other	1,221					1,221
	$ 34,758	$ 80,794	$ 16,239	$ 25,072	$ 407	$ 157,270

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands except per share data)

NOTE 5 FORECLOSED ASSETS

Foreclosed assets were as follows:

	June 30, 2012	December 31, 2011
Real Estate:		
Single-family residential	$ 48	$
Commercial	3,436	3,509
Subtotal	3,484	3,509
Valuation allowance	(1,139)	(1,139)
Total	$ 2,345	$ 2,370

Activity in the valuation allowance was as follows:

	Three months ended June 30,		Six months ended June 30,	
	2012	2011	2012	2011
Beginning valuation allowance	$ 1,139	$	$ 1,139	$
Additions charged to expense	182	1,139	182	1,139
Direct write-downs	(182)		(182)	
Ending valuation allowance	$ 1,139	$ 1,139	$ 1,139	$ 1,139

Expenses related to foreclosed assets include:

	Three months ended June 30,		Six months ended June 30,	
	2012	2011	2012	2011
Net loss (gain) on sales	$	$	$	$
Provision for unrealized losses	182	1,139	182	1,139
Operating expenses, net of rental income	6	13	24	46
	$ 188	$ 1,152	$ 206	$ 1,185

Foreclosed assets at June 30, 2012 included one single-family residential property and five commercial real estate properties. Foreclosed assets at December 31, 2011 included three commercial real estate properties. The valuation allowance was established in the second quarter of 2011 due to a decline in real estate values on one of the commercial real estate properties, which is undeveloped commercial real estate located in Columbus, Ohio.

CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands except per share data)

NOTE 6 FAIR VALUE

Fair value is the exchange price that would be received for an asset or paid to transfer a liability 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:

Securities available for sale: The fair value of securities available for sale is determined using pricing models that vary based on asset class and include available trade, bid and other market information or matrix pricing, which is a mathematical technique widely used in the industry to value debt securities without relying exclusively on quoted prices for the specific securities but rather by relying on the securities relationship to other benchmark quoted securities (Level 2).

Loans held for sale, at fair value: Loans held for sale are carried at fair value, as determined by outstanding commitments from third party investors (Level 2).

Derivatives: The fair value of derivatives is based on valuation models using observable market data as of the measurement date (Level 2).

Loan servicing rights: On a quarterly basis, loan servicing rights are evaluated for impairment based on the fair value of the rights as compared to carrying amount. If the carrying amount of an individual tranche exceeds fair value, impairment is recorded on that tranche so that the servicing asset is carried at fair value. Fair value is determined at a tranche level based on a valuation model that calculates the present value of estimated future net servicing income. The valuation model utilizes assumptions that market participants would use in estimating future net servicing income and that can be validated against available market data (Level 2).

Impaired loans: At the time a loan is considered impaired, it is valued at the lower of cost or fair value. Impaired loans carried at fair value generally receive specific allocations of the ALLL. For collateral dependent loans, fair value is commonly based on recent real estate appraisals. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the independent appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are usually significant and typically result in a Level 3 classification of the inputs for determining fair value. Non-real estate collateral may be valued using an appraisal, net book value per the borrower s financial statements, or aging reports, adjusted or discounted based on management s historical knowledge, changes in market conditions from the time of the valuation, and management s expertise and knowledge of the client and client s business, resulting in a Level 3 fair value classification. Impaired loans are evaluated on a quarterly basis for additional impairment and adjusted accordingly.

Foreclosed assets: 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. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the independent appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are usually significant and typically result in a Level 3 classification of the inputs for determining fair value.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands except per share data)

NOTE 6 FAIR VALUE (continued)

Assets and liabilities measured at fair value on a recurring basis, including financial assets and liabilities for which the Company has elected the fair value option, are summarized below:

	Fair Value Measurements at June 30, 2012 Using Significant Other Observable Inputs (Level 2)	
Financial Assets:		
Securities available for sale:		
Issued by U.S. government-sponsored entities and agencies:		
Mortgage-backed securities residential	$	1,755
Collateralized mortgage obligations		15,557
Total securities available for sale	$	17,312
Loans held for sale	$	1,573
Yield maintenance provisions (embedded derivatives)	$	1,055
Interest rate lock commitments	$	40
Financial Liabilities:		
Interest-rate swaps	$	1,055

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands except per share data)

NOTE 6 FAIR VALUE (continued)

	Fair Value Measurements at December 31, 2011 Using Significant Other Observable Inputs (Level 2)
Financial Assets:	
Securities available for sale:	
Issued by U.S. government-sponsored entities and agencies:	
Mortgage-backed securities residential	$ 1,673
Collateralized mortgage obligations	16,843
Total securities available for sale	$ 18,516
Loans held for sale	$ 1,210
Yield maintenance provisions (embedded derivatives)	$ 999
Interest rate lock commitments	$ 39
Financial Liabilities:	
Interest-rate swaps	$ 999

The Company had no assets or liabilities measured at fair value on a recurring basis that were measured using Level 1 or Level 3 inputs at June 30, 2012 or December 31, 2011.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands except per share data)

NOTE 6 FAIR VALUE (continued)

Assets and liabilities measured at fair value on a non-recurring basis are summarized below:

	Fair Value Measurements at June 30, 2012 Using	
	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Loan servicing rights	$ 1	
Impaired loans:		
Commercial		$ 132
Real Estate:		
Multi-family residential		3,943
Commercial:		
Non-owner occupied		1,882
Owner occupied		409
Land		162
Total impaired loans		$ 6,528
Foreclosed assets		
Real Estate:		
Single-family residential		$ 48
Commercial:		
Non-owner occupied		985
Land		1,209
Total foreclosed assets		$ 2,242

	Fair Value Measurements at December 31, 2011 Using	
	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Loan servicing rights	$ 9	
Impaired loans:		

Commercial	$	108
Real Estate:		
Multi-family residential		3,065
Commercial:		
Non-owner occupied		2,887
Owner occupied		516
Land		233
Total impaired loans	$	6,809
Foreclosed assets		
Real Estate:		
Commercial:		
Land	$	1,209
Total foreclosed assets	$	1,209

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CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands except per share data)

NOTE 6 FAIR VALUE (continued)

The Company had no assets or liabilities measured at fair value on a non-recurring basis that were measured using Level 1 inputs at June 30, 2012 or December 31, 2011.

Impaired loan servicing rights, which are carried at fair value, were $1, which was made up of the amortized cost of $2, net of a valuation allowance of $1 at June 30, 2012. At December 31, 2011, impaired loan servicing rights, which are carried at fair value, were $9, which was made up of the amortized cost of $11, net of a valuation allowance of $2. There was a $1 charge against earnings with respect to servicing rights for the three months ended June 30, 2012, and a $1 increase in earnings for the six months ended June 30, 2012. There was a $1 increase in earnings with respect to servicing rights for the three months ended June 30, 2011, and a $3 increase in earnings for the six months ended June 30, 2011.

Impaired loans carried at the fair value of the collateral for collateral dependent loans, had an unpaid principal balance of $8,836, and a fair value of $6,528, with no valuation allowance at June 30, 2012. Impaired collateral dependent loans were written down to the fair value of collateral during the three and