BankFinancial CORP
Form 10-K
March 09, 2011

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-K

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

For the fiscal year ended December 31, 2010

or

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

For transition period from to

Commission File Number 0-51331

BANKFINANCIAL CORPORATION

(Exact Name of Registrant as Specified in Charter)

Maryland	**75-3199276**
(State or Other Jurisdiction of Incorporation)	**(I.R.S. Employer Identification No.)**
15W060 North Frontage Road, Burr Ridge, Illinois	**60527**
(Address of Principal Executive Offices)	**(Zip Code)**

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

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class:	**Name of Each Exchange on Which Registered:**
Common Stock, par value $0.01 per share	**The NASDAQ Stock Market LLC**

Securities registered pursuant to Section 12(g) of the Act:

None

Indicate by check mark whether the issuer is a well-known seasoned issuer as defined in Rule 405 of the Securities Act. Yes ¨ No x.

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ¨ No x.

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

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

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

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

The aggregate market value of the registrant s outstanding voting common stock held by non-affiliates on June 30, 2010, determined using a per share closing price on that date of $8.31, as quoted on The Nasdaq Stock Market, was $165.6 million.

At March 7, 2011, there were 21,072,966 shares of common stock, $0.01 par value, outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

None

PART I

ITEM 1. BUSINESS

Forward Looking Statements

This Annual Report on Form 10-K contains, and other periodic and current reports and press releases of BankFinancial Corporation may contain, forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, that involve significant risks and uncertainties. We intend such forward-looking statements to be covered by the safe harbor provisions for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995, and are including this statement for the purpose of invoking these safe harbor provisions. Forward-looking statements are based on certain assumptions or describe our future plans, strategies and expectations, and are generally identifiable by use of the words believe, expect, intend, anticipate, estimate, project, plan, or similar expressions. Ou predict results or the actual effect of plans or strategies is inherently uncertain, and actual results or effects may differ from those predicted. Factors that could have a material adverse effect on operations and could affect management s outlook or our future prospects include, but are not limited to: higher than expected overhead, infrastructure and compliance costs, changes in market interest rates, changes in the yield curve, balance sheet shrinkage or less than anticipated balance sheet growth, lack of demand for loan products, illiquidity and changes in financial markets, including the market for mortgage backed securities and other debt obligations, declining demand for real estate and real estate valuations, increasing unemployment levels, deposit flows, pricing, underwriting and other forms of competition, adverse federal or state legislative or regulatory developments, monetary and fiscal policies of the U.S. Government, including policies of the U.S. Treasury and Federal Reserve Board, adverse economic conditions that could result in increased delinquencies in our loan portfolio or a decline in the value of our investment securities and the collateral for our loans, the quality or composition of our loan or investment portfolios, demand for financial services and multi-family, commercial and residential real estate loans in our market areas, the possible dilutive effect of potential acquisitions or de novo branches, if any, changes in accounting principles, policies and guidelines, increased costs of federal deposit insurance, our failure to integrate an acquired institution successfully or achieve expected synergies and cost savings, and future adverse developments concerning the Federal Home Loan Bank of Chicago. These risks and uncertainties, as well as the Risk Factors set forth in Item 1A below, should be considered in evaluating forward-looking statements and undue reliance should not be placed on such statements. We do not undertake any obligation to update any forward-looking statement in the future, or to reflect circumstances and events that occur after the date on which the forward-looking statement was made.

BankFinancial Corporation

BankFinancial Corporation, a Maryland corporation headquartered in Burr Ridge, Illinois (the Company), became the owner of all of the issued and outstanding capital stock of BankFinancial, F.S.B. (the Bank) on June 23, 2005, when we consummated a plan of conversion and reorganization that the Bank and its predecessor holding companies, BankFinancial MHC, Inc. and BankFinancial Corporation, a federal corporation, adopted on August 25, 2004. BankFinancial Corporation, the Maryland corporation, was organized in 2004 to facilitate the mutual-to-stock conversion and to become the holding company for the Bank upon its completion.

As part of the mutual-to-stock conversion, BankFinancial Corporation, the Maryland corporation, sold 24,466,250 shares of common stock in a subscription offering for $10.00 per share. The separate corporate existences of BankFinancial MHC and BankFinancial Corporation, the federal corporation, ceased upon the completion of the mutual-to-stock conversion. For a further discussion of the mutual-to-stock conversion, see our Prospectus as filed on April 29, 2005 with the Securities and Exchange Commission (SEC) pursuant to Rule 424(b)(3) of the Rules and Regulations of the Securities Act of 1933 (File Number 333-119217).

We manage our operations as one unit, and thus do not have separate operating segments. Our chief operating decision-makers use consolidated results to make operating and strategic decisions.

BankFinancial, F.S.B.

The Bank is a full-service, community-oriented federal savings bank principally engaged in the business of commercial, family and personal banking, and offers our customers a broad range of loan, deposit, and other financial products and services through 18 full-service banking offices and three Express Branch facilities located in Cook, DuPage, Lake and Will Counties, Illinois, and through our Internet Branch, www.bankfinancial.com.

The Bank s primary business is making loans and accepting deposits. The Bank also offers our customers a variety of financial products and services that are related or ancillary to loans and deposits, including cash management, funds transfers, bill payment and other online banking transactions, automated teller machines, safe deposit boxes, wealth management, and general insurance agency services.

The Bank s primary lending area consists of the counties where our branch offices are located, and contiguous counties in the State of Illinois. We derive the most significant portion of our revenues from these geographic areas. Through our Wholesale Commercial Lending and National Commercial Leasing Departments, we also engage in multi-family lending activities in selected metropolitan areas outside our primary lending area and in commercial leasing activities on a nationwide basis. The Bank s primary market for deposits is concentrated around the areas where our full-service banking offices and Express Branch facilities are located.

Lending Activities

Our loan portfolio consists primarily of investment and business loans (multi-family, nonresidential real estate, commercial, construction and land loans, and commercial leases), which represented 75.9% of our total loan portfolio at December 31, 2010. At December 31, 2010, $296.9 million, or 27.7%, of our total loan portfolio consisted of multi-family mortgage loans; $282.0 million, or 26.3%, of our total loan portfolio consisted of nonresidential real estate loans; $64.7 million, or 6.0%, of our total loan portfolio consisted of commercial loans; $151.1 million, or 14.1%, of our total loan portfolio consisted of commercial leases; and $18.4 million, or 1.7%, of our total loan portfolio consisted of construction and land loans. $256.3 million, or 23.9%, of our total loan portfolio consisted of one-to-four family residential mortgage loans (of which $76.0 million, or 7.1%, were loans to investors in non-owner-occupied single-family homes), including home equity loans and lines of credit.

Deposit Activities

Our deposit accounts consist principally of savings accounts, NOW accounts, checking accounts, money market accounts, certificates of deposit, and IRAs and other qualified plan accounts. We provide commercial checking accounts and related services such as cash management. We also provide low-cost checking account services. We rely on our favorable locations, customer service, competitive pricing, our Internet Branch and related deposit services such as cash management to attract and retain deposit accounts.

At December 31, 2010, our deposits totaled $1.235 billion. Interest-bearing deposits totaled $1.123 billion and noninterest-bearing demand deposits totaled $112.5 million, which included $6.0 million in internal checking accounts such as bank cashier checks and money orders. Savings, money market and NOW account deposits totaled $742.8 million, and certificates of deposit totaled $380.1 million, of which $271.2 million had maturities of one year or less.

Related Products and Services

The Bank s Wealth Management Group provides investment, financial planning and other wealth management services to our customers through arrangements with a third-party broker-dealer. The Bank s wholly-owned subsidiary, Financial Assurance Services, Inc. (Financial Assurance), sells life insurance, fixed annuities, property and casualty insurance and other insurance products on an agency basis. Financial Assurance was engaged in the sale of title insurance on an agency basis until March 15, 2008. On that date, Financial Assurance completed the sale of its title insurance agency business to a newly formed, third-party title insurance agency. The sale of the title insurance agency business did not affect Financial Assurance s other insurance businesses. During the year ended December 31, 2010, Financial Assurance reported net income of $209,000. At December 31, 2010, Financial Assurance had four full-time employees. The Bank s other wholly-owned subsidiary, BF Asset Recovery Corporation, is in the business of holding title to and selling certain Bank-owned real estate, and reported a loss of $2.2 million for the year ended December 31, 2010.

Website and Stockholder Information

The website for the Company and the Bank is www.bankfinancial.com. Information on this website does not constitute part of this Annual Report on Form 10-K.

The Company makes available, free of charge, its Annual Report on Form 10-K, its quarterly reports on Quarterly Report on Form 10-Q, its current reports on Form 8-K and amendments to such reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended (Exchange Act), as soon as reasonably practicable after such forms are filed with or furnished to the SEC. Copies of these documents are available to stockholders at BankFinancial s web site, www.bankfinancial.com, under Stockholder Information, and at the SEC s web site, www.sec.gov.

Competition

We face significant competition in both originating loans and attracting deposits. The Chicago metropolitan area and some other areas in which we operate have a high concentration of financial institutions, many of which are significantly larger institutions that have greater financial resources than we have, and many of which are our competitors to varying degrees. Our competition for loans and leases comes principally from commercial banks, savings banks, mortgage banking companies, credit unions, leasing companies, insurance companies, real estate conduits and other companies that provide financial services to businesses and individuals. Our most direct competition for deposits has historically come from commercial banks, savings banks and credit unions. We face additional competition for deposits from online financial institutions and non-depository competitors such as the mutual fund industry, securities and brokerage firms and insurance companies.

We seek to meet this competition by emphasizing personalized service and efficient decision-making tailored to individual needs. In addition, we reward long-standing relationships with preferred rates and terms on deposit products based on existing and prospective lending business. We do not rely on any individual, group or entity for a material portion of our loans or our deposits.

Employees

At December 31, 2010, we had 310 full-time employees and 27 part-time employees. The employees are not represented by a collective bargaining unit and we consider our working relationship with our employees to be good.

Supervision and Regulation

General

As a federally chartered savings bank, the Bank is currently regulated and supervised primarily by the Office of Thrift Supervision (OTS). The Bank is also subject to regulation by the Federal Deposit Insurance Corporation (FDIC) in more limited circumstances because the Bank s deposits are insured by the FDIC. This regulatory and supervisory structure establishes a comprehensive framework of activities in which a financial institution may engage, and is intended primarily for the protection of the FDIC s deposit insurance funds, depositors and the banking system. Under this system of federal regulation, financial institutions are periodically examined to ensure that they satisfy applicable standards with respect to their capital adequacy, assets, management, earnings, liquidity and sensitivity to market interest rates. After completing an examination, the OTS critiques the financial institution s operations in a report of examination and assigns it a rating (known as an institution s CAMELS rating). Under federal law, an institution may not disclose its CAMELS rating to the public.

The Bank is a member of, and owns stock in, the Federal Home Loan Bank of Chicago (FHLBC), which is one of the 12 regional banks in the Federal Home Loan Bank System. The Bank also is regulated to a lesser extent by the Board of Governors of the Federal Reserve System with regard to reserves it must maintain against deposits and other matters. The OTS examines the Bank and prepares reports for the consideration of its Board of Directors on any identified operating deficiencies. The Bank s relationship with its depositors and borrowers also is regulated in some respects by both federal and state laws, especially in matters concerning the ownership of deposit accounts, and the form and content of the Bank s consumer loan documents.

The Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), which was signed by the President on July 21, 2010, provides for the transfer of the authority for regulating and supervising federal savings banks from the OTS to the Office of the Comptroller of the Currency (OCC), and the authority for regulating and supervising savings and loan holding companies and their non-depository subsidiaries from the OTS to the Board of Governors of the Federal Reserve Board (FRB). The transfer is currently scheduled to occur July 21, 2011. The Dodd-Frank Act also creates a new federal agency, the Consumer Financial Protection Bureau (CFPB), as an independent bureau of the Federal Reserve Board, to conduct rule-making, supervision, and enforcement of federal consumer financial protection and fair lending laws and regulations. The CFPB will have examination and primary enforcement authority in connection with these laws and regulations for depository institutions with total assets of more than $10 billion. Depository institutions with $10 billion or less in total assets will continue to be examined for compliance with these laws and regulations by their primary federal regulators, and will remain subject to their enforcement authority. Because of these changes, the OCC will become the primary federal regulator of the Bank and the FRB will become the primary federal regulator of the Company on the transfer date. The Bank will not be subject to the examination or the primary enforcement authority of the CFPB.

There can be no assurance that laws, rules and regulations will not change in the future, which could make compliance more difficult or expensive or otherwise adversely affect our business, financial condition, results of operations or prospects. Any change in these laws or regulations, or in regulatory policy, whether by the OCC, FDIC, the FRB, the OTS, the CFPB or Congress, could have a material adverse impact on the Company, the Bank and their respective operations.

Federal Banking Regulation

Business Activities. As a federal savings bank, the Bank derives its lending and investment powers from the Home Owners Loan Act, as amended, and the regulations of the OTS. Under these laws and regulations, the Bank may invest in mortgage loans secured by residential and nonresidential real estate, commercial business and consumer loans, certain types of securities and certain other loans and assets. Specifically, the Bank may originate, invest in, sell, or purchase unlimited loans on the security of residential real estate, while loans on nonresidential real property generally may not, on a combined basis, exceed 400% of the Bank s total capital. In addition, secured and unsecured commercial loans and certain types of commercial personal property leases may not exceed 20% of the Bank s assets; however, amounts in excess of 10% of assets may only be used for small business loans. Further, the Bank may generally invest up to 35% of its assets in consumer loans, corporate debt securities and commercial paper on a combined basis, and up to the greater of its capital or 5% of its assets in unsecured construction loans. The Bank may invest up to 10% of its assets in tangible personal property, for rental or sale. Certain leases on tangible personal property are not aggregated with commercial or consumer loans for the purposes of determining compliance with the limitations set forth for those investment categories. The Bank also may establish subsidiaries that may engage in activities not otherwise permissible for the Bank directly, including real estate investment and insurance agency activities. A violation of the lending and investment limitations may be subject to the same enforcement mechanisms of the primary federal regulator as other violations of a law or regulation.

Capital Requirements. The regulations of the OTS require federal savings banks to meet three minimum capital standards: a ratio of tangible capital to adjusted total assets of 1.5%; a ratio of Tier 1 (core) capital to adjusted total assets of 4.0% (3% for institutions receiving the highest rating on the CAMELS rating system); and a ratio of total capital to total risk-adjusted assets of 8.0%. The prompt corrective action standards discussed below, in effect, establish a minimum 2% tangible capital standard.

The risk-based capital standard for federal savings banks requires the maintenance of Tier 1, or core capital, and total capital (which is defined as core capital and supplementary capital) to risk-weighted assets of at least 4% and 8%, respectively. In determining the amount of risk-weighted assets, all assets, including certain off-balance sheet assets, are multiplied by a risk-weight factor of 0% to 100%, assigned by the OTS capital regulation based on the risks inherent in the type of asset. Core capital is defined as common stockholders equity (including retained earnings), certain noncumulative perpetual preferred stock and related surplus and minority interests in equity accounts of consolidated subsidiaries, less intangibles other than certain mortgage servicing rights and credit card relationships. The components of supplementary capital currently include cumulative perpetual preferred stock, long-term preferred stock, mandatory convertible securities, subordinated debt and intermediate-term preferred stock, allowance for loan and lease losses up to a maximum of 1.25% of risk-weighted assets and up to 45% of net unrealized gains on available-for-sale equity securities with readily determinable fair market values. Overall, the amount of supplementary capital included as part of total capital cannot exceed 100% of core capital.

At December 31, 2010, the Bank s capital exceeded all applicable regulatory requirements.

Loans-to-One-Borrower. A federal savings bank generally may not make a loan or extend credit to a single or related group of borrowers in excess of 15% of unimpaired capital and surplus. An additional amount may be loaned, equal to 10% of unimpaired capital and surplus, if the loan is secured by readily marketable collateral, which generally does not include real estate. As of December 31, 2010, the Bank was in compliance with the loans-to-one-borrower limitations.

Qualified Thrift Lender Test. As a federal savings bank, the Bank is subject to a qualified thrift lender, or QTL, test. Under the QTL test, the Bank must maintain at least 65% of its portfolio assets in qualified thrift investments in at least nine months of the most recent 12-month period. Portfolio assets generally means the total assets of a savings institution, less the sum of specified liquid assets up to 20% of total assets, goodwill and other intangible assets, and the value of property used in the conduct of the federal savings bank s business.

Qualified thrift investments include various types of loans made for residential and housing purposes, investments related to those purposes, including certain mortgage-backed and related securities, and loans for personal, family, household and certain other purposes up to a limit of 20% of portfolio assets. Qualified thrift investments also include 100% of an institution s credit card loans, education loans and small business loans. The Bank also may satisfy the QTL test by qualifying as a domestic building and loan association as defined in the Internal Revenue Code of 1986. At December 31, 2010, the Bank maintained approximately 76.95% of its portfolio assets in qualified thrift investments, and as of that date, satisfied the QTL test. A federal savings bank that fails the QTL test must operate under specified restrictions, including limits on growth, branching, new investment and dividends. As a result of the Dodd-Frank Act, noncompliance with the QTL test is subject to regulatory enforcement action as a violation of law.

Capital Distributions. The regulations of the OTS govern capital distributions by a federal savings bank, which include cash dividends, stock repurchases and other transactions charged to the institution s capital account. A federal savings bank must file an application for approval of a capital distribution if:

- the total capital distributions for the applicable calendar year exceed the sum of the institution s net income for that year to date plus the federal savings bank s retained net income for the preceding two years;
- the institution would not be at least adequately capitalized following the distribution;
- the distribution would violate any applicable statute, regulation, agreement or OTS-imposed condition; or
- the institution is not eligible for expedited treatment of its filings.

Even if an application is not otherwise required, every federal savings bank that is a subsidiary of a holding company must still file a notice with the OTS at least 30 days before the board of directors declares a dividend or approves a capital distribution. At December 31, 2010, the Bank would be required to file an application for approval of a capital distribution to the Company.

The OTS may disapprove a notice or application if:

- the federal savings bank would be undercapitalized following the distribution;
- the proposed capital distribution raises safety and soundness concerns; or
- the capital distribution would violate a prohibition contained in any statute, regulation or agreement.

Liquidity. A federal savings bank is required to maintain a sufficient amount of liquid assets to ensure its safe and sound operation.

Community Reinvestment Act and Fair Lending Laws. All federal savings banks have a responsibility under the Community Reinvestment Act (CRA) and related regulations of the OTS to help meet the credit needs of their communities, including low and moderate income neighborhoods. In connection with its examination of a federal savings bank, the OTS is required to evaluate and rate the federal savings bank s record of compliance with the CRA. In addition, the Equal Credit Opportunity Act and the Fair Housing Act prohibit lenders from discriminating in their lending practices based on the characteristics specified in those statutes. A federal savings bank s failure to comply with the provisions of the CRA could, at a minimum, result in regulatory restrictions on its activities. The failure to comply with the Equal Credit Opportunity Act and the Fair Housing Act could result in enforcement actions by the OTS, as well as other federal regulatory agencies and the Department of Justice. The OTS has rated the Bank s CRA performance as Outstanding, the highest possible rating, in the CRA Performance Evaluations the OTS has completed on the Bank since 1999.

Privacy Standards. Financial institutions are subject to regulations implementing the privacy protection provisions of the Gramm-Leach-Bliley Act. These regulations require the Bank to disclose its privacy policy, including identifying with whom it shares nonpublic personal information to customers at the time of establishing the customer relationship and annually thereafter. In addition, the Bank is required to provide its customers with the ability to opt-out of or consent to having the Bank share their nonpublic personal information with unaffiliated third parties before it can disclose such information, subject to certain exceptions. The implementation of these regulations did not have a material adverse effect on the Bank. The Gramm-Leach-Bliley Act also allows each state to enact legislation that is more protective of consumers personal information.

The OTS and other federal banking agencies have adopted guidelines establishing standards for safeguarding customer information to implement certain provisions of the Gramm-Leach-Bliley Act. The guidelines describe the agencies expectations for the creation, implementation and maintenance of an information security program, which would include administrative, technical and physical safeguards appropriate to the size and complexity of a financial institution and the nature and scope of its activities. The standards set forth in the guidelines are intended to ensure the security and confidentiality of customer records and information, to protect against any anticipated threats or hazards to the security or integrity of such records, and to protect against unauthorized access to or use of such records or other information that could result in substantial harm or inconvenience to any customer. The Bank has implemented these guidelines, and such implementation has not had a material adverse effect on our operations.

Transactions with Related Parties. A federal savings bank s authority to engage in transactions with its affiliates is limited by OTS regulations and by Sections 23A and 23B of the Federal Reserve Act and its implementing regulation, Regulation W. The term affiliates for these purposes generally means any company that controls or is under common control with an insured depository institution, although subsidiaries of federal savings banks are generally not considered affiliates for the purposes of Sections 23A and 23B of the Federal Reserve Act. The Company is an affiliate of the Bank. In general, transactions with affiliates must be on terms that are as favorable to the federal savings bank as comparable transactions with non-affiliates. In addition, certain types of these transactions are restricted to an aggregate percentage of the federal savings bank s capital. Collateral in specified amounts must usually be provided by affiliates in order to receive loans from the federal savings bank. OTS regulations also prohibit a federal savings bank from lending to any of its affiliates that are engaged in activities that are not permissible for bank holding companies, and from purchasing the securities of any affiliate, other than a subsidiary.

The Bank s authority to extend credit to its directors, executive officers and 10% stockholders, as well as to entities controlled by such persons, is currently governed by the requirements of Sections 22(g) and 22(h) of the Federal Reserve Act and Regulation O of the Federal Reserve Board. Among other things, these provisions require that extensions of credit to insiders be made on terms that are substantially the same as, and follow credit underwriting procedures that are not less stringent than, those prevailing for comparable transactions with unaffiliated persons and that do not involve more than the normal risk of repayment or present other unfavorable features, and not exceed certain limitations on the amount of credit extended to such persons, individually and in the aggregate, which limits are based, in part, on the amount of the Bank s capital. In addition, extensions of credit in excess of certain limits must receive the prior approval of the Bank s Board of Directors.

Enforcement. The OTS has primary enforcement responsibility over federal savings banks, and has the authority to bring enforcement action against the Bank and all institution-affiliated parties, including stockholders, attorneys, appraisers and accountants who knowingly or recklessly participate in wrongful action likely to have an adverse effect on an insured institution. Formal enforcement action may range from the issuance of a capital directive or cease and desist order to the removal of officers and/or directors, receivership, conservatorship or the termination of deposit insurance. Civil monetary penalties cover a wide range of violations and actions, and range up to $25,000 per day, unless a finding of reckless disregard is made, in which case penalties may be as high as $1 million per day. The FDIC also has the authority to recommend to the Director of the OTS that an enforcement action be taken with respect to a particular savings institution. If action is not taken by the Director, the FDIC has authority to take action under specified circumstances. The OTS enforcement authority over federal savings banks is currently scheduled to be transferred to the OCC on July 21, 2011 pursuant to the Dodd-Frank Act.

Standards for Safety and Soundness. Federal law requires each federal banking agency to prescribe certain standards for all insured depository institutions. These standards relate to, among other things, internal controls, information systems and audit systems, loan documentation, credit underwriting, interest rate risk exposure, asset growth, compensation and other operational and managerial standards as the agency deems appropriate. The federal banking agencies adopted Interagency Guidelines Prescribing Standards for Safety and Soundness to implement the safety and soundness standards required under federal law. The guidelines set forth the safety and soundness standards that the federal banking agencies use to identify and address problems at insured depository institutions before capital becomes impaired. The guidelines address internal controls and information systems, internal audit systems, credit underwriting, loan documentation, interest rate risk exposure, asset growth, compensation, fees and benefits. If the appropriate federal banking agency determines that an institution fails to meet any standard prescribed by the guidelines, the agency may require the institution to submit to the agency an acceptable plan to achieve compliance with the standard.

Prompt Corrective Action Regulations. Under the prompt corrective action regulations, the OTS is required and authorized to take supervisory actions against undercapitalized federal savings banks. For this purpose, a federal savings bank is placed in one of the following five categories based on the federal savings bank s capital:

well-capitalized (at least 5% leverage capital, 6% tier 1 risk-based capital and 10% total risk-based capital);

adequately capitalized (at least 4% leverage capital, 4% tier 1 risk-based capital and 8% total risk-based capital);

undercapitalized (less than 3% leverage capital, 4% tier 1 risk-based capital or 8% total risk-based capital);

significantly undercapitalized (less than 3% leverage capital, 3% tier 1 risk-based capital or 6% total risk-based capital); and

critically undercapitalized (less than 2% tangible capital).

Generally, the banking regulator is required to appoint a receiver or conservator for a federal savings bank that is critically undercapitalized. The regulation also provides that a capital restoration plan must be filed with the OTS within 45 days of the date a bank receives notice that it is undercapitalized, significantly undercapitalized or critically undercapitalized. In addition, numerous mandatory supervisory actions become immediately applicable to the federal savings bank, including, but not limited to, restrictions on growth, investment activities, capital distributions and affiliate transactions. The OTS may also take any one of a number of discretionary supervisory actions against undercapitalized federal savings banks, including the issuance of a capital directive and the replacement of senior executive officers and directors.

At December 31, 2010, the Bank met the criteria for being considered well-capitalized.

Interest on Deposits. Federal laws and regulations currently prohibits depository institutions from paying interest on commercial checking accounts. The Dodd-Frank Act authorizes the payment of interest on commercial checking accounts effective July 21, 2011.

Insurance of Deposit Accounts. The Bank s deposits are insured up to applicable limits by the Deposit Insurance Fund of the FDIC. Under the FDIC s risk-based assessment system, insured institutions are assigned to one of four risk categories based on supervisory evaluations, regulatory capital levels and certain other factors, with less risky institutions paying lower assessments. An institution s assessment rate depends upon the category to which it is assigned, subject to certain adjustments specified by the FDIC s. Assessment rates currently range from seven to 77.5 basis points of assessable deposits. The FDIC may adjust the scale uniformly, except that no adjustment can deviate by more than three basis points from the base scale without notice and comment. No institution may pay a dividend if it is in default of the federal deposit insurance assessment.

The Dodd-Frank Act requires the FDIC to revise its procedures to base its assessments upon total assets less tangible equity instead of on deposits. The FDIC recently issued a final rule that will implement that change beginning the second quarter of 2011.

The FDIC imposed on all insured institutions a special emergency assessment of five basis points of total assets minus Tier 1 capital (as of June 30, 2009), capped at ten basis points of an institution s deposit assessment base, in order to cover losses to the Deposit Insurance Fund. That special assessment was collected on September 30, 2009.

The FDIC provided for similar assessment authority during the final two quarters of 2009, if deemed necessary. In lieu of further special assessments, the FDIC required insured institutions to prepay estimated quarterly risk-based assessments for the fourth quarter of 2009 through the fourth quarter of 2012. The estimated assessments which included an assumed annual base increase of 5%, were recorded as a prepaid expense asset as of December 31, 2009, and each quarter thereafter, a charge to earnings is recorded for each regulator assessment with an offsetting credit to the prepaid asset.

The Dodd-Frank Act increased the minimum target Deposit Insurance Fund ratio from 1.15% of estimated insured deposits to 1.35% of estimated insured deposits. The FDIC must seek to achieve the 1.35% ratio by September 30, 2020. Insured institutions with assets of $10 billion or more are supposed to fund the increase. The Dodd-Frank Act eliminated the 1.5% maximum fund ratio, instead leaving the ratio to the discretion of the FDIC. The FDIC recently exercised that discretion by establishing a long-range fund ratio of 2%.

The FDIC has authority to increase insurance assessments. A significant increase in insurance premiums would be likely have an adverse effect on the operating expenses and results of operations of the Bank. The Bank cannot predict what the insurance assessment rates will be in the future.

An insured institution s deposit insurance may be terminated by the FDIC upon a finding that the institution has engaged in unsafe or unsound practices, is in an unsafe or unsound condition to continue operations or has violated any applicable law, regulation, rule, order or regulatory condition imposed in writing. The management of the Bank does not know of any practice, condition or violation that might lead to termination of deposit insurance.

In addition to the FDIC assessments, the Financing Corporation (FICO) is authorized to impose and collect, with the approval of the FDIC, assessments for anticipated payments, issuance costs and custodial fees on bonds issued by the FICO in the 1980 s to recapitalize the former Federal Savings and Loan Insurance Corporation. The bonds issued by the FICO are due to mature in 2017 through 2019. For the quarter ended December 31, 2010, the annualized FICO assessment was equal to 1.04 basis points for each $100 in domestic deposits maintained at an insured institution.

Temporary Liquidity Guarantee Program. On October 14, 2008, the FDIC announced the Temporary Liquidity Guarantee Program. This program has two components The Debt Guarantee Program and the Transaction Account Guarantee Program. The Debt Guarantee Program guarantees newly issued senior unsecured debt of a participating organization, up to certain limits established for each institution, issued between October 14, 2008 and June 30, 2009, later extended to October 31, 2010. The Bank and the Company opted not to participate in the Debt Guarantee Program.

The Transaction Account Guarantee Program provides, for a fee, full federal deposit insurance coverage for non-interest bearing transaction deposit accounts, regardless of dollar amount, until June 30, 2010, later extended to December 31, 2010. The Bank participated in the Transaction Account Guarantee Program. The Dodd-Frank Act extended unlimited federal deposit insurance coverage for certain non-interest bearing transaction accounts until December 31, 2012, without opportunity for opt out.

U.S. Treasury s Troubled Asset Relief Program Capital Purchase Program. The Emergency Economic Stabilization Act of 2008 (EESA) provided the U.S. Secretary of the Treasury with broad authority to implement certain actions to help restore stability and liquidity to U.S. markets. One of the provisions resulting from the legislation is the Troubled Asset Relief Program Capital Purchase Program (TARP), which provides direct equity investment by the U.S. Treasury Department in qualified financial institutions. The TARP program was voluntary. The Company did not participate in TARP.

Prohibitions Against Tying Arrangements. Federal savings banks are prohibited, subject to some exceptions, from extending credit to or offering any other service, or fixing or varying the consideration for such extension of credit or service, on the condition that the customer obtain some additional service from the institution or its affiliates or not obtain services of a competitor of the institution.

Federal Home Loan Bank System. The Bank is a member of the Federal Home Loan Bank System, which consists of 12 regional Federal Home Loan Banks. The Federal Home Loan Bank System provides a central credit facility primarily for member institutions. As a member of the FHLBC, the Bank is required to acquire and hold shares of capital stock in the FHLBC in an amount at least equal to 1% of the aggregate principal amount of its unpaid residential mortgage loans and similar obligations at the beginning of each year, or 1/20 of its borrowings from the FHLBC, whichever is greater. As of December 31, 2010, the Bank was in compliance with this requirement.

The USA PATRIOT Act and the Bank Secrecy Act

The USA PATRIOT Act and the Bank Secrecy Act require financial institutions to develop programs to detect and report money-laundering and terrorist activities, as well as suspicious activities. The USA PATRIOT Act also gives the federal government powers to address terrorist threats through enhanced domestic security measures, expanded surveillance powers, increased information sharing and broadened anti-money laundering requirements. The federal banking agencies are required to take into consideration the effectiveness of controls designed to combat money-laundering activities in determining whether to approve a merger or other acquisition application of a member institution. Accordingly, if we engage in a merger or other acquisition, our controls designed to combat money laundering would be considered as part of the application process. In addition, non-compliance with these laws and regulations could result in fines, penalties and other enforcement measures. We have developed policies and continue to augment procedures and systems designed to comply with these laws and regulations.

Federal Reserve System

The FRB s regulations require federal savings banks to maintain noninterest-earning reserves against their transaction accounts, such as negotiable order of withdrawal and regular checking accounts. At December 31, 2010, the Bank was in compliance with these reserve requirements. The balances maintained to meet the reserve requirements imposed by the FRB may be used to satisfy liquidity requirements imposed by the OTS.

Holding Company Regulation

The Company is a unitary savings and loan holding company, and is currently subject to regulation and supervision by the OTS. The OTS also currently has enforcement authority over the Company and its non-savings institution subsidiaries. Among other things, this authority permits the OTS to restrict or prohibit activities that are determined to be a risk to the Bank. The Dodd-Frank Act provides for the transfer of the authority for supervising and regulating savings and loan holding companies and their non-depository subsidiaries from the OTS to the FRB. The transfer is presently scheduled to occur on July 21, 2011.

The Company s activities are limited to the activities permissible for financial holding companies or for multiple savings and loan holding companies. A financial holding company may engage in activities that are financial in nature, including underwriting equity securities and insurance, incidental to financial activities or complementary to a financial activity. A multiple savings and loan holding company is generally limited to activities permissible for bank holding companies under Section 4(c) (8) of the Bank Holding Company Act, subject to the prior approval of the OTS, and certain additional activities authorized by OTS regulations.

Federal law prohibits a savings and loan holding company, directly or indirectly, or through one or more subsidiaries, from acquiring control of another savings institution or holding company thereof, without prior written approval of the OTS. It also prohibits the acquisition or retention of, with specified exceptions, more than 5% of the equity securities of a company engaged in activities that are not closely related to banking or financial in nature or acquiring or retaining control of an institution that is not federally insured. In evaluating applications by holding companies to acquire savings institutions, the OTS must consider the financial and managerial resources and future prospects of the savings institution, the effect of the acquisition on the risk to the insurance fund, the convenience and needs of the community and competitive factors.

Capital. Savings and loan holding companies are not currently subject to specific regulatory capital requirements. The Dodd-Frank Act, however, requires the FRB to promulgate consolidated capital requirements for depository institution holding companies that are no less stringent, both quantitatively and in terms of components of capital, than those applicable to their subsidiary depository institutions. As is currently the case with bank holding companies, instruments such as cumulative preferred stock and trust-preferred securities will no longer be includable as Tier 1 capital. However, instruments issued by May 19, 2010 will be grandfathered for holding companies with assets of $15 billion or less. There is a five-year transition period from the July 21, 2010 effective date of the Dodd-Frank Act before the capital requirements will apply to savings and loan holding companies.

Source of Strength Doctrine. The source of strength doctrine requires bank holding companies to provide financial assistance to their subsidiary depository institutions in the event the subsidiary depository institution experiences financial distress. The Dodd-Frank Act extends the source of strength doctrine to savings and loan holding companies. The applicable regulatory agencies must issue regulations requiring that all bank holding companies and savings and loan holding companies serve as a source of strength to their subsidiary depository institutions by providing capital, liquidity and other support in times of financial distress.

Sarbanes-Oxley Act of 2002

The Sarbanes-Oxley Act of 2002 was enacted in response to public concerns regarding corporate accountability in connection with certain accounting scandals. The stated goals of the Sarbanes-Oxley Act are to increase corporate responsibility, to provide for enhanced penalties for accounting and auditing improprieties at publicly traded companies, and to protect investors by improving the accuracy and reliability of corporate disclosures pursuant to the securities laws. The Sarbanes-Oxley Act generally applies to all companies that file or are required to file periodic reports with the Securities and Exchange Commission, under the Exchange Act.

The Sarbanes-Oxley Act includes specific additional disclosure requirements, requires the Securities and Exchange Commission and national securities exchanges to adopt extensive additional disclosure, corporate governance and other related rules, and mandates further studies of certain issues by the Securities and Exchange Commission.

Federal Securities Laws

The Company s common stock is registered with the Securities and Exchange Commission under the Exchange Act. The Company is subject to the information, proxy solicitation, insider trading restrictions and other requirements of the Exchange Act.

Taxation

Federal Taxation. The Company and the Bank are subject to federal income taxation in the same general manner as other corporations, with some exceptions discussed below. The following discussion of federal taxation is intended only to summarize material federal income tax matters and is not a comprehensive description of the tax rules applicable to the Company and the Bank.

Method of Accounting. For federal income tax purposes, the Company currently reports its income and expenses on the accrual method of accounting and uses a tax year ending December 31 for filing its consolidated federal income tax returns.

Bad Debt Reserves. The Small Business Protection Act of 1996 eliminated the use of the reserve method of accounting for bad debt reserves by federal savings banks, effective for taxable years beginning after 1995. Prior to the enactment of this law, the Bank was permitted to establish a reserve for bad debts for tax purposes and to make annual additions to the reserve. These additions could, within specified formula limits, be deducted in arriving at the Bank s taxable income. Because of the Small Business Protection Act of 1996, the Bank must use the specific charge-off method in computing its bad debt deduction for tax purposes.

Taxable Distributions and Recapture. Prior to the Small Business Protection Act of 1996, bad debt reserves created prior to 1988 were subject to recapture into taxable income if the Bank failed to meet certain thrift asset and definition tests. The Small Business Protection Act of 1996 eliminated these thrift-related recapture rules. However, under current law, pre-1988 reserves remain subject to tax recapture should the Bank make certain distributions from its tax bad debt reserve or cease to maintain a financial institution charter. At December 31, 2010, the Bank s total federal pre-1988 reserve was $14.9 million. This reserve reflects the cumulative effects of federal tax deductions by the Bank for which no federal income tax provision has been made.

Alternative Minimum Tax. The Internal Revenue Code of 1986, as amended, imposes an alternative minimum tax at a rate of 20% on a base of regular taxable income plus certain tax preferences, referred to as alternative minimum taxable income. The alternative minimum tax is payable to the extent alternative minimum taxable income is in excess of an exemption amount. Net operating losses can, in general, offset no more than 90% of alternative minimum taxable income unless resulting from a loss carryback from 2008 or 2009 pursuant to the special provisions of the Worker, Homeownership & Business Assistance Act of 2009.

Net Loss Carryovers. A financial institution may carry back net operating losses to the preceding two taxable years (up to five years for losses incurred in 2008 or 2009 pursuant to the special provisions of the Worker, Homeownership & Business Assistance Act of 2009) and forward to the succeeding 20 taxable years. At December 31, 2010, the Company had a federal net operating loss carryforward of $5.9 million that will begin to expire in 2029. At December 31, 2010, the Company had a state net operating loss carryforward for the State of Illinois of $32.0 million that will expire in 2025. The net operating losses have resulted in the recording of deferred taxes.

Corporate Dividends. The Company may exclude from its income 100% of the dividends it receives from the Bank as a member of the same affiliated group of corporations.

State and Local Taxation. The Company pays income tax to the State of Illinois. As a Maryland business corporation, the Company is required to file annual returns and pay annual fees to the State of Maryland, but these fees are not material in amount. At December 31, 2010, the Company had a state net operating loss for the State of Illinois of $32.0 million, which will expire in 2025. Beginning in 2010 and 2009, the Company and the Bank became subject to income taxes in the States of Colorado and New Jersey, respectively, due to the physical presence of regional National Commercial Leasing bankers in these jurisdictions.

Deferred Income Taxes. The Company evaluates deferred taxes for recoverability using an approach that considers the relative impact of negative and positive evidence, including historical financial performance, projections of future taxable income, future reversals of existing taxable temporary differences, tax-planning strategies and any available carryback capacity. In evaluating the need for a valuation allowance, the Company estimates future taxable income based on management-approved business plans and ongoing tax planning. Only those tax planning strategies that are both prudent and feasible, and which management has the ability and intent to implement, may be incorporated into the analysis and assessment.

The Company s historical financial performance includes a cumulative loss over a three-year period consisting of the current year and the previous two years. The most significant component of the cumulative loss was impairment losses that the Company recorded on Freddie Mac preferred stocks that it previously held in its investment portfolio. The Company sold these securities in 2009 so the impairment losses will not recur. The most significant component of the Company s net loss in 2010 was the combined effects of specific valuation allowances on classified loans and write-downs on other real estate owned (OREO), together with the expenses incurred to resolve collection litigation and manage the related collateral. In 2011, we expect to further deploy our excess liquidity to generate additional loan-related interest income and we expect the negative effects from classified loans and assets to diminish over time. In addition, we expect further pre-tax net income contributions from our acquisition of Downers Grove National Bank (see Note 13 Subsequent Events of the Consolidated Financial Statements). After taking these factors into account, we believe it more likely than not that the Company will return to profitability during 2011 and maintain profitability in subsequent years such that it will fully realize the benefit of the deferred tax assets recorded at December 31, 2010. Should the Company not return to profitability in 2011 or in subsequent years, it may become necessary to record a valuation allowance for all or a portion of the deferred tax asset.

ITEM 1A. RISK FACTORS

The risks set forth below may adversely affect our business, financial condition and operating results. In addition to the risks set forth below and the other risks described in Item 1, Business, Forward Looking Statements, and Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations, there may also be additional risks and uncertainties that are not currently known to us or that we currently deem to be immaterial that could materially and adversely affect our business, financial condition or operating results. As a result, past financial performance may not be a reliable indicator of future performance, and historical trends should not be used to anticipate results or trends in future periods.

Current Economic Conditions Present Higher Risks to Our Loan Portfolio

At December 31, 2010, our loan portfolio included $296.9 million in multi-family mortgage loans, or 27.7% of total loans; $282.0 million in nonresidential real estate loans, or 26.3% of total loans; $151.1 million in commercial leases, or 14.1% of total loans; $64.7 million in commercial loans, or 6.0% of total loans; and $76.0 million in non owner occupied residential real estate loans, or 7.1% of total loans; $103.3 million in residential real estate loans, or 16.7% of total loans; and $18.4 million in construction and land loans, or 1.7% of total loans. Current economic conditions, including high unemployment rates, weakened consumer and business spending and materially declining real estate values, all present risks to our loan portfolio. Our historical loan underwriting standards presumed a reasonable range of economic and operating conditions for our borrowers and their underlying business or personal circumstances. The depth and speed of the decline in economic activity exceeded, and will continue to exceed, the financial and management capabilities of certain borrowers to meet their credit obligations. Furthermore, the decline in real estate values in all market segments not only diminishes an important source of repayment, but also diminishes the economic interest of borrowers in investing additional financial resources into their businesses or residences. Though the risk of a sudden and catastrophic event in financial markets appears to have receded, persistently weak economic growth in the U.S. and certain of its trading partners will continue to depress the operating results of certain commercial lessees. These factors and conditions and prudent loan portfolio management have also combined to reduce the overall level of acceptable credit exposures available in the market, resulting in lower loan portfolio balances and reduced interest income from the loan portfolio.

If Our Allowance for Loan Losses is Not Sufficient to Cover Actual Loan Losses, Our Earnings Could Decrease

In the event that our loan customers do not repay their loans according to their terms, and the collateral securing the repayment of these loans is insufficient to cover any remaining loan balance, we could experience significant loan losses or increase our provision for loan losses or both, which could have a material adverse effect on our operating results. At December 31, 2010, our allowance for loan losses was $22.2 million, representing 2.07% of total loans and 48.5% of nonperforming loans as of that date. In determining the amount of our allowance for loan losses, we rely on our loan quality reviews, our experience and our evaluation of economic conditions, among other factors. In addition, we make various estimates and assumptions about the collectability of our loan portfolio, including the creditworthiness of our borrowers and the value of the real estate and other assets, if any, serving as collateral for the repayment of our loans. We also make judgments concerning our legal positions and the priority of our interests in contested legal or bankruptcy proceedings, and at times, we may lack sufficient information to establish specific reserves for loans involved in such proceedings. We base these estimates, assumptions and judgments on information that we consider reliable, but if an estimate, assumption or judgment that we make ultimately proves to be incorrect, additional provisions to our allowance for loan losses may become necessary.

We Have a Goodwill Asset that Could Be Classified as Impaired in the Future. If the Goodwill Asset Is Considered to Be Partially or Fully Impaired in the Future, Our Earnings and the Book Values of This Asset Would Decrease

As of December 31, 2010, we maintained goodwill as an asset in the amount of $22.6 million. We assess our goodwill asset for impairment at least annually. In fourth quarter, 2010, we engaged an independent third-party valuation firm to assist us in our most recent goodwill impairment testing as of December 31, 2010. In its valuation analysis, the third-party valuation firm determined that the fair value of BankFinancial, F.S.B., the reporting unit pursuant to ASC 350-20-35-36, was sufficient to support the carrying value of our goodwill asset. However, if our market capitalization remains below its tangible book value or if the fair value of the reporting unit were to decline, future goodwill impairment testing could result in a partial or full impairment of the value of the Bank s goodwill asset. If we determine that an impairment of our goodwill asset exists at a given point in time, our earnings and the book value of our goodwill asset will be reduced by the amount of the impairment. An impairment of our goodwill asset would have little or no impact on our tangible book value or regulatory capital levels.

If the Company s Deferred Tax Assets Require a Valuation Allowance in the Future, Earnings Will Be Negatively Impacted

We periodically evaluate our deferred tax assets to determine whether a valuation allowance is needed for some portion or all of our deferred tax assets. A valuation allowance must be recognized for a deferred tax asset if, based on the weight of available evidence, it is more likely than not that some portion or all of the deferred tax asset will not be realized. We concluded from our most recent evaluation of our deferred tax assets that it is more likely than not that we will realize the $17.6 million in gross deferred tax assets that were recorded at December 31, 2010. However, if we record net losses in 2011 or in future years, this could call into question our ability to realize some portion or all of the deferred tax assets that we have recorded and require us to recognize a valuation allowance. The recognition of a valuation allowance would have a corresponding impact on our earnings in the period it is recognized.

Changes in Market Interest Rates Could Adversely Affect Our Financial Condition and Results of Operations

Our financial condition and results of operations are significantly affected by changes in market interest rates because our assets, primarily loans, and our liabilities, primarily deposits, are monetary in nature. Our results of operations depend substantially on our net interest income, which is the difference between the interest income that we earn on our interest-earning assets and the interest expense that we pay on our interest-bearing liabilities. We are unable to predict changes in market interest rates that are affected by many factors beyond our control, including inflation, recession, unemployment, money supply, domestic and international events and changes in the United States and other financial markets. Our net interest income is affected not only by the level and direction of interest rates, but also by the shape of the yield curve and relationships between interest sensitive instruments and key driver rates, including credit risk spreads, and by balance sheet growth, customer loan and deposit preferences and the timing of changes in these variables which themselves are impacted by changes in market interest rates. As a result, changes in market interest rates can significantly impact our net interest income as well as the fair market valuation of our assets and liabilities.

The Risks Presented by the Acquisition of Other Institutions Could Adversely Affect Our Financial Condition and Results of Operations

If we acquire other institutions, we will be presented with many risks that could have a material adverse effect on our financial condition and results of operations. An institution that we acquire may have unknown asset quality issues or unknown or contingent liabilities that we did not discover or fully recognize in the due diligence process, thereby resulting in unanticipated losses, particularly in the case of FDIC-assisted transactions due to the highly restrictive due diligence available to potential bidders. The acquisition of other institutions typically requires the integration of different corporate cultures, loan and deposit products, pricing strategies, data processing systems and other technologies, accounting, internal audit and financial reporting systems, operational processes, policies, procedures and internal controls, marketing programs and personnel of the acquired institution in order to make the transaction economically advantageous. The integration process is complicated and time consuming, and could divert our attention from other business concerns and be disruptive to our customers and the customers of the acquired institution. Our failure to integrate an acquired institution successfully could result in the loss of key customers and employees, and prevent us from achieving expected synergies and cost savings. Acquisitions also result in professional fees, purchase price adjustments, the amortization of core deposit intangibles and other expenses that could adversely affect our earnings, and in goodwill that could become impaired, requiring us to recognize further charges. We may finance acquisitions with borrowed funds, thereby increasing our leverage and reducing our liquidity, or with potentially dilutive issuances of equity securities.

Since Our Business is Concentrated in the Chicago Metropolitan Area, Local Economic Conditions May Adversely Affect Our Business

Although we make certain types of loans and leases to borrowers located in other states, our lending and deposit gathering activities are concentrated primarily in the Chicago metropolitan area. Our success can be affected by the general economic conditions of this area and surrounding areas. In addition, many of the loans in our loan portfolio are secured by real estate located in the Chicago metropolitan area. Negative conditions in the real estate markets where collateral for a mortgage loan is located could adversely affect the borrower s ability to repay the loan and the value of the collateral securing the loan. Real estate values are affected by various other factors beyond our control, including real estate supply and demand, the impact of mortgage foreclosures and short sales, changes in general or regional economic conditions and unemployment rates, interest rates, governmental rules or policies and natural disasters. The value of real estate located in many segments of the Chicago metropolitan area has been and continues to be adversely impacted by many of these factors, and this has had, and may continue to have, a negative impact on our loan growth, our ability to collect certain loans according to their terms, and our results of operations.

Difficult Economic Conditions Have Adversely Affected the Banking Industry

National and local economic conditions have been difficult in recent years, and this has resulted in declining real estate values, a tightening of the availability of credit, illiquidity in certain securities markets, increasing loan delinquencies, mortgage foreclosures, personal and business bankruptcies, rising unemployment rates, declining consumer confidence and spending, significant write-downs of asset values by financial institutions and government-sponsored entities, and a reduction of manufacturing and service business activity and international trade. These conditions have contributed to significant declines in the trading prices of certain financial institution stocks, many of which have not fully recovered. We do not expect that the national and local economies will fully recover over the short term, and a continuation or worsening of these conditions could exacerbate their adverse effects. The adverse effects of these conditions could include increases in loan delinquencies and charge-offs, increases to the portion of our loan loss reserve that we base on national or local economic factors, increases to our specific loan loss reserves due to the impact of these conditions on specific borrowers or the collateral for their loans, declines in the value of our investment securities, increases in regulatory and compliance costs, and declines in the trading price of our common stock.

If Our Investment in the Federal Home Loan Bank of Chicago is Classified as Other-Than-Temporarily Impaired, Our Earnings Could Decrease

We own FHLBC common stock to qualify for membership in the Federal Home Loan Bank System and to be eligible to borrow funds under the FHLBC s advance program. The aggregate cost of our FHLBC common stock as of December 31, 2010 was $15.6 million based on its par value. There is no market for our FHLBC common stock. Due to our receipt of stock dividends and a reduction of our outstanding FHLBC advances, we owned shares of FHLBC common stock at December 31, 2010 with a par value that was $9.0 million more than we were required to own to maintain our membership, in the Federal Home Loan Bank System and to be eligible to obtain advances (excess or voluntary capital stock).

The FHLBC is subject to a cease and desist order issued by the Federal Housing Finance Board, now known as the Federal Housing Finance Agency (FHFA), in 2007. Among other things, the cease and desist order requires the FHLBC to submit a capital plan to the FHFA, prohibits certain capital stock repurchases and stock redemptions, including certain redemptions upon membership withdrawal, without the prior approval of the Director of the Office of Supervision of the FHFA (Director), and prohibits the payments of dividends without the prior approval of the Director. The FHLBC has reported that it has submitted a capital plan to the Director but that it has not yet been approved. The FHLBC did not pay any dividends from the third quarter of 2007 through 2010, but in the first quarter of 2011, paid a nominal cash dividend at an annualized rate of 10 basis points per share. The FHLBC reported in February 2011 that it had earnings of net income of $366 million for 2010, compared to a net loss of $65 million in 2009, and that it is in compliance with its regulatory capital requirements.

Current accounting guidance requires us to evaluate our FHLBC common stock for impairment based on the ultimate recoverability of the par value of the security without regard to temporary declines in value. We concluded from our most recent impairment testing that it is probable that the par value of our FHLBC common stock is ultimately recoverable based on the FHLBC s current compliance with its regulatory capital requirements, the net income that it reported for 2010, its receipt of regulatory approval to pay a dividend in the first quarter of 2011 and published reports indicating that it is continuing to work with its regulator to finalize a capital plan. However, if events were to occur that give rise to substantial doubt about the ultimate recoverability of the par value of our FHLBC common stock, this investment could become other-than-temporarily impaired, and the impairment loss that we would be required to record would cause our earnings to decrease by the after-tax amount of the impairment loss.

Our Future Success is Dependent on Our Ability to Compete Effectively in the Highly Competitive Banking Industry

We face substantial competition in all phases of our operations from a variety of different competitors. Our future growth and success will depend on our ability to compete effectively in this highly competitive environment. To date, we have grown our business successfully by focusing on our geographic markets and emphasizing the high level of service and responsiveness desired by our customers. We compete for loans, deposits and other financial services with other commercial banks, thrifts, credit unions, brokerage houses, mutual funds, insurance companies, real estate conduits, and specialized finance companies. Many of our competitors offer products and services that we do not offer, and many have substantially greater resources and lending limits, name recognition and market presence that benefit them in attracting business. In addition, larger competitors may be able to price loans and deposits more aggressively than we do, and smaller newer competitors may be more aggressive in pricing loans and deposits in order to increase their market share. Some of the financial institutions and financial services organizations with which we compete are not subject to the extensive regulations imposed on federal savings banks and their holding companies. As a result, these nonbank competitors have certain advantages over us in accessing funding and in providing various financial services.

Our Business May Be Adversely Affected by the Highly Regulated Environment in Which We Operate

We are subject to extensive federal and state legislation, regulation, examination and supervision. The Dodd-Frank Act and other recently enacted legislation, the regulations promulgated there, and future legislation and regulations that may be enacted or promulgated, could have an adverse effect on our business and operations. In addition, the OTS will cease to be the primary federal regulator of the Company and the Bank on July 21, 2011, and we may need to make adjustments in our policies and procedures to ensure compliance with the rules and regulations of the OCC and the FRB. Our success will be impacted by our continued ability to comply with applicable laws and regulations. Some of these laws and regulations may increase our costs. While we cannot predict what effect any future changes in these laws or regulations or their interpretations would have on us, these changes or interpretations may adversely affect our future operations.

Trading Activity in the Company s Common Stock Could Result in Material Price Fluctuations

It is possible that trading activity in the Company s common stock, including short-selling or significant sales by current stockholders, could result in material price fluctuations of the price per share of the Company s common stock. In addition, such trading activity and the resultant volatility could make it more difficult for the Company to sell equity or equity-related securities in the future at a time and price it deems appropriate, or to use its stock as consideration for an acquisition. *See Our Ability to Successfully Conduct Acquisitions Will Affect Our Ability to Grow Our Franchise and Compete Effectively in Our Marketplace* .

Our Return on Stockholders Equity Will Continue to Be Low Due to Our High Capital Level

Net income divided by average stockholders equity, known as return on equity, is a ratio that many investors use to compare the performance of a financial institution to its peers. Our capital remains relatively high by industry standards pending a more optimal deployment of the additional capital raised in our 2005 mutual-to-stock conversion. Until we can increase our net interest income and noninterest income, we expect our return on equity to continue to be below the historical industry average, which may negatively affect the value of our shares of common stock

The Company s Ability to Pay Dividends is Affected by Regulatory Limitations on the Bank s Ability to Pay Dividends and Other Regulatory Limitations

The Company is a separate legal entity from its subsidiaries and does not have significant operations of its own. Dividends from the Bank provide a significant source of cash for the Company. The availability of dividends from the Bank is limited by various statutes and regulations. Under these statutes and regulations, the Bank is not permitted to pay dividends on its capital stock to the Company, its sole stockholder, if the dividend would reduce the stockholders equity of the Bank below the amount of the liquidation account established in connection with the mutual-to-stock conversion. The Bank may pay dividends without the approval of its primary federal regulator only if the Bank meets its applicable regulatory capital requirements before and after the payment of the dividends and its total dividends do not exceed its net income to date over the calendar year plus its retained net income over the preceding two years. Although the Bank s capital exceeded applicable regulatory requirements at December 31, 2010, the Bank did not have sufficient net income over the preceding two years to pay a dividend to the Company without the prior approval of its primary federal regulator. If the Bank were to seek the approval of its primary federal regulator to pay a dividend, there can be no assurance that such approval would be granted. If at some point in the future the Company utilizes its available cash for other purposes Bank is unable to pay dividends to the Company, the Company may not have sufficient funds to continue to pay dividends on its common stock. In addition, the Company s ability to pay dividends on its common stock could be further limited by the application of the source of strength doctrine, which requires holding companies to provide financial support to their subsidiary depository institutions if the subsidiary is in financial distress, or by regulatory order.

We Continually Encounter Technological Change, and May Have Fewer Resources than Many of Our Competitors to Continue to Invest in Technological Improvements

The financial services industry is undergoing rapid technological changes, with frequent introductions of new technology-driven products and services. The effective use of technology increases efficiency and enables financial institutions to better serve customers and to reduce costs. Our future success will depend, in part, upon our ability to address the needs of our customers by using technology to provide products and services that will satisfy customer demands for convenience, as well as to create additional efficiencies in our operations. Many of our competitors have substantially greater resources to invest in technological improvements. We also may not be able to effectively implement new technology-driven products and services or be successful in marketing these products and services to our customers.

Our Ability to Successfully Conduct Acquisitions Will Affect Our Ability to Grow Our Franchise and Compete Effectively in Our Marketplace

We consider the possible acquisition of other banks, thrifts and other financial services companies in private or FDIC-assisted transactions to supplement internal growth. Although we entered into a definitive agreement to acquire DG Bancorp, Inc. and its subsidiary, Downers Grove National Bank in the third quarter of 2010, our efforts to acquire other financial institutions and financial service companies in the future may not be successful. Other potential acquirors exist for most acquisition candidates, creating competition that can affect the purchase price for which the institution can be acquired. In many cases, our competitors have significantly greater resources than we have, and greater flexibility to structure the consideration for the transaction. We may not participate in specific acquisition opportunities if we consider the proposed transaction unacceptable, including the current or potential future terms, conditions and limitations imposed by an FDIC-assisted transaction. We also may not be the successful bidder in acquisition opportunities that we pursue due to the willingness or ability of other potential acquirors to propose a higher purchase price or more attractive terms and conditions than we are willing or able to propose. The results of a merger or acquisition could change materially based on future changes in applicable accounting principles and regulatory requirements related to acquired assets and liabilities. If we are unable to or do not conduct acquisitions to supplement internal growth, our ability to deploy effectively the capital we raised in the 2005 offering, expand our geographic presence and improve our results of operations could be adversely affected.

FDIC Deposit Insurance Premiums Have Increased and May Increase Further in the Future

The Federal Deposit Insurance Act, as amended, requires the FDIC to maintain a reserve ratio between 1.15% and 1.50%. The FDIC s Board of Directors is required to establish a designated reserve ratio within that range and set assessment rates to meet that target within a time frame that the FDIC s Board of Directors deems appropriate. If the reserve ratio falls below 1.15%, the FDIC s Board of Directors is required to establish a restoration plan to bring the reserve ratio back to 1.15% within five years. The FDIC s reserve ratio declined over the past several years due to costs associated with bank failures, and it is possible that the reserve ratio could be placed under stress due to future bank failures. As part of its plan to restore the reserve ratio to 1.15%, the FDIC s Board of Directors imposed a special assessment equal to five basis points of assets less Tier 1 capital as of June 30, 2009, which was payable on September 30, 2009. In addition, the FDIC increased its quarterly assessment rates and amended the method by which rates are calculated. On November 12, 2009, the FDIC approved a final rule requiring insured depository institutions to prepay, on December 30, 2009, their estimated quarterly risk-based assessments for the fourth quarter of 2009, and for all of 2010, 2011, and 2012. Prepaid assessments are to be applied against the actual quarterly assessments until exhausted, and may not be applied to any special assessments that may occur in the future. Any unused prepayments will be returned on June 30, 2013. See Supervision and Regulation Insurance of Deposit Accounts. On December 30, 2009, the Bank paid the estimated assessment fees for the fourth quarter of 2009 and prepaid $6.8 million in estimated assessment fees through 2012. These increased assessments have had an adverse impact on our results of operations in

2009 and will continue to have an adverse impact in future years. If circumstances require the FDIC to impose additional special assessments or further increase its quarterly assessment rates, the adverse impact will be exacerbated.

Various Factors May Make Takeover Attempts That You Want to Succeed More Difficult to Achieve, Which May Affect the Value of Shares of Our Common Stock

Provisions of our articles of incorporation and bylaws, federal regulations, Maryland law and various other factors may make it more difficult for companies or persons to acquire control of the Company without the consent of our board of directors. You may want a takeover attempt to succeed because, for example, a potential acquiror could offer a premium over the then prevailing price of our shares of common stock. The OTS regulations prohibit the direct or indirect acquisition of more than 10% of any class of equity security of a converted savings institution without the prior approval of the OTS. Provisions of our articles of incorporation and bylaws also may make it difficult to remove our current board of directors or management if our board of directors opposes the removal. We have elected to be subject to the Maryland Business Combination Act, which places restrictions on mergers and other business combinations with large stockholders. In addition, our articles of incorporation provide that certain mergers and other similar transactions, as well as amendments to our articles of incorporation, must be approved by stockholders owning at least two-thirds of our shares of common stock entitled to vote on the matter unless first approved by at least two-thirds of the number of our authorized directors, assuming no vacancies. If approved by at least two-thirds of the number of our authorized directors, assuming no vacancies, the action must still be approved by a majority of our shares entitled to vote on the matter. In addition, a director can be removed from office, but only for cause, if such removal is approved by stockholders owning at least two-thirds of our shares of common stock entitled to vote on the matter. However, if at least two-thirds of the number of our authorized directors, assuming no vacancies, approves the removal of a director, the removal may be with or without cause, but must still be approved by a majority of our voting shares entitled to vote on the matter. Additional provisions include limitations on the voting rights of any beneficial owners of more than 10% of our common stock. Our bylaws, which can only be amended by the board of directors, also contain provisions regarding the timing, content and procedural requirements for stockholder proposals and nominations.

Non-Compliance with USA PATRIOT Act, Bank Secrecy Act, Real Estate Settlement Procedures Act, Truth-in-Lending Act or Other Laws and Regulations Could Result in Fines or Sanctions, and Curtail Expansion Opportunities

Financial institutions are required under the USA PATRIOT and Bank Secrecy Acts to develop programs to prevent financial institutions from being used for money-laundering and terrorist activities. Financial institutions are also obligated to file suspicious activity reports with the U.S. Treasury Department s Office of Financial Crimes Enforcement Network if such activities are detected. These rules also require financial institutions to establish procedures for identifying and verifying the identity of customers seeking to open new financial accounts. Failure or the inability to comply with these regulations could result in fines or penalties, curtailment of expansion opportunities, intervention or sanctions by regulators and costly litigation or expensive additional controls and systems. During the last few years, several banking institutions have received large fines for non-compliance with these laws and regulations. In addition, the U.S. Government imposed and will continue to expand laws and regulations relating to residential and consumer lending activities that create significant new compliance burdens and financial risks. We have developed policies and continue to augment procedures and systems designed to assist in compliance with these laws and regulations.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

As of December 31, 2010 the net book value of our properties was $28.5 million. The following is a list of our offices:

Burr Ridge (Executive Office) 15W060 North Frontage Road Burr Ridge, IL 60527	Deerfield 630 N. Waukegan Road Deerfield, IL 60015	Northbrook 1368 N. Shermer Road Northbrook, IL 60062
Calumet City 1901 Sibley Boulevard Calumet City, IL 60409	Hazel Crest 3700 W. 183rd Street Hazel Crest, IL 60429	Olympia Fields 21110 S. Western Avenue Olympia Fields, IL 60461
Calumet Park 1333 W. 127th Street Calumet Park, IL 60827	Joliet 1401 N. Larkin Joliet, IL 60435	Orland Park 48 Orland Square Drive Orland Park, IL 60462
Chicago - Hyde Park 1354 East 55th Street Chicago, IL 60615	Lincolnshire One Marriott Drive Lincolnshire, IL 60069	Schaumburg 1005 W. Wise Road Schaumburg, IL 60193
Chicago - Hyde Park East 55th at Lake Park Avenue Chicago, IL 60615	Lincolnwood 3443 W. Touhy Lincolnwood, IL 60712	South Libertyville 1123 S. Milwaukee Avenue Libertyville, IL 60048
Chicago Ridge 6415 W. 95th Street Chicago Ridge, IL 60415	Naperville 1200 E. Ogden Avenue Naperville, IL 60563	
Chicago - Lincoln Park 2424 N. Clark Street Chicago, IL 60614	North Libertyville 1409 W. Peterson Road Libertyville, IL 60048	

Except for our Chicago-Lincoln Park, Northbrook, and Hyde Park East offices, which are leased, all of our offices are owned. In addition to the above listed properties, we also operate three Express Branch facilities, two satellite national commercial leasing offices and two remote ATMs on sites where we do not have a full-service banking office.

ITEM 3. LEGAL PROCEEDINGS

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

ITEM 4. [RESERVED]

PART II

ITEM 5. MARKET FOR REGISTRANT S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Our shares of common stock are traded on the Nasdaq Global Select Market under the symbol BFIN. The approximate number of holders of record of the Company s common stock as of December 31, 2010 was 1,820. Certain shares of the Company s common stock are held in nominee or street name, and accordingly, the number of beneficial owners of such shares is not known or included in the foregoing number.

The following table presents quarterly market information provided by the Nasdaq Stock Market for the Company s common stock and cash dividends paid for the periods ended December 31, 2010 and 2009.

2009 and 2010 Quarterly Periods	High	Low	Close	Cash Dividends Paid
Quarter ended December 31, 2010	$ 9.90	$ 9.06	$ 9.75	$ 0.07
Quarter ended September 30, 2010	9.38	8.12	9.17	0.07
Quarter ended June 30, 2010	9.99	8.28	8.31	0.07
Quarter ended March 31, 2010	10.16	9.01	9.17	0.07
Quarter ended December 31, 2009	$ 10.40	$ 9.07	$ 9.90	$ 0.07
Quarter ended September 30, 2009	11.04	8.75	9.60	0.07
Quarter ended June 30, 2009	11.10	8.07	8.86	0.07
Quarter ended March 31, 2009	11.10	7.19	9.97	0.07

The Company is subject to state law limitations on the payment of dividends. Maryland law generally limits dividends to an amount equal to the excess of our capital surplus over payments that would be owed upon dissolution to stockholders whose preferential rights upon dissolution are superior to those receiving the dividend, and to an amount that would not make us insolvent provided, however, that even if the Company s assets are less than the amount necessary to satisfy the requirement set forth above, the Company may make a distribution from: (A) the Company s net earnings for the fiscal year in which the distribution is made; (B) the Company s net earnings for the preceding fiscal year; or (C) the sum of the Company s net earnings for the preceding eight fiscal quarters. Dividends from the Bank provide a significant source of cash for the Company. The availability of dividends from the Bank is limited by various statutes and regulations. For a discussion of the Bank s ability to pay dividends, see Part I, Item 1, Business - Supervision and Regulation Federal Banking Regulation Capital Distributions.

Recent Sales of Unregistered Securities

The Company had no sales of unregistered stock during the quarter ended December 31, 2010.

Repurchases of Equity Securities

Our Board of Directors has authorized the repurchase of up to 5,047,423 shares of our common stock. In accordance with this authorization, we had repurchased 4,239,134 shares of our common stock as of December 31, 2010. There were no share repurchases conducted in the fourth quarter of 2010. The current share repurchase authorization will expire on May 16, 2011, unless extended by our Board of Directors.

Stock Performance Graph

The following Performance Graph and related information shall not be deemed soliciting material or to be filed with the Securities and Exchange Commission, nor shall such information be incorporated by reference into any future filing under the Securities Act of 1933 or Securities Exchange Act of 1934, each as amended, except to the extent that the Company specifically incorporates it by reference into such filing.

We completed our mutual-to-stock conversion on June 23, 2005, in connection with which the Company sold an aggregate of 24,466,250 shares of common stock at a price of $10.00 per share. The Company s common stock began trading on the Nasdaq Stock Market under the symbol BFIN on June 24, 2005, and the per share closing price of one share of the Company s common stock on that date was $13.60. The following graph represents $100 invested in our common stock at the $13.60 per share closing price on June 24, 2005. The graph illustrates the comparison of the cumulative total returns for the common stock of the Company, the Russell 2000 Index, the NASDAQ Bank Index and the America s Community Bankers NASDAQ Index for the periods indicated.

There can be no assurance that our stock performance will continue in the future with the same or similar trend depicted in the graph below. We will not make or endorse any predictions as to future stock performance.

	12/31/2005	12/31/2006	12/31/2007	12/31/2008	12/31/2009	12/31/2010
BankFinancial Corporation	107.94	132.36	119.65	78.58	78.45	79.41
Russell 2000 Index	107.49	127.24	125.24	82.93	105.46	133.78
NASDAQ Bank Index	102.58	113.88	88.74	67.51	55.02	61.56
America s Community Bankers NASDAQ Index	103.69	114.92	86.43	69.51	54.65	59.71

ITEM 6. SELECTED FINANCIAL DATA

The following information is derived from the audited consolidated financial statements of the Company. For additional information, reference is made to Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations and the Consolidated Financial Statements of the Company and related notes included elsewhere in this Annual Report.

	At December 31,				
	2010	2009	2008	2007	2006
	(Dollars in thousands)				
Selected Financial Condition Data:					
Total assets	$ 1,530,655	$ 1,566,963	$ 1,554,855	$ 1,480,712	$ 1,613,150
Loans, net	1,050,766	1,218,540	1,268,122	1,254,167	1,329,943
Loans held-for-sale	2,716		872	173	298
Securities, at fair value	120,747	102,126	124,919	77,049	117,853
Goodwill	22,566	22,566	22,566	22,566	22,579
Core deposit intangible	2,700	4,295	5,985	7,769	9,648
Deposits	1,235,377	1,233,395	1,069,855	1,073,650	1,129,585
Borrowings	23,749	50,784	200,350	96,433	138,148
Equity	253,285	263,603	266,791	291,137	326,015

	Years Ended December 31,				
	2010	2009	2008	2007	2006
	(Dollars in thousands, except per share data)				
Selected Operating Data:					
Interest and dividend income	$ 64,936	$ 74,109	$ 77,960	$ 91,953	$ 94,086
Interest expense	13,186	20,557	25,667	38,304	37,489
Net interest income	51,750	53,552	52,293	53,649	56,597
Provision (credit) for loan losses	12,083	8,811	5,092	697	(136)
Net interest income after provision (credit) for loan losses	39,667	44,741	47,201	52,952	56,733
Noninterest income	7,128	7,239	10,418	9,665	10,554
Noninterest expense (1)	53,849	52,731	89,056	52,499	52,415
Income (loss) before income tax expense	(7,054)	(751)	(31,437)	10,118	14,872
Income tax expense (benefit)	(2,747)	(13)	(12,048)	2,963	4,826
Net income (loss)	$ (4,307)	$ (738)	$ (19,389)	$ 7,155	$ 10,046
Basic earnings (loss) per common share	$ (0.22)	$ (0.04)	$ (0.98)	$ 0.35	$ 0.45
Diluted earnings (loss) per common share	$ (0.22)	$ (0.04)	$ (0.98)	$ 0.35	$ 0.45

(footnotes on following page)

	At or For the Years Ended December 31,				
	2010	2009	2008	2007	2006
Selected Financial Ratios and Other Data:					
Performance Ratios:					
Return on assets (ratio of net income (loss) to average total assets)	(0.28)%	(0.05)%	(1.33)%	0.47%	0.61%
Return on equity (ratio of net income (loss) to average equity)	(1.64)	(0.28)	(6.84)	2.30	3.02
Net interest rate spread (2)	3.36	3.36	3.35	2.94	2.89
Net interest margin (3)	3.57	3.69	3.88	3.78	3.68
Efficiency ratio (4)	91.46	86.74	142.01	82.92	78.06
Noninterest expense to average total assets	3.45	3.36	6.09	3.42	3.19
Average interest-earning assets to average interest-bearing liabilities	122.56	123.43	127.85	130.95	132.67
Dividends declared per share	$ 0.28	$ 0.28	$ 0.28	$ 0.28	$ 0.18
Dividend payout ratio	N.M.	N.M.	N.M.	90.6%	44.3%
Asset Quality Ratios:					
Nonperforming assets to total assets (5)	3.94%	3.42%	0.94%	0.87%	0.57%
Nonperforming loans to total loans	4.26	4.01	1.07	0.95	0.69
Allowance for loan losses to nonperforming loans	48.54	37.63	107.97	91.65	115.13
Allowance for loan losses to total loans	2.07	1.51	1.15	0.87	0.79
Net charge-offs to average loans outstanding	0.75	0.39	0.11	0.02	0.07
Capital Ratios:					
Equity to total assets at end of period	16.55%	16.82%	17.16%	19.66%	20.21%
Average equity to average assets	16.77	17.02	19.39	20.32	20.25
Tier 1 leverage ratio (Bank only)	12.48	12.44	12.08	13.95	15.05
Other Data:					
Number of full-service offices	18	18	18	18	18
Employees (full-time equivalents)	328	372	393	425	438

(1) Noninterest expense for the years ended December 31, 2009 and 2008 includes $401,000 and $35.9 million, respectively, of impairment loss on securities.
(2) The net interest rate spread represents the difference between the yield on average interest-earning assets and the cost of average interest-bearing liabilities for the period.
(3) The net interest margin represents net interest income divided by average total interest-earning assets for the period.
(4) The efficiency ratio represents noninterest expense divided by the sum of net interest income and noninterest income.
(5) Nonperforming assets include nonperforming loans and other real estate owned and in process.

N.M. Not Meaningful

ITEM 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS
The discussion and analysis that follows focuses on the factors affecting our consolidated financial condition at December 31, 2010 and 2009, and our consolidated results of operations for the three years ended December 31, 2010. The consolidated financial statements, the related notes and the discussion of our critical accounting policies appearing elsewhere in this Annual Report should be read in conjunction with this discussion and analysis.

Overview

Loans. Our loan portfolio consists primarily of investment and business loans (multifamily, nonresidential real estate, commercial, construction and land loans, and commercial leases), which together make up 75.9% of gross loans at December 31, 2010. Net loans receivable decreased $167.8 million, or 13.8%, to $1.051 billion at December 31, 2010, from $1.219 billion at December 31, 2009. Multi-family mortgage loans decreased by $32.3 million, or 9.8%, due in substantial part to a HUD refinancing that was completed by a related group of borrowers. Commercial loans decreased by $23.4 million, or 26.6%, due to the combined impact of loan pay downs and reduced originations. Commercial leases decreased by $25.7 million, or 14.5%, as scheduled lease payments outpaced originations. Nonresidential real estate loans decreased $34.6 million, or 10.9%, primarily due to principal payments of $56.6 million, which were partially offset by $15.3 million in draws on existing credit commitments. Construction and land loans decreased $14.2 million, or 43.5%, primarily due to project sales and conversions to permanent amortizing loans. One-to-four family residential mortgage loans decreased $33.3 million, or 11.5%, primarily due to refinancings that were not replaced with new originations. Future loan growth could be adversely affected by our unwillingness to compete for loans by relaxing our historical underwriting standards.

Securities. Securities increased $18.6 million, or 18.2%, to $120.7 million at December 31, 2010, from $102.1 million at December 31, 2009. The primary reason for the increase was $50.5 million in purchases, offset by $31.8 million of principal repayments and maturities of securities. During 2010 we utilized FDIC insured certificates of deposit as an investment option.

Deposits. Deposits increased $2.0 million, or 0.2%, to $1.235 billion at December 31, 2010, from $1.233 billion at December 31, 2009. We increased our core deposits (savings, money market, noninterest-bearing demand and NOW accounts) by $25.5 million and reduced our balances of wholesale deposits by $14.7 million during the year. Core deposits increased as a percentage of total deposits, representing 69.2% of total deposits at December 31, 2010, compared to 67.3% of total deposits at December 31, 2009.

Borrowings. Borrowings decreased $27.0 million, or 53.2%, to $23.7 million at December 31, 2010, from $50.8 million at December 31, 2009, due to our repayments of maturing FHLBC advances.

Stockholders Equity. Total stockholders equity was $253.3 million at December 31, 2010, compared to $263.6 million at December 31, 2009. The decrease in total stockholders equity was primarily due to the combined impact of our repurchase of 356,411 shares of our common stock during 2010 at a total cost of $3.1 million, our declaration and payment of cash dividends totaling $5.9 million, the $4.3 million net loss that we recorded for 2010 and a $50,000 decrease in accumulated other comprehensive income. These items were partially offset by a $3.1 million increase in total stockholders equity that resulted from the vesting of stock-based compensation and ESOP shares earned. The unallocated shares of common stock that our ESOP owns were reflected as a $14.2 million reduction to stockholders equity at December 31, 2010, compared to a $15.2 million reduction to stockholders equity at December 31, 2009.

Net Loss. We recorded a net loss of $4.3 million for the year ended December 31, 2010, compared to net losses of $738,000 and $19.4 million for 2009 and 2008, respectively. The net loss in 2010 was due in substantial part to our recording a $12.1 million provision for loan losses, $7.3 million for nonperforming asset management expense and operations of other real estate owned combined with a $1.8 million decrease in net interest income. The net loss in 2009 was due primarily to the recording of an $8.8 million provision for loan losses, a $2.1 million increase in FDIC expense and $1.4 million in combined pre-tax losses that we recorded in connection with the impairment and subsequent sale of our Freddie Mac preferred stocks. The impact of these items was partially offset by a $1.3 million gain that we recognized on the sale of our merchant processing operations in 2009. The net loss in 2008 was due in substantial part to a $35.9 million pre-tax impairment loss that we recorded on our Freddie Mac preferred stocks after Freddie Mac was placed into conservatorship. Our basic loss per common share was $0.22, $0.04 and $0.98 for the years ended December 31, 2010, 2009 and 2008, respectively.

Net Interest Income. We recorded net interest income of $51.8 million for the year ended December 31, 2010, compared to $53.6 million for 2009 and $52.3 million for 2008. The decrease in net interest income for 2010 reflected a $9.2 million decrease in interest income, which was partially offset, by a $7.4 million decrease in interest expense. Our net interest rate spread was 3.36% for the years ended December 31, 2010 and 2009.

Provision for Loan Losses. We recorded a provision for loan losses of $12.1 million for the year ended December 31, 2010, compared to $8.8 million for 2009 and $5.1 million for 2008. The provision for loan losses that we recorded in 2010 reflects the combined impact of a $4.4 million increase in the portion of the specific allowance for loan losses that we allocate to impaired loans and $8.5 million in net charge-offs, which were partially offset by a $794,000 decrease in the general component of the allowance for loan losses.

Noninterest Income. Noninterest income for the year ended December 31, 2010 was $7.1 million, compared to $7.2 million for 2009 and $10.4 million for 2008. Our noninterest income for 2010 included service charges and fees of $3.0 million, compared to $3.4 million for 2009 and $3.6 million for 2008. Earnings on bank-owned life insurance were $430,000 for the year ended December 31, 2010, compared to a $20,000 loss for 2009 and earnings of $586,000 for 2008. Our noninterest income for 2009 included a $988,000 loss on the sale of our Freddie Mac preferred stocks and a $1.3 million gain on the sale of our merchant processing operations. Our noninterest income for 2008 included a $1.4 million pre-tax gain on the sale of shares of Visa, Inc. Class B common stock that we received in connection with Visa, Inc. s initial public offering, and a $1.2 million pre-tax gain on additional shares of Visa, Inc. Class B common stock that were allocated to us in the initial public offering and are currently held in a litigation escrow under Visa, Inc. s retrospective responsibility plan. The gain that we recorded on the escrowed shares of the Visa, Inc. Class B common stock reduced our obligation to indemnify Visa USA under Visa, Inc. s retrospective responsibility plan.

Noninterest Expense. Noninterest expense for the year ended December 31, 2010 was $53.9 million, compared to $52.7 million for 2009 and $89.1 million for 2008. Noninterest expense for 2010 included $3.3 million in nonperforming asset management expenses, compared to $770,000 in 2009. Operations of other real estate owned totaled $4.0 million in 2010, compared to $1.3 million in 2009. Noninterest expense for 2009 included a $401,000 pre-tax impairment loss that we recorded on our holdings of Freddie Mac preferred stocks. Expense for FDIC deposit insurance totaled $2.1 million during the year ended December 31, 2010, compared to $2.2 million for 2009 and $162,000 for 2008. The increase in our 2009 expense for FDIC deposit insurance was due to the combined effect of the FDIC s increase in its quarterly assessment rate, the FDIC s imposition of a special assessment against all insured institutions and the full utilization of the FDIC assessment credits that we previously had available to offset or reduce FDIC quarterly assessments. Noninterest expense for 2008 included a $35.9 million pre-tax impairment loss that we recorded on our holdings of Freddie Mac preferred stocks and a $2.0 million pre-tax loss on the early extinguishment of borrowings that we recorded in connection with the prepayment of a $25 million FHLBC term advance.

Income Taxes. We recorded an income tax benefit of $2.7 million for the year ended December 31, 2010, compared to $13,000 and $12.0 million for 2009 and 2008. The effective tax rates were 38.94%, 1.73% and 38.32% for the years ended December 31, 2010, 2009 and 2008, respectively. For 2009, the difference between the GAAP basis (fair market value at the date of grant) and the tax basis (fair market value at the date of vesting) of equity-based compensation granted in prior years reduced our income tax benefit. The income tax benefit for 2008 was due in substantial part to the recording of an impairment loss on our Freddie Mac preferred stocks.

Key Strategic Initiatives and Events

Stock Repurchase Program. Our Board of Directors has authorized the repurchase of up to 5,047,423 shares of our common stock. The authorization permits shares to be repurchased in open market or negotiated transactions, and pursuant to any trading plan that may be adopted in accordance with Rule 10b5-1 of the Securities and Exchange Commission. The authorization may be utilized at management's discretion, subject to the limitations set forth in Rule 10b-18 of the Securities and Exchange Commission and other applicable legal requirements, and to price and other internal limitations established by the Board of Directors. The repurchase authorization will expire on May 16, 2011, unless extended by the Board of Directors. As of December 31, 2010, the Company had repurchased 4,239,134 shares of its common stock pursuant to the repurchase authorization.

Quarterly Cash Dividends. Our Board of Directors declared four quarterly cash dividends of $0.07 per share during 2010. Cash dividends totaling $5.9 million were paid in 2010. On January 27, 2011, the Board of Directors declared a quarterly cash dividend of $0.07 per share that is payable on March 4, 2011.

Pending Acquisition. On September 13, 2010, we entered into a definitive agreement to acquire DG Bancorp, Inc., the bank holding company for Downers Grove National Bank, a privately held community bank with approximately $219 million in assets and $213 million in deposits as of December 31, 2010. Downers Grove National Bank has two banking offices located in Downers Grove and Westmont, Illinois. We have received all regulatory approvals that are required to consummate the transaction and the closing is expected to occur during the first quarter of 2011, subject to customary closing conditions. Downers Grove National Bank will be merged into the Bank as part of the consummation of the transaction.

We are in the process of negotiating the acquisition of a portfolio of performing loans from Citibank N.A. with an aggregate unpaid principal balance of approximately $155.8 million. The purchase is scheduled to close in March 2011, subject to customary closing conditions. This loan portfolio consists of multifamily loans originated by Citibank N.A. or the former Citibank, F.S.B. and the loans are secured by real estate collateral located in the Chicago metropolitan market area. The portfolio consists of 470 loans with an overall weighted average effective yield of 5.87%. All loans in the portfolio were current on all payments due as of the month prior to the month in which the purchase is scheduled to close. Upon the closing of the purchase, we expect to file a Current Report on Form 8-K further describing the portfolio acquisition transaction and the portfolio characteristics.

Economic and Competitive Conditions

General U.S. financial market conditions further stabilized during 2010. The national economy began a very modest expansion but local economic conditions remained largely unchanged from 2009. Pricing and underwriting for multi-family and commercial real estate loans were generally favorable, but we experienced relatively low demand for these loan types throughout 2010. Pricing for commercial leases became less favorable during 2010 amid weak supply as lessors deployed excess cash and several competitors re-entered the market during the year. Demand for the Bank s traditional adjustable-rate residential mortgage loans remained low due to an overwhelming market preference for fixed-rate residential mortgage loans given low market interest rates and our underwriting standards.

We experienced net declines in all loan portfolio component balances during 2010 due to several factors, including overall weak loan demand, loan payoffs, our decisions to exit certain credit relationships and transfers of certain loans to OREO upon the conclusion of formal collection proceedings. We expect a return to modest growth in most loan portfolio segments if real estate market valuations stabilize and the supply of commercial lease opportunities improves based on global macroeconomic conditions.

Our loan portfolio quality metrics reflected the overall economic environment in 2010. The net increase in nonaccrual loans and a related increase in our loan loss reserves resulted primarily from a corresponding material decline in the valuations of the underlying collateral and a decline in effective rents and occupancies in certain income-producing properties; however, effective rents and occupancies in multifamily properties began to stabilize late in 2010. We also noted a continued influx of personal and business bankruptcy cases; of these, the majority of borrowers sought to avoid their obligations while a minority sought to restructure their debt to continue ownership of their assets. General market conditions and efforts by various governmental entities and local courts to further slow the pace of foreclosures continued to affect the pace of our progress in resolving classified assets, but we expect the pace of resolutions to increase in 2011. We continue to believe that unemployment, consumer spending and borrower perceptions of residential and commercial real estate valuations will be the primary factors affecting loan portfolio quality in 2011.

As we expected, our general loan loss reserves continued to increase. As part of our computation of the required level for our general loan loss reserve, our model incorporates the changes in national and local economic risk factors, the changes in the levels of classified loans by loan type, and the impact of the additional specific valuation allowances or charge-offs recorded on classified loans. Our underwriting standards remain consistent with our historical standards, although our credit analyses incorporate somewhat more conservative assumptions with respect to effective rents, expenses and occupancies given the current economic environment.

Deposits increased slightly in 2010. Pricing conditions for local deposits, whether low-balance core deposits, certificates of deposits or high-balance, high-yield transaction accounts, remained favorable during the year due to very low market yields and continued weak industry-wide loan demand. We continued to moderate our competitive position given the weak lending environment and our excess liquidity position. We expect a similar competitive environment for the first half of 2011, and we will continue our marketing efforts to further enhance the depth and quality of our deposit portfolio.

Our net interest spread declined in 2010 as the decline in loan portfolio balances and, to a lesser extent, the impact of loans placed on non-accrual status offset the benefits of a favorable yield curve and improved credit spreads. Given the quantity and volatility of the variables affecting our net interest margin and net interest spread, we are unable to confidently predict our net interest margin and net interest spread in 2011.

Non-interest income decreased in 2010 due to a materially lower net gain on the sale of securities and reduced deposit-related fee income, which was partially offset by higher income from insurance and annuities and other fee income. Wealth management performed slightly better than our expectations for 2010.

Non-interest expense increased slightly in 2010 as a significant increase in expenses related to non-performing assets and write-downs on OREO offset the favorable impact of our focus on improving efficiency through operational reviews and technology deployments. We expect that the expenses related to non-performing loans and classified asset management will decline in the latter part of 2011 in conjunction with the anticipated gradual decline of the levels of non-performing assets.

Critical Accounting Policies

Critical accounting policies are defined as those that are reflective of significant judgments and uncertainties, and could potentially result in materially different results under different assumptions and conditions. We believe that the most critical accounting policies upon which our financial condition and results of operation depend, and which involve the most complex subjective decisions or assessments, are as follows:

Allowance for Loan Losses. Arriving at an appropriate level of allowance for loan losses involves a high degree of judgment. Our allowance for loan losses provides for probable incurred losses based upon evaluations of known and inherent risks in the loan portfolio. We review the level of the allowance on a quarterly basis and establish the provision for loan losses based upon historical loan loss experience, the nature and volume of the loan portfolio, information about specific borrower situations, estimated collateral values, economic conditions and other factors to assess the adequacy of the allowance for loan losses. Among the material estimates that we must make to establish the allowance are loss exposure at default; the amount and timing of future cash flows on affected loans; the value of collateral; and a determination of loss factors to be applied to the various elements of the loan portfolio. All of these estimates are susceptible to significant change. Although we believe that we use the best information available to us to establish the allowance for loan losses, future adjustments to the allowance may be necessary if borrower financial, collateral valuation or economic conditions differ substantially from the information and assumptions used in making the evaluation. In addition, as an integral part of their examination process, our regulatory agencies periodically review the allowance for loan losses. These agencies may require us to recognize additions to the allowance based on their judgments of information available to them at the time of their examination. A large loss could deplete the allowance and require increased provisions to replenish the allowance, which would negatively affect earnings.

Intangible Assets. Acquisitions accounted for under purchase accounting require us to record as assets on our financial statements both goodwill, an intangible asset that is equal to the excess of the purchase price which we pay for another company over the estimated fair value of the net assets acquired, and identifiable intangible assets such as core deposit intangibles and non-compete agreements. We evaluate our goodwill asset at least annually, or when other indicators suggest that an impairment may have occurred. We are required to reduce the carrying value of our goodwill asset through a charge to earnings if an impairment exists. Core deposit and other identifiable intangible assets are amortized to expense over their estimated useful lives and are reviewed for impairment at least annually, or whenever events or changes in circumstances indicate that the carrying amount of the asset may not be fully recoverable. The valuation techniques that we use to determine the carrying value of tangible and intangible assets acquired in acquisitions and the estimated lives of identifiable intangible assets involve estimates for discount rates, projected future cash flows and time period calculations, all of which are susceptible to change based on changes in economic conditions and other factors. Future events or changes in the estimates that we used to determine the carrying value of our goodwill and identifiable intangible assets or which otherwise adversely affect their value or estimated lives could have a material adverse impact on our results of operations. As of December 31, 2010, our intangible assets consisted of a goodwill asset of $22.6 million and core deposit intangibles of $2.7 million.

In performing its analysis, the third-party valuation firm considered three general approaches to valuation: the asset-based approach, the market approach, and the income approach. In its valuation, the third-party valuation firm used two methods within the market approach and one method within the income approach. The method utilized within the income approach was the discounted cash flow method, which relies upon the perception of a future stream of benefits, the present value of which represents the indication of value of BankFinancial FSB, the reporting unit pursuant to applicable ASC 350 guidance. The methods utilized within the market approach were the guideline public company method and guideline transaction method. The guideline public company method utilizes the pricing of guideline public companies, which in our case were publicly-traded banks and bank holding companies bearing certain similarities to the reporting unit, including asset size, geographic region, and profitability. The third-party valuation firm concluded that the fair value of the reporting unit, exceeded its carrying value as of the valuation date, and therefore, there was no impairment of our goodwill asset pursuant to the first step of the goodwill impairment test prescribed by ASC 350, Intangibles Goodwill and Other. We concurred with the methodology and the conclusion of the third-party valuation firm.

Income Taxes. We consider accounting for income taxes a critical accounting policy due to the subjective nature of certain estimates that are involved in the calculation. We use the asset/liability method of accounting for income taxes in which deferred tax assets and liabilities are established for the temporary differences between the financial reporting basis and the tax basis of our assets and liabilities. We must assess the realization of the deferred tax asset and, to the extent that we believe that recovery is not likely, a valuation allowance is established. Adjustments to increase or decrease the valuation allowance are charged or credited, respectively, to income tax expense. No valuation allowance was required at December 31, 2010. Although we have determined a valuation allowance is not required for any deferred tax assets at December 31, 2010, there is no guarantee that a valuation allowance will not be required in the future.

Statement of Financial Condition at December 31, 2010 and December 31, 2009

Total assets decreased $36.3 million, or 2.3%, to $1.531 billion at December 31, 2010, from $1.567 billion at December 31, 2009, primarily due to a $167.8 million decrease in net loans, to $1.051 billion at December 31, 2010, from $1.219 billion at December 31, 2009, partially offset by a $112.6 million increase in net cash and cash equivalents to $220.8 million at December 31, 2010, from $108.2 million at December 31, 2009.

Our loan portfolio consists primarily of investment and business loans (multi-family, nonresidential real estate, commercial, construction and land loans, and commercial leases), which together make up 75.9% of gross loans. Net loans receivable decreased $167.8 million, or 13.8%, to $1.051 billion at December 31, 2010, from $1.219 billion at December 31, 2009. Nonresidential real estate loans decreased $34.6 million, or 10.9%, primarily due to principal payments of $56.6 million, which were partially offset by $15.3 million in draws on existing credit commitments. Multi-family mortgage loans decreased by $32.3 million, or 9.8%, due in substantial part to a HUD refinancing that was completed by a related group of borrowers. Commercial loans decreased by $23.4 million, or 26.6%, due the combined impact of loan pay downs and reduced originations. Commercial leases decreased by $25.7 million, or 14.5%, as scheduled lease payments outpaced originations. Construction and land loans decreased $14.2 million, or 43.5%, primarily due to project sales and conversions to permanent amortizing loans. One-to-four family residential mortgage loans decreased $33.3 million, or 11.5%, primarily due to refinancings that were not replaced with new originations.

Our allowance for loan losses increased by $3.6 million, to $22.2 million at December 31, 2010, from $18.6 million at December 31, 2009. The increase reflects the combined impact of a $4.4 million increase in the portion of the specific allowance for loan losses that we allocate to impaired loans and $8.5 million in net charge-offs, which were partially offset by a $794,000 decrease in the general component of the allowance for loan losses. Increases in the specific portion of the allowance for loan losses occurred principally in the following areas: multi-family mortgage loans ($2.6 million); non-residential real estate loans ($131,000); commercial loans ($1.1 million); construction and land loans ($729,000); and commercial leases ($72,000). Net decreases in the specific portion of the allowance for loan losses that we allocate to impaired loans occurred for investor-owned one-to-four family residential loans ($283,000), due to the transfer of properties to other real estate owned during 2010.

Securities increased by $18.6 million, or 18.2%, to $120.7 million at December 31, 2010, from $102.1 million at December 31, 2009. The primary reason for the increase was $50.5 million in security purchases, which were partially offset by $31.8 million in principal repayments, sales and maturities of securities. In 2010, we utilized investments in FDIC insured certificates of deposit as an investment option.

We owned common stock of the FHLBC with a stated par value of $15.6 million at December 31, 2010 and 2009. The FHLBC did not declare or pay any dividends from the third quarter of 2007 through 2010. In the first quarter of 2011, the FHLBC declared and paid a cash dividend at an annualized rate of 10 basis points per share.

In late 2009, we prepaid our estimated quarterly risk-based assessments for the remainder of 2009, and for all of 2010, 2011, and 2012, pursuant to the FDIC final rule requiring the prepayment of deposit insurance assessments by insured depository institutions. At December 31, 2010, the remaining prepaid FDIC assessment was $4.8 million.

In conjunction with the sale of our Freddie Mac preferred stocks in 2009, we recorded an income tax receivable of $11.7 million at December 31, 2009. We received $11.3 million in tax refunds during 2010. Other assets increased $2.9 million to $15.1 million at December 31, 2010, from $12.2 million at December 31, 2009, primarily due to a $2.7 million increase in deferred tax assets.

Deposits increased $2.0 million, or 0.2%, to $1.235 billion at December 31, 2010, from $1.233 billion at December 31, 2009, primarily due to increased money market account, savings and noninterest-bearing demand balances. Money market accounts increased $18.9 million, or 5.9%, to $341.0 million at December 31, 2010, from $322.1 million at December 31, 2009. Savings accounts increased $2.8 million, or 2.9%, to $98.9 million at December 31, 2010, from $96.1 million at December 31, 2009, and noninterest-bearing demand accounts increased $4.2 million to $112.5 million at December 31, 2010, from $108.3 million at December 31, 2009. Total core deposits (savings, money market, noninterest-bearing demand and interest-bearing NOW accounts) increased as a percentage of total deposits, representing 69.2% of total deposits at December 31, 2010, compared to 67.3% of total deposits at December 31, 2009.

Borrowings decreased $27.0 million, or 53.2%, to $23.7 million at December 31, 2010, from $50.8 million at December 31, 2009, due to our repayments of maturing FHLBC advances.

Total stockholders equity was $253.3 million at December 31, 2010, compared to $263.6 million at December 31, 2009. The decrease in total stockholders equity was primarily due to the combined impact of our repurchase of 356,411 shares of our common stock during 2010 at a total cost of $3.1 million, and our declaration and payment of cash dividends totaling $5.9 million, the $4.3 million net loss that we recorded for 2010 and a $50,000 decrease accumulated other comprehensive income. These items were partially offset by a $3.1 million increase in total stockholders equity that resulted from the vesting of stock-based compensation and ESOP shares earned. The unallocated shares of common stock that our ESOP owns were reflected as a $14.2 million reduction to stockholders equity at December 31, 2010, compared to a $15.2 million reduction to stockholders equity at December 31, 2009.

Loans

We originate multi-family mortgage loans, nonresidential real estate loans, commercial loans, commercial leases, and construction and land loans. In addition, we originate one-to-four family residential mortgage loans and consumer loans, and purchase and sell loan participations from time-to-time. The following briefly describes our principal loan products.

Multi-family Mortgage Loans. Loans secured by multi-family mortgage loans totaled $296.9 million, or 27.7%, of our total loan portfolio, at December 31, 2010. At December 31, 2010, $73.0 million of our multi-family mortgage loan portfolio consisted of loans originated in carefully selected metropolitan markets outside the Bank s primary lending area, and these loans represented 24.6% of our multi-family mortgage loan portfolio and 6.8% of our total loan portfolio. Multi-family mortgage loans generally are secured by multi-family rental properties such as apartment buildings, including subsidized apartment units. The majority of our multi-family mortgage loans have adjustable interest rates following an initial fixed-rate period, typically between three and five years.

Nonresidential Real Estate Loans. Loans secured by nonresidential real estate totaled $282.0 million, or 26.3%, of our total loan portfolio, at December 31, 2010. We emphasize nonresidential real estate loans with initial principal balances between $1.0 million and $5.0 million. The nonresidential real estate properties securing these loans are predominantly office buildings, light industrial buildings, shopping centers and mixed-use developments, and to a lesser extent, more specialized properties such as nursing homes and other healthcare facilities. Substantially all of our nonresidential real estate loans are secured by properties located in our primary market area. Our nonresidential real estate loans are typically written as three- or five-year adjustable-rate mortgage loans or mortgage loans with balloon maturities of three or five years. Amortization of these loans is typically based on 20- to 25-year payout schedules. We also originate some 15-year fixed-rate, fully amortizing loans.

Commercial Loans. Commercial loans totaled $64.7 million, or 6.0%, of our total loan portfolio, at December 31, 2010. This total includes unsecured commercial loans with an aggregate outstanding balance of $7.8 million. We generally make commercial loans to customers in our primary market area to finance equipment acquisition, expansion, working capital and other general business purposes. The terms of these loans generally range from less than one year to five years. The loans either carry a fixed-rate or adjustable interest rates indexed to a lending rate that is either determined internally or based on a short-term market rate index.

Commercial Leases. Commercial leases totaled $151.1 million, or 14.1%, of our total loan portfolio, at December 31, 2010. Our commercial leases primarily involve technology equipment, material handling equipment, medical equipment and other capital equipment. The transactions are generally structured as a non-recourse assignment by the leasing company of the payment stream on the lease supplemented by the grant of a security interest in the lease and the leased equipment. Consequently, we underwrite leases by examining the creditworthiness of the lessee rather than the lessor. The lessee generally agrees to send the lease payments directly to us. As of December 31, 2010, 57.7% of our commercial lease portfolio involved lessees with investment-grade rated public debt, 39.9% involved publicly-traded lessees with no public debt and thus no public debt rating, and 2.4% involved privately-held lessees or lessees with a below investment-grade public debt rating. Debt ratings are determined by Moody s, Standard & Poors, Fitch, A.M. Best or an equivalent rating firm. Commercial leases typically have a maximum maturity of seven years and we limit our maximum outstanding credit exposure to $10.0 million to any single lessee. Leases to companies with no public debt ratings generally involve companies with a net worth in excess of $25.0 million and typically have a maximum maturity of five years.

Construction and Land Loans. Construction and land loans totaled $18.4 million, or 1.7%, of our total loan portfolio at December 31, 2010. These loans generally consist of land acquisition loans to help finance the purchase of land intended for further development, including single-family homes, multi-family housing and commercial income property, development loans to builders in our market area to finance improvements to real estate, consisting mostly of single-family subdivisions, typically to finance the cost of utilities, roads, sewers and other development costs. These builders generally rely on the sale of single-family homes to repay development loans, although in some cases the improved building lots may be sold to another builder, often in conjunction with development loans. In general, the maximum loan-to-value ratio for raw land acquisition loan is 65% of the appraised value of the property, and the maximum term of these loans is two years. The maximum amount loaned on a development loan is generally limited to the cost of the land and public improvements, and advances are made in accordance with a schedule reflecting the cost of the improvements. Advances are generally limited to 90% of actual construction costs and, as required by applicable regulations, a 75% loan to completed appraised value ratio. We have discouraged new construction lending for the past several years and have had only limited interest in site acquisition loans for future construction.

One-to-Four Family Residential Mortgage Lending. Conforming and non-conforming fixed-rate and adjustable-rate residential mortgage loans totaled $256.3 million, or 23.9%, of our total loan portfolio at December 31, 2010. Our residential mortgage loan portfolio includes traditional one-to-four family residential mortgage loans, home equity loans and home equity lines of credit that are secured by the borrower s primary residence, and loans to investors in non-owner-occupied single-family homes. At December 31, 2010, home equity loans totaled $9.8 million, or 0.9%, of total loans, home equity lines of credit totaled $79.7 million, or 7.4%, of total loans, and loans to investors in non-owner-occupied single-family homes totaled $76.0 million, or 7.1% of total loans. We generally originate both fixed- and adjustable-rate loans in amounts up to the maximum conforming loan limits as established by Fannie Mae, which currently is $417,000 for single-family homes in our market area. Private mortgage insurance is required for first mortgage loans with loan-to-value ratios in excess of 80%. At December 31, 2010, our adjustable-rate residential first mortgage loan portfolio totaled $129.6 million, and included $18.6 million in loans that re-price once a year and $111.0 million in loans that re-price periodically after an initial fixed-rate period of three years or more.

We also originate loans above conforming limits, referred to as jumbo loans, that are underwritten to the credit standards of Fannie Mae given the demand for these loans in the Chicago metropolitan area. We also originate loans that do not fully meet the credit standards of Fannie Mae if they are considered acceptable risks given their favorable compensating risk factors. In general, we do not originate or purchase loans with underwriting characteristics that, taken together, are materially lower than the credit standards of Fannie Mae, and as part of the underwriting process, we consider the availability of purchasers for jumbo and other nonconforming loans.

Loan Portfolio Composition

The following table sets forth the composition of our loan portfolio, excluding loans held-for-sale, by type of loan at the dates indicated.

	At December 31,									
	2010		2009		2008		2007		2006	
	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent
	(Dollars in thousands)									
One-to-four family residential	$ 256,300	23.92%	$ 289,623	23.44%	$ 312,390	24.39%	$ 345,245	27.33%	$ 397,545	29.71%
Multi-family mortgage	296,916	27.71	329,227	26.65	305,318	23.84	291,395	23.07	297,131	22.20
Nonresidential real estate	281,987	26.31	316,607	25.62	342,583	26.74	325,885	25.80	320,729	23.97
Construction and land	18,398	1.72	32,577	2.64	50,687	3.96	64,483	5.10	85,222	6.37
Commercial loans	64,679	6.04	88,067	7.13	92,679	7.23	87,777	6.95	94,305	7.05
Commercial leases	151,107	14.10	176,821	14.31	174,644	13.63	144,841	11.47	139,164	10.40
Consumer	2,182	0.20	2,539	0.21	2,655	0.21	3,506	0.28	4,045	0.30
Total loans	1,071,569	100.00%	1,235,461	100.00%	1,280,956	100.00%	1,263,132	100.00%	1,338,141	100.00%
Net deferred loan origination costs	1,377		1,701		1,912		2,086		2,424	
Allowance for loan losses	(22,180)		(18,622)		(14,746)		(11,051)		(10,622)	
Total loans, net	$ 1,050,766		$ 1,218,540		$ 1,268,122		$ 1,254,167		$ 1,329,943	

Loan Portfolio Maturities

The following table summarizes the scheduled repayments of our loan portfolio at December 31, 2010. Demand loans, loans having no stated repayment schedule or maturity and overdraft loans are reported as being due in one year or less.

	Within One Year	One Year Through Five Years	Beyond Five Years	Total
		(Dollars in thousands)		
Scheduled Repayments of Loans:				
One-to-four family residential	$ 31,866	$ 66,179	$ 158,255	$ 256,300
Multi-family mortgage	59,279	91,429	146,208	296,916
Nonresidential real estate	110,529	162,893	8,565	281,987
Construction and land	14,734	3,660	4	18,398
Commercial loans and leases	127,057	86,562	2,167	215,786
Consumer	1,025	753	404	2,182
Total loans	$ 344,490	$ 411,476	$ 315,603	$ 1,071,569

	Total
Loans Maturing After One Year:	
Predetermined (fixed) interest rates	$ 360,108
Adjustable interest rates	366,971
Total loans	$ 727,079

Past Due Loans

The following table reflects investment and business loans past due less than 90 days:

	30 - 59 Days Past Due	60 - 89 Days Past Due	Total 30 - 89 Days Past Due
		(Dollars in thousands)	
Multi-family mortgage loans	$ 8,346	$ 4,235	$ 12,581
Nonresidential real estate loans	9,331	16,244	25,575
Construction and land loans	1,260	1,268	2,528
Commercial	8,522	886	9,408
Past due investment and business loans	$ 27,459	$ 22,633	$ 50,092
Matured loans	$ 17,401	$ 12,123	$ 29,524
% of past due investment and business matured loans	63.37%	53.56%	58.94%

At December 31, 2010, multifamily, non-residential real estate, construction and development and commercial loans past due loans totaled $50.1 million. Of the $50.1 million, $29.5 million or 58.9% were Pass rated matured loans in the process of renewal and $8.4 million or 16.8% were on non-accrual status. The remaining $13.0 million or 24.5% were subject to informal collection activity to bring the loan current.

Nonperforming Loans and Assets

We review loans on a regular basis, and generally place loans on nonaccrual status when either principal or interest is 90 days or more past due. In addition, we place loans on nonaccrual status when we do not expect to receive full payment of interest or principal. Interest accrued and unpaid at the time a loan is placed on nonaccrual status is reversed from interest income. Interest payments received on nonaccrual loans are recognized in accordance with our significant accounting policies. Once a loan is placed on nonaccrual status, the borrower must generally demonstrate at least six months of payment performance before the loan is eligible to return to accrual status. We may have loans classified as 90 days or more delinquent and still accruing. Generally, we do not utilize this category of loan classification unless: (1) the loan is repaid in full shortly after the period end date; (2) the loan is well secured and there are no asserted or pending legal barriers to its collection; or (3) the borrower has remitted all scheduled payments and is otherwise in substantial compliance with the terms of the loan, but the processing of loan payments actually received or the renewal of the loan has not occurred for administrative reasons. At December 31, 2010, we had four loans totaling $818,000 in this category.

We typically obtain new third-party appraisals or collateral valuations when we place a loan on nonaccrual status or when we commence formal collection action, unless the existing valuation information for the collateral is sufficiently current to comply with the requirements of our Appraisal and Collateral Valuation Policy (ACV Policy). We also obtain new third-party appraisals or collateral valuations when the judicial foreclosure process concludes with respect to real estate collateral, and when we otherwise acquire actual or constructive title to real estate collateral. We use updated valuation information based on Multiple Listing Service data, broker opinions of value, actual sales prices of similar assets sold by us, and approved sales prices in response to offers to purchase similar assets owned by us to provide interim valuation information for financial statement and management purposes. Our ACV Policy establishes the maximum useful life of a real estate appraisal at 18 months. As of December 31, 2010, the average life of the third-party appraisals on collateral supporting the computation of ASC 310-10-35 specific valuation allowances was 12 months and the average life of the appraisals supporting the net realizable value of OREO was nine months. Because appraisals and updated valuations utilize historical or ask-side data in reaching valuation conclusions, the appraised or updated valuation may or may not reflect the actual sales price that we will receive at the time of sale.

Real estate appraisals may include up to three approaches to value: the sales comparison approach, the income approach (for income-producing property) and the cost approach. Not all appraisals utilize all three approaches. Depending on the nature of the collateral and market conditions, we may emphasize one approach over another in determining the fair value of real estate collateral. Appraisals may also contain different estimates of value based on the level of occupancy or planned future improvements. As-is valuations represent an estimate of value based on current market conditions with no changes to the use or condition of the real estate collateral. As-stabilized or as-completed valuations assume the real estate collateral will be improved to a stated standard or achieve its highest and best use in terms of occupancy. As-stabilized or as-completed valuations may be subject to a present value adjustment for market conditions or the schedule of improvements.

As part of the asset classification process, we develop an exit strategy for real estate collateral or OREO by assessing overall market conditions, the current use and condition of the asset, and its highest and best use. For most income-producing real estate, investors value most highly a stable income stream from the asset; consequently, we conduct a comparative evaluation to determine whether conducting a sale on an as-is, as-stabilized or as-improved basis is most likely to produce the highest net realizable value. If we determine that the as-stabilized or as-improved basis is appropriate, we then complete the necessary improvements or tenant stabilization tasks, with the applicable time value discount and improvement expenses incorporated into our estimates of the expected costs to sell. As of December 31, 2010, impaired real estate loans and OREO valued on an as-is basis was $27.3 million, or 74.0% of the total principal balance of impaired real estate loans, and $10.3 million, or 70.7% of the net book value of OREO.

Our estimates of the net realizable value of real estate collateral also include a deduction for the expected costs to sell the collateral or such other deductions from the cash flows resulting from the operation and liquidation of the asset as are appropriate. For most real estate collateral subject to the judicial foreclosure process, we apply a 10.0% deduction to the value of the asset to determine the expected costs to sell the asset. This estimate includes one year of real estate taxes, sales commissions and miscellaneous repair and closing costs. If we receive a purchase offer that requires unbudgeted repairs, or if the expected resolution period for the asset exceeds one year, we then include, on a case-by-case basis, the costs of the additional real estate taxes and repairs and any other material holding costs in the expected costs to sell the collateral. For OREO, we only apply a 5.0% deduction to determine the expected costs to sell, as expenses for real estate taxes and repairs are expensed when incurred.

Nonperforming Assets Summary

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

	At December 31,				
	2010	2009	2008	2007	2006
	(Dollars in thousands)				
Nonaccrual loans:					
One-to-four family residential	$ 10,059	$ 11,453	$ 2,205	$ 2,196	$ 2,212
Multi-family mortgage	13,228	13,961	2,101	4,186	1,165
Nonresidential real estate	12,428	11,074	2,961	2,823	4,378
Construction and land	6,139	8,841	5,145	988	
Commercial loans	3,766	4,160	1,141	1,751	1,419
Commercial leases	72		105	112	47
Consumer	3			2	5
Total nonaccrual loans	45,695	49,489	13,658	12,058	9,226
Other real estate owned:					
One-to-four family residential	2,770	601	588	252	
Multi-family mortgage	2,486	976	133		
Nonresidential real estate	5,835	1,416		568	
Land	1,745	1,091	234		
Total other real estate owned	12,836	4,084	955	820	
Other real estate owned in process:					
One-to-four family residential	245				
Nonresidential real estate	1,541				
Total other real estate owned	1,786				
Total nonperforming assets	$ 60,317	$ 53,573	$ 14,613	$ 12,878	$ 9,226
Ratios:					
Nonperforming loans to total loans	4.26%	4.01%	1.07%	0.95%	0.69%
Nonperforming assets to total assets	3.94	3.42	0.94	0.87	0.57

Loans on Nonaccrual Status

At December 31, 2010, nonaccrual loans declined slightly due principally to transfers of loans to OREO and resolutions of pending cases. The decline was partially offset by isolated increases in nonaccrual loans in the commercial real estate and commercial lease categories. Nonaccrual loans decreased by $3.8 million to $45.7 million at December 31, 2010, from $49.5 million at December 31, 2009. For the year ended December 31, 2010, no accrued interest on nonaccrual loans had been recognized.

At December 31, 2010, our total non-performing loans involved 105 borrower relationships, or an average of $435,000 loan per borrower relationship. Therefore, there are no specific concentrations of credit risk such that a majority of loans involves only a few borrower relationships. Our three largest non-performing borrower relationships represent 31.9% of total non-performing loans. These loans are briefly described as follows:

We have a $5.8 million nonperforming loan that is secured by a retail shopping center located in our primary Chicago metropolitan market. As of December 31, 2010, this loan was on nonaccrual status and had a $787,000 specific valuation allowance that was based on an updated as improved third party appraisal. The shopping center is 92% occupied by businesses that are affiliated with investors in the entity that owns the shopping center. The loan is further secured by additional collateral pledged by the investors, and is supported by the personal guarantees of the investors. The business operations of the existing tenants of the shopping center, together with the supplementary personal resources of the guarantors, were not sufficient to comply with the planned payment schedule of principal and interest. Accordingly, pursuant to applicable regulatory guidance, future renewals of the loan will be classified as a troubled debt restructuring (TDR), and the loan will remain on nonaccrual status until the borrower s business operations demonstrate the capability to sustain at least six months of debt service on a fully amortizing basis.

We have a $4.4 million nonperforming loan that is secured by a 242-unit multifamily residential building located outside of our primary Chicago metropolitan market. This loan is included in our Wholesale Commercial Lending category of loans. As of December 31, 2010, this loan was on nonaccrual status and had a $1.5 million specific valuation allowance that was based on an updated as improved third-party appraisal. The borrower initially filed a Chapter 11 bankruptcy petition, but the bankruptcy case was recently dismissed. A court-appointed receiver is now in place. We recently received two separate offers to purchase this property for prices in excess of our net book value, and tentatively expect this matter to be fully resolved in 2011.

We have a $4.4 million credit exposure to a single borrower, that is secured by a completed single-family residence that the borrower constructed for the purposes of sale, a parcel of vacant land, and the borrower s personal residence. All of the real estate collateral is located in our primary Chicago metropolitan market. As of December 31, 2010, the loans were on nonaccrual status and had a $1.2 million specific valuation allowance based on updated as is third-party appraisals. The Bank has been appointed mortgagee-in-possession of the completed single family residence, and the pending foreclosure action is expected to conclude in 2011.

Other Real Estate Owned or In Process

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

	Balance at December 31, 2009	Additions	Write-downs	Charge-Offs	Sale	Balance at December 31, 2010
			(Dollars in thousands)			
Other real estate owned and in process:						
One-to-four family residential	$ 601	$ 3,777	$ (1,196)	$	$ (167)	$ 3,015
Multi-family mortgage	976	5,037	(609)	(51)	(2,867)	2,486
Nonresidential real estate	1,416	7,219	(407)		(852)	7,376
Land	1,091	1,404	(84)	(45)	(621)	1,745
Total other real estate owned and in process	$ 4,084	$ 17,437	$ (2,296)	$ (96)	$ (4,507)	$ 14,622

As discussed above, the appraised value of real estate assets may or may not reflect the actual sales price that will be received. We market real estate for sale based on our estimate of its net realizable value. Depending on the levels of market interest received during the initial period of market exposure, we may reduce the offering price in subsequent periods; if we do so, the new offering price becomes the new net realizable value. We may also accept an offer to purchase a given real estate asset at a price below the net realizable value if there has been limited interest at the original offering price and we conclude that further market exposure time (even at a price lower than the current offering price but higher than the proposed actual sales price) will not produce materially better results given the holding costs and management risks incurred over time.

Loan Extensions and Modifications

Maturing loans are subject to our standard loan underwriting policies and practices. Due to the need to obtain updated borrower and guarantor financial information, collateral information or to prepare revised loan documentations, loans in the process of renewal may appear as past due because the information needed to underwrite a renewal of the loan is not available to us prior to the maturity date of the loan. At times, short-term administrative extensions, which are typically 90 days in duration, are granted to facilitate proper underwriting. In general, loan modifications are subject to a risk-adjusted pricing analysis. We do not grant loan modification requests that involve below-market interest rates. Other than split-note restructurings conducted in conformance with applicable Federal Financial Institutions Examination Council (FFIEC) workout guidance, we do not grant loan modifications that involve principal concessions. We also do not grant loan modifications that suspend all loan payments for any period; however, we may grant loan modifications that involve the short-term suspension of principal amortization payments. Typically, we grant loan modifications for three to six month periods, at the conclusion of which the loan will either mature or return in all material respects to its original terms and conditions. During 2010, the Bank conducted thirteen commercial loan modifications to eight borrowers totaling $7.1 million (or 0.66% of total loans as of December 31, 2010) that did not qualify as troubled debt restructurings due to the fact that no concessions were made to the borrowers other than those which we would grant in the ordinary course of business. The modifications involved actions such as reducing an above-market interest rate to a market interest rate or extending a shorter-duration amortization period to a longer amortization period that remained in compliance with our normal underwriting standards. We also conducted loan modifications to four residential borrowers with a total exposure of $410,296. These modifications generally involved the repayment of past due principal and/or interest loan payments over a three- to six-month period of time, in exchange for a forbearance of our legal remedies.

When appropriate, we evaluate loan extensions or modifications in accordance with ASC 310-40 and related federal regulatory guidance concerning TDRs and the FFIEC workout guidance to determine the required treatment for nonaccrual status and risk classification purposes. In general, if we grant a loan modification or extension that involves either the absence of principal amortization (other than for revolving lines of credit which are customarily granted on interest-only terms), or if we grant a material extension of an existing loan amortization period in excess of our underwriting standards, the loan will be placed on nonaccrual status and impairment testing conducted to determine whether a specific valuation allowance or loss classification / charge-off is required. If the loan is well secured by an abundance of collateral and the collectability of both interest and principal is probable, the loan may remain on accrual status, but it will be classified as a TDR due to the concession made in the loan principal amortization payment component. A loan in full compliance with the payment requirements specified in a loan modification will not be considered as past due, but may nonetheless be placed on nonaccrual status or be classified as a TDR, as appropriate under the circumstances.

In accordance with the FFIEC workout guidance, the resulting A promissory note in a split-note restructuring will be considered a TDR at the time of the restructuring and will remain so classified for at least 12 months. The resulting B note will be either placed on nonaccrual status or charged-off and any payments on the B promissory note will be treated as a recovery of principal unless the note is fully collateralized pursuant to our underwriting standards and we believe that the collection of both the principal and interest of the B note is probable.

Troubled Debt Restructurings

The following table sets forth the troubled debt restructurings by loan category as of December 31,

	2010	2009
	(dollars in thousands)	
Multi-family mortgage	$ 1,675	$
Nonresidential real estate	1,699	7,406
Troubled debt restructured loans accrual loans	3,374	7,406
Multi-family mortgage	13	
Nonresidential real estate	3,137	2,152
Troubled debt restructured loans nonaccrual loans	3,150	2,152
Total troubled debt restricted loans	$ 6,524	$ 9,558

TDR loans decreased $3.0 million in 2010. Total loans classified as TDRs represented 0.61% of the total loans at December 31, 2010.

Of the $6.5 million in loans that were classified as TDRs at December 31, 2010, 52% were on accrual status and continued to perform according to the terms of the applicable loan agreements. Of the $9.6 million in loans that were classified as TDRs at December 31, 2009, $7.4 million, or 77%, remained on accrual status as of that date. Subsequently, approximately 50% of the TDRs that were on accrual status at December 31, 2009 were placed on nonaccrual status during 2010 due principally to an inability of the borrowers to continue debt service on a fully-amortizing basis.

Risk Classification of Assets

Our policies, consistent with regulatory guidelines, provide for the classification of loans and other assets that are considered to be of lesser quality as substandard, doubtful, or loss assets, or designated as special mention.

An asset is considered substandard if it is inadequately protected by the current net worth and paying capacity of the obligor or the collateral for the loan, if any. Substandard assets include those characterized by the distinct possibility that we will sustain some loss if the deficiencies are not corrected. Assets classified as doubtful have all of the weaknesses inherent in assets classified as substandard with the added characteristic that the weaknesses present also make collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable and improbable. Assets classified as loss are those considered uncollectible and of such little value that their continuance as assets is not warranted; such balances are promptly charged-off as required by applicable federal regulations. An asset designated as special mention has potential weaknesses that deserve close attention and, if left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the asset or in the institution s credit position with respect to the asset at some future date. Assets designated special mention assets are not adversely classified and do not expose an institution to sufficient risk to warrant adverse classification.

Based on a review of our assets at December 31, 2010, classified assets consisted of substandard assets of $60.4 million, doubtful assets of $477,000, and no loans classified as loss assets. As of December 31, 2010, we had $25.9 million of assets designated as special mention.

Allowance for Loan Losses

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

We provide for loan losses based on the allowance method. Accordingly, all loan losses are charged to the related allowance and all recoveries are credited to it. Additions to the allowance for loan losses are provided by charges to income based on various factors that, in our judgment, deserve current recognition in estimating probable incurred credit losses. We review the loan portfolio on an ongoing basis and make provisions for loan losses on a quarterly basis to maintain the allowance for loan losses in accordance with accounting principles generally accepted in the United States of America. The allowance for loan losses consists of two components:

- specific allowances established for any impaired residential owner or non-owner occupied mortgage, multi-family mortgage, nonresidential real estate, construction and land, commercial, and commercial lease loans for which the recorded investment in the loan exceeds the measured value of the loan; and

- general allowances for loan losses for each loan class based on historical loan loss experience; and adjustments to historical loss experience (general allowances), maintained to cover uncertainties that affect our estimate of probable incurred credit losses for each loan class.

The adjustments to historical loss experience are based on our evaluation of several factors, including levels of, and trends in, past due and classified loans; levels of, and trends in, charge-offs and recoveries; trends in volume and terms of loans, including any credit concentrations in the loan portfolio; experience, ability, and depth of lending management and other relevant staff; and national and local economic trends and conditions.

We evaluate the allowance for loan losses based upon the combined total of the specific and general components. Generally, when the loan portfolio increases, absent other factors, the allowance for loan loss methodology results in a higher dollar amount of estimated probable incurred credit losses than would be the case without the increase. Conversely, when the loan portfolio decreases, absent other factors, the allowance for loan loss methodology generally results in a lower dollar amount of estimated probable losses than would be the case without the decrease.

We review our loan portfolio on an ongoing basis to determine whether any loans require classification and impairment testing in accordance with applicable regulations and accounting principles. When we classify loans as either substandard or doubtful and in certain other cases, we review the collateral and future cash flow projections to determine if a specific reserve is necessary. The allowance for loan losses represents amounts that have been established to recognize incurred credit losses in the loan portfolio that are both probable and reasonably estimable at the date of the financial statements. When we classify problem loans as loss, we charge-off such amounts.

We refined the calculation of the general component of the allowance for loan losses during the fourth quarter of 2010 in response to the new FASB disclosure requirement to segment each loan portfolio category into specific loan classes (FASB Standards Update 2010-20 (ASU 210-20), Receivables (Topic 310): Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses). Loan class segmentation tables are presented in Note 4 Loans Receivable of the Consolidated Financial Statements. As a matter of consistency, the loan class segmentation was also applied within the 12-quarter loss history used to calculate the general component of the allowance for loan losses, an adjustment of the inherent risk factor weightings based on our evaluation of their relevance to the new loan classes, and the elimination of duplicative historical loss factors as a result of the segmentation of the portfolio by class. These refinements were applied to the loan balances, net of impaired loans, to calculate a $12.8 million general component of our allowance for loan losses at December 31, 2010. The refinements resulted in a net reduction of $1.7 million to the general component of our allowance for loan losses at December 31, 2010, principally due to the establishment of loan class segments that had lower historical loss ratios than the general loan categories to which they belong. Specifically, the refinements reduced the portion of the general component of the allowance for loan losses attributable to commercial leases by $908,000, the portion attributable to commercial loans by $788,000, the portion attributable to non-residential real estate loans by $195,000, and the portion attributable to multi-family mortgage loans by $144,000. These reductions were partially offset by a $384,000 increase in the portion of the general component of the allowance for loan losses that is attributable to one-to-four family mortgage loans.

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While we use the best information available to make evaluations, future adjustments to the allowance may become necessary if conditions differ substantially from the information that we used in making the evaluations. Our determinations as to the risk classification of our loans and the amount of our allowance for loan losses are subject to review by our regulatory agencies, which can require that we establish additional loss allowances.

Net Charge-offs and Recoveries

The following table sets forth activity in our allowance for loan losses for the years indicated.

	At or For the Years Ended December 31,				
	2010	2009	2008	2007	2006
	(Dollars in thousands)				
Balance at beginning of year	$ 18,622	$ 14,746	$ 11,051	$ 10,622	$ 11,514
Charge-offs:					
One-to-four family residential	(2,292)	(461)	(248)	(10)	
Multi-family mortgage	(2,385)	(297)	(169)		
Nonresidential real estate	(2,897)	(1,518)	(605)		
Construction and land	(525)	(2,262)	(115)		
Commercial loans	(1,174)	(463)	(130)	(237)	(946)
Commercial leases		(22)			
Consumer	(16)	(42)	(146)	(58)	(26)
Total charge-offs	(9,289)	(5,065)	(1,413)	(305)	(972)
Recoveries:					
One-to-four family residential	69	82	1		
Multi-family mortgage	3				
Nonresidential real estate	633	36	4		
Construction and land	58				
Commercial loans	1	3	1	14	
Commercial leases		6			
Consumer		3	10	23	4
Total recoveries	764	130	16	37	4
Net charge-offs	(8,525)	(4,935)	(1,397)	(268)	(968)
Allowance of acquired bank					212
Provision (credit) for loan losses	12,083	8,811	5,092	697	(136)
Balance at end of year	$ 22,180	$ 18,622	$ 14,746	$ 11,051	$ 10,622
Ratios:					
Net charge-offs to average loans outstanding	0.75%	0.39%	0.11%	0.02%	0.07%
Allowance for loan losses to nonperforming loans	48.54	37.63	107.97	91.65	115.13
Allowance for loan losses to total loans	2.07	1.51	1.15	0.87	0.79

Net charge-offs and total charge-offs were $8.5 million and $9.3 million, respectively, for the year ended December 31, 2010, compared to $4.9 million in net charge-offs and $5.1 million in total charge-offs for the year ended December 31, 2009, and $1.4 million in net charge-offs and total charge-offs for the year ended December 31, 2008. Total recoveries were $764,000 in 2010, compared to $130,000 in 2009 and $16,000 in 2008.

We recorded a provision for loan losses of $12.1 million in 2010, compared to $8.8 million in 2009 and $5.1 million in 2008. Of the $12.1 million provision for loan losses that we recorded in 2010, $4.4 million is attributable to the specific portion of the allowance for loan losses that we allocate to impaired loans and $8.5 million in charge-offs, which were partially offset by a $794,000 decrease in the general portion of the allowance for loan losses.

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

Included in 2010 charge-offs of $9.3 million were $3.3 million in charge-offs related to final disposition of collateral or other loan resolutions, of which $1.7 million occurred in the fourth quarter 2010. $6.0 million of charge-offs recorded at the time real estate transferred to other real estate owned, of which $3.8 million occurred in the fourth quarter 2010.

Allocation of Allowance for Loan Losses

The following table sets forth our allowance for loan losses allocated by loan category. The allowance for loan losses allocated to each category is not necessarily indicative of future losses in any particular category and does not restrict the use of the allowance to absorb losses in other categories.

	At December 31,								
	2010			2009			2008		
	Allowance for Loan Losses	Loan Balances by Category	Percent of Loans in Each Category to Total Loans	Allowance for Loan Losses	Loan Balances by Category	Percent of Loans in Each Category to Total Loans	Allowance for Loan Losses	Loan Balances by Category	Percent of Loans in Each Category to Total Loans
	(Dollars in thousands)								
One-to-four family residential	$ 3,556	$ 256,300	23.92%	$ 3,333	$ 289,623	23.44%	$ 2,040	$ 312,390	24.39%
Multi-family mortgage	7,032	296,916	27.71	3,597	329,227	26.65	2,370	305,318	23.84
Nonresidential real estate	5,714	281,987	26.31	5,696	316,607	25.62	4,659	342,583	26.74
Construction and land	2,461	18,398	1.72	1,861	32,577	2.64	1,899	50,687	3.96
Commercial loans	2,879	64,679	6.04	2,520	88,067	7.13	2,058	92,679	7.23
Commercial leases	518	151,107	14.10	1,591	176,821	14.31	1,668	174,644	13.63
Consumer	20	2,182	0.20	24	2,539	0.21	52	2,655	0.21
Total	$ 22,180	$ 1,071,569	100.00%	$ 18,622	$ 1,235,461	100.00%	$ 14,746	$ 1,280,956	100.00%

	At December 31,					
	2007			2006		
	Allowance for Loan Losses	Loan Balances by Category	Percent of Loans in Each Category to Total Loans	Allowance for Loan Losses	Loan Balances by Category	Percent of Loans in Each Category to Total Loans
	(Dollars in thousands)					
One-to-four family residential	$ 1,823	$ 345,245	27.33%	$ 1,855	$ 397,545	29.71%
Multi-family mortgage	2,206	291,395	23.07	1,908	297,131	22.20
Nonresidential real estate	3,055	325,885	25.80	2,846	320,729	23.97
Construction and land	937	64,483	5.10	1,120	85,222	6.37
Commercial loans	1,799	87,777	6.95	1,741	94,305	7.05
Commercial leases	1,174	144,841	11.47	1,112	139,164	10.40
Consumer	57	3,506	0.28	40	4,045	0.30
Total	$ 11,051	$ 1,263,132	100.00%	$ 10,622	$ 1,338,141	100.00%

Securities

Our investment policy is established by our Board of Directors. The policy emphasizes safety of the investment, liquidity requirements, potential returns, cash flow targets, and consistency with our interest rate risk management strategy.

At December 31, 2010, our mortgage-backed securities and collateralized mortgage obligations (CMOs) reflected in the following table were issued by U.S. government-sponsored enterprises and agencies, Freddie Mac, Fannie Mae and Ginnie Mae, and are obligations which the federal government has affirmed its commitment to support. The equity securities reflected in the 2008 columns in the table consist of Freddie Mac preferred stocks. All securities reflected in the table were classified as available-for-sale at December 31, 2010, 2009 and 2008.

We hold the FHLBC common stock to qualify for membership in the Federal Home Loan Bank System and to be eligible to borrow funds under the FHLBC s advance program. The aggregate cost of our FHLBC common stock as of December 31, 2010 was $15.6 million based on its par value. There is no market for FHLBC common stock. Due to our receipt of stock dividends in prior years and the amount of our outstanding FHLBC advances, we owned shares of FHLBC common stock at December 31, 2010 with a par value that was $9.0 million more than we were required to own to maintain our membership in the Federal Home Loan Bank System and to be eligible to obtain advances (excess or voluntary capital stock).

The following table sets forth the composition, amortized cost and fair value of our securities at the dates indicated.

	At December 31,					
	2010		2009		2008	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value	Amortized Cost	Fair Value
	(Dollars in thousands)					
Securities:						
Certificate of deposits	$ 27,766	$ 27,766	$	$	$ 500	$ 500
Municipal securities	675	709	1,225	1,303	1,735	1,811
SBA guaranteed loan participation certificates	103	105	114	115	131	125
Equity securities:						
Freddie Mac					2,356	353
Total	28,544	28,580	1,339	1,418	4,722	2,789
Mortgage-backed Securities:						
Mortgage-backed securities - residential	41,034	42,435	33,008	34,057	41,865	41,976
CMOs and REMICs - residential	48,262	49,732	64,791	66,651	79,425	80,154
Total mortgage-backed securities	89,296	92,167	97,799	100,708	121,290	122,130
Total	$ 117,840	$ 120,747	$ 99,138	$ 102,126	$ 126,012	$ 124,919

The fair values of marketable equity securities are generally determined by quoted prices, in active markets, for each specific security. If quoted market prices are not available for a marketable equity security, we determine its fair value based on the quoted price of a similar security traded in an active market. The fair values of debt securities are generally determined by matrix pricing, which is a mathematical technique widely used in the industry to value debt securities without relying exclusively on quoted prices for the specific securities, but rather by relying on the securities relationship to other benchmark quoted securities. The fair value of a security is used to determine the amount of any unrealized losses that must be reflected in our other comprehensive income and the net book value of our securities.

We evaluate marketable investment securities with significant declines in fair value on a quarterly basis to determine whether they should be considered other-than-temporarily impaired under current accounting guidance, which generally provides that if a marketable security is in an unrealized loss position, whether due to general market conditions or industry or issuer-specific factors, the holder of the securities must assess whether the impairment is other-than-temporary.

We also periodically evaluate our FHLBC common stock, which is not a marketable investment security, for impairment in accordance with Statement of Position (SOP) 01-6 (ASC 942-325-35), Accounting by Certain Entities (Including Entities with Trade Receivables) that lend to or Finance the Activities of Others. SOP 01-6 provides that when evaluating FHLB stock for impairment, its value should be determined based on the ultimate recovery of its par value rather than by recognizing temporary declines in value.

The FHLBC is subject to a cease and desist order issued by the FHFA, in 2007. Among other things, the cease and desist order requires the FHLBC to submit a capital plan to the FHFA, prohibits certain capital stock repurchases and stock redemptions, including certain redemptions upon membership withdrawal, without the prior approval of the Director, and prohibits the payments of dividends without the prior approval of the Director. The FHLBC has reported that it has submitted a capital plan to the Director but that it has not yet been approved. The FHLBC did not pay any dividends from the third quarter of 2007 through 2010, but in the first quarter of 2011, paid a nominal cash dividend at an annualized rate of 10 basis points per share. The FHLBC reported in February 2011 that it had earnings of net income of $366 million for 2010, compared to a net loss of $65 million in 2009, and that it is compliance with its regulatory capital requirements.

We considered the above evidence in accordance with SOP 01-6 and concluded that it is probable that its par value is ultimately recoverable based on the FHLBC s current compliance with its regulatory capital requirements, the net income that it reported for 2010, its receipt of approval from the Director to pay a dividend in the first quarter of 2011 and published reports indicating that it is continuing to work with the FHFA to finalize a capital plan.

Portfolio Maturities and Yields

The composition and maturities of the securities portfolio and the mortgage-backed securities portfolio at December 31, 2010 are summarized in the following table. Maturities are based on the final contractual payment dates, and do not reflect the impact of prepayments or early redemptions that may occur. Municipal securities yields have not been adjusted to a tax-equivalent basis, as the amount is immaterial.

	One Year or Less		More than One Year through Five Years		More than Five Years through Ten Years		More than Ten Years		Total Securities		
	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Amortized Cost	Weighted Average Yield	Fair Value
					(Dollars in thousands)						
Mortgage-backed Securities:											
Pass-through securities:											
Fannie Mae	$	%	$ 178	4.50%	$ 946	5.87%	$ 19,359	3.24%	$ 20,483	3.37%	$ 21,579
Freddie Mac			98	3.13	581	2.11	4,546	5.05	5,225	4.69	5,512
Ginnie Mae							15,326	2.34	15,326	2.34	15,344
CMOs and REMICs					154	3.11	48,108	4.09	48,262	4.08	49,732
Total			276	4.02	1,681	4.32	87,339	3.64	89,296	3.66	92,167
Securities:											
Certificates of deposit	22,712	0.58	5,054	0.74					27,766	0.61	27,766
Municipal securities	160	4.15	515	4.47					675	4.39	709
SBA guaranteed loan participation certificates					103	1.75			103	1.75	105
Total	22,872	0.60	5,569	1.09	103	1.75			28,544	0.70	28,580
Total securities	$ 22,872	0.60%	$ 5,845	1.22%	$ 1,784	4.17%	$ 87,339	3.64%	$ 117,840	2.94%	$ 120,747

Sources of Funds

Deposits. At December 31, 2010, our deposits totaled $1.235 billion. Interest-bearing deposits totaled $1.123 billion and noninterest-bearing demand deposits totaled $112.5 million. NOW, savings and money market accounts totaled $742.8 million. Noninterest-bearing demand deposits at December 31, 2010 included $6.0 million in internal checking accounts, such as accounts for Bank cashier s checks and money orders. At December 31, 2010, we had $380.1 million of certificates of deposit outstanding, of which $271.2 million had maturities of one year or less. Although we have a significant portion of our deposits in shorter-term certificates of deposit, we believe, based on historical experience and our current pricing strategy, that we will retain a significant portion of these accounts upon maturity.

We originate deposits predominantly from the areas where our branch offices are located. We rely on our favorable locations, customer service, competitive pricing, our Internet Branch and related deposit services such as cash management to attract and retain these deposits. While we accept certificates of deposit in excess of the FDIC s deposit insurance limits, we generally do not solicit such deposits because they are more difficult to retain than core deposits and at times are more costly than brokered deposits.

The following table sets forth the distribution of total deposit accounts, by account type, for the periods indicated.

	Years Ended December 31,								
	2010			2009			2008		
	Average Balance	Percent	Weighted Average Rate	Average Balance	Percent	Weighted Average Rate	Average Balance	Percent	Weighted Average Rate
	(Dollars in thousands)								
Non-interest bearing demand:									
Retail	$ 26,308	2.11%	%	$ 28,058	2.39%	%	$ 25,617	2.45%	%
Commercial	75,986	6.08		77,279	6.55		79,099	7.53	
Total non-interest bearing demand	102,294	8.19		105,337	8.94		104,716	9.98	
Savings deposits	98,338	7.87	0.43	97,187	8.24	0.51	98,171	9.35	0.73
Money market accounts	347,250	27.81	0.94	270,583	22.94	1.66	210,857	20.08	2.56
Interest-bearing NOW accounts	295,720	23.68	0.49	284,583	24.13	0.77	311,886	29.71	1.55
Certificates of deposit	405,188	32.45	1.78	421,640	35.75	2.69	324,239	30.88	3.42
Total deposits	$ 1,248,790	100.00%		$ 1,179,330	100.00%		$ 1,049,869	100.00%	

The following table sets forth certificates of deposit by time remaining until maturity at December 31, 2010.

	Maturity				
	3 Months or Less	Over 3 to 6 Months	Over 6 to 12 Months	Over 12 Months	Total
	(Dollars in thousands)				
Certificates of deposit less than $100,000	$ 52,472	$ 51,449	$ 75,817	$ 63,346	$ 243,084
Certificates of deposit of $100,000 or more	23,728	26,132	41,645	45,485	136,990
Total certificates of deposit	$ 76,200	$ 77,581	$ 117,462	$ 108,831	$ 380,074

Borrowings. Our borrowings consist primarily of Federal Home Loan Bank advances and repurchase agreements. The following table sets forth information concerning balances and interest rates on our borrowings at the dates and for the periods indicated.

	At or For the Years Ended December 31,		
	2010	2009	2008
	(Dollars in thousands)		
Balance at end of year	$ 23,749	$ 50,784	$ 200,350
Average balance during year	37,653	101,785	110,039
Maximum outstanding at any month end	50,384	141,970	200,350
Weighted average interest rate at end of year	2.00%	2.44%	1.33%
Average interest rate during year	2.27%	2.02%	3.30%

At December 31, 2010, we had the capacity to borrow an additional $240.5 million under our credit facilities with the FHLBC. Furthermore, we had unpledged securities that could be used to support in excess of $71.4 million of additional FHLBC borrowings.

At December 31, 2010, we had a pre-approved overnight federal funds borrowing capacity of $28.0 million and a line of credit with the Federal Reserve Bank of Chicago for $425,000. At December 31, 2010, there were no outstanding federal funds borrowings and there was no outstanding balance on the line of credit.

Statement of Operating Results for the Years Ended December 31, 2010, 2009 and 2008

Net Income

Comparison of Year 2010 to 2009. We recorded a net loss of $4.3 million for the year ended December 31, 2010, compared to net loss of $738,000 for the year ended December 31, 2009. The net loss for 2010 was attributable in substantial part to the combined impact of a $12.1 million provision for loan losses and $7.3 million for nonperforming asset management expense and operations of other real estate owned. The 2009 results included an $8.8 million provision for loan losses and a $401,000 loss on impairment of securities. The impact of these items in 2009 was partially offset by a $1.3 million gain that we recognized on the sale of our merchant processing operations. Our loss per share of common stock for year ended December 31, 2010 was $0.22 per share, compared to $0.04 per share for the year ended December 31, 2009.

Comparison of Year 2009 to 2008. We recorded a net loss of $738,000 for the year ended December 31, 2009, compared to net loss of $19.4 million for the year ended December 31, 2008. The net loss for 2009 was attributable in substantial part to the combined impact of an $8.8 million provision for loan losses, a $401,000 pre-tax impairment loss on our Freddie Mac preferred stocks, and a $998,000 pre-tax loss that we recognized upon the subsequent sale of these securities. In addition, we recorded a $2.2 million expense, compared to $162,000 in 2008, for FDIC quarterly and special assessments in 2009 due to the combined effect of the FDIC s increase in its quarterly assessment rate, the FDIC s imposition of a special assessment against all insured depository institutions and the full utilization of the FDIC assessment credits that we previously had available to offset or reduce FDIC quarterly assessments. The impact of these items was partially offset by a $1.3 million gain that we recognized on the sale of our merchant processing operations in 2009. The net loss for 2008 was primarily due to a $35.9 million pre-tax impairment loss that we recorded on our Freddie Mac preferred stocks. Our loss per share of common stock for year ended December 31, 2009 was $0.04 per share, compared to a loss of $0.98 per share for the year ended December 31, 2008.

Net Interest Income

Comparison of Year 2010 to 2009. Net interest income decreased by $1.8 million, or 3.4%, to $51.8 million for the year ended December 31, 2010, from $53.6 million for the year ended December 31, 2009. Our net interest rate spread remained at 3.36% for the years ended December 31, 2010 and 2009. Our net interest margin decreased by 12 basis points to 3.57% for the year ended December 31, 2010, from 3.69% for the year ended December 31, 2009. Our average interest-earning assets remained at $1.451 billion for the year ended 2010 and 2009, and our average interest-bearing liabilities increased $8.4 million to $1.184 billion in 2010, from $1.176 billion in 2009.

Interest income decreased by $9.2 million, or 12.4%, to $64.9 million for the year ended December 31, 2010, from $74.1 million for the year ended December 31, 2009. The decrease in interest income resulted primarily from a 64 basis point decrease in the average yield on interest earning assets to 4.47% for the year ended December 31, 2010, from 5.11% for the year ended December 31, 2009, and a decrease in average loans receivable.

Interest income on loans, the most significant portion of interest income, decreased by $8.2 million, or 11.9%, to $60.9 million for the year ended December 31, 2010, from $69.2 million for the year ended December 31, 2009. The average yield on loans decreased 10 basis points to 5.34% for the year ended December 31, 2010, from 5.44% for the year ended December 31, 2009. Interest income on loans and the average yield on loans were impacted by a $130.2 million, or 10.2%, decrease in average loans receivable to $1.141 billion for the year ended December 31, 2010, from $1.271 billion for the year ended December 31, 2009, and a net increase of $381,000 in the reserve for uncollected interest relating to loans that were placed on nonaccrual status during the year ended December 31, 2010.

Interest income on securities decreased $1.3 million, or 27.6%, to $3.5 million for the year ended December 31, 2010, from $4.8 million for the year ended December 31, 2009. The decrease in interest income on securities was due in substantial part to a $26.6 million, or 23.6%, decrease in the average balance of securities to $86.0 million for the year ended December 31, 2010, from $112.7 million for the year ended December 31, 2009. The average yield on securities decreased by 23 basis points to 4.05% for the year ended December 31, 2010, from 4.28% for the year ended December 31, 2009.

The FHLBC did not pay dividends on its common stock in 2010 or 2009.

Interest income on interest-bearing deposits in other financial institutions increased $399,000 to $522,000 for the year ended December 31, 2010, from $123,000 for the year ended December 31, 2009. The increase was primarily due to a $156.7 million increase in the average balance of our interest bearing deposits in other financial institutions to $208.7 million for the year ended December 31, 2010, from $52.0 million for the year ended December 31, 2009. The average yield on our interest-bearing deposits in other financial institutions increased one basis point to 0.25% for the year ended December 31, 2010, from 0.24% for the year ended December 31, 2009.

Interest expense decreased by $7.4 million, or 35.9%, to $13.2 million for the year ended December 31, 2010, from $20.6 million for the year ended December 31, 2009, representing a decrease in both interest expense on deposits and interest expense on borrowings.

Interest expense on deposits decreased by $6.2 million, or 33.3%, to $12.3 million for the year ended December 31, 2010, from $18.5 million for the year ended December 31, 2009. The decrease in interest expense on deposits was primarily due to a 64 basis point decrease in the average rates paid on deposits, which was partially offset by a $72.5 million, or 6.8%, net increase in the average balance of deposits. The average cost of deposits was 1.08% for the year ended December 31, 2010, compared to 1.72% for the year ended December 31, 2009. The average rate paid on savings accounts decreased eight basis points to 0.43% from 0.51%. On a year over year basis, the average cost of money market accounts decreased 72 basis points to 0.94%, from 1.66%, the average cost of NOW accounts decreased 28 basis points to 0.49%, from 0.77%, and the average cost of certificates of deposit decreased 91 basis points to 1.78% from 2.69%. The average balances of money market accounts increased $76.7 million, or 28.3%, the average balance of NOW accounts increased $11.1 million, or 3.9%, and the average balance of savings accounts increased $1.2 million, or 1.2% for the year ended December 31, 2010. These increases were partially offset by a decrease in the average balances of certificates of deposit of $16.5 million, or 3.9% for the year ended December 31, 2010.

Interest expense on borrowings decreased by $1.2 million, or 58.5%, to $853,000 for the year ended December 31, 2010, from $2.1 million for the year ended December 31, 2009. This decrease was due in substantial part to a decrease in the average balance of borrowings of $64.1 million, or 63.0%, to $37.7 million at December 31, 2010, from $101.8 million at December 31, 2009. The decrease was partially offset by a 25 basis point increase in the average cost of borrowings to 2.27% for the year ended December 31, 2010, from 2.02% for the year ended December 31, 2009.

Comparison of Year 2009 to 2008. Net interest income increased by $1.3 million, or 2.4%, to $53.6 million for the year ended December 31, 2009, from $52.3 million for the year ended December 31, 2008. Our net interest rate spread improved by one basis point to 3.36% for the year ended December 31, 2009, from 3.35% for the year ended December 31, 2008. Our net interest margin decreased by 19 basis points to 3.69% for the year ended December 31, 2009, from 3.88% for the year ended December 31, 2008. Our average interest-earning assets increased $102.2 million to $1.451 billion in 2009, from $1.349 billion in 2008, and our average interest-bearing liabilities increased $120.6 million to $1.176 billion in 2009, from $1.055 billion in 2008.

Interest income decreased by $3.9 million, or 5.0%, to $74.0 million for the year ended December 31, 2009, from $78.0 million for the year ended December 31, 2008. The decrease in interest income resulted primarily from a 68 basis point decrease in the average yield on interest earning assets to 5.10% for the year ended December 31, 2009, from 5.78% for the year ended December 31, 2008. This decrease was partially offset by a $102.2 million increase in total average interest-earning assets to $1.451 billion for the year ended December 31, 2009, from $1.349 billion for the year ended December 31, 2008.

Interest income on loans, the most significant portion of interest income, decreased by $4.8 million, or 6.5%, to $69.2 million for the year ended December 31, 2009, from $74.0 million for the year ended December 31, 2008. Interest income on loans and the average yield on loans were reduced by a net increase of $1.7 million in the reserve for uncollected interest that we established for loans that were placed on nonaccrual status during the year ended December 31, 2009. This increase accounts for 34.4% of the decrease in interest income from loans. In addition, the average yield on loans decreased 52 basis points to 5.44% for the year ended December 31, 2009, from 5.96% for the year ended December 31, 2008. These decreases were partially offset by a $29.5 million, or 2.4%, increase in the average balance of loans outstanding to $1.271 billion for the year ended December 31, 2009, from $1.242 billion for the year ended December 31, 2008.

Interest income on securities increased $955,000, or 24.7%, to $4.8 million for the year ended December 31, 2009, from $3.9 million for the year ended December 31, 2008. The increase in interest income on securities resulted primarily from a $29.5 million, or 35.0%, increase in the average balance of securities to $112.7 million for the year ended December 31, 2009, from $83.5 million for the year ended December 31, 2008. This increase was partially offset by a 35 basis point decrease in the average yield on securities to 4.28% for the year ended December 31, 2009, from 4.63% for the year ended December 31, 2008.

The FHLBC did not pay dividends on its common stock in 2009 or 2008.

Interest income on interest-bearing deposits in other financial institutions increased $7,000, or 6.0%, to $123,000 for the year ended December 31, 2009, from $116,000 for the year ended December 31, 2008. The increase was primarily due to a $43.5 million increase in the average balance of our interest bearing deposits to $52.0 million for the year ended December 31, 2009, from $8.5 million for 2008. This increase was partially offset by a decrease of 113 basis points in the average yield on our interest-bearing deposits to 0.24% for the year ended December 31, 2009, from 1.37% for the year ended December 31, 2008.

Interest expense decreased by $5.1 million, or 19.9%, to $20.6 million for the year ended December 31, 2009, from $25.7 million for the year ended December 31, 2008. The decrease was due to decreased interest expense on deposits and borrowings.

Interest expense on deposits decreased by $3.5 million, or 16.0%, to $18.5 million for the year ended December 31, 2009, from $22.0 million for the year ended December 31, 2008. The decrease in interest expense on deposits was primarily due to a 61 basis point decrease in the average rates paid on deposits, partially offset by a $128.8 million, or 13.6%, net increase in the average balance of deposits. The average cost of deposits was 1.72% for the year ended December 31, 2009, compared to 2.33% for the year ended December 31, 2008. The average rate on savings accounts decreased 22 basis points to 0.51% from 0.73%. On a year over year basis, the average cost of money market accounts decreased 90 basis points to 1.66%, from 2.56%, the average cost of NOW accounts decreased 78 basis points to 0.77%, from 1.55%, and the average cost of certificates of deposit decreased 73 basis points to 2.69% from 3.42%. The average balances of money market accounts increased $59.7 million, or 28.3%, and the average balance of certificates of deposit increased $97.4 million, or 30.0%, for the year ended December 31, 2009. These increases were partially offset by a decrease in the average balances of NOW accounts of $27.3 million, or 8.8%, and a decrease in the average balances of savings accounts of $984,000, or 1.0% for the year ended December 31, 2009.

Interest expense on borrowings decreased by $1.6 million, or 43.4%, to $2.1 million for the year ended December 31, 2009, from $3.6 million for the year ended December 31, 2008. This decrease was due in substantial part to a 128 basis point decrease in the average cost of such borrowings to 2.02% for the year ended December 31, 2009, from 3.30% for the year ended December 31, 2008, and a decrease in the average balance of borrowings of $8.3 million, or 7.5%, to $101.8 million at December 31, 2009, from $110.0 million at December 31, 2008.

Average Balance Sheets

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

	Years Ended December 31,								
	2010			2009			2008		
	Average Outstanding Balance	Interest	Yield/Rate	Average Outstanding Balance	Interest	Yield/Rate	Average Outstanding Balance	Interest	Yield/Rate
	(Dollars in thousands)								
Interest-earning Assets:									
Loans	$ 1,140,865	$ 60,926	5.34%	$ 1,271,024	$ 69,170	5.44%	$ 1,241,518	$ 73,983	5.96%
Securities	86,032	3,488	4.05	112,645	4,816	4.28	83,455	3,861	4.63
Stock in FHLBC	15,598			15,598			15,598		
Other	208,742	522	0.25	52,032	123	0.24	8,487	116	1.37
Total interest-earning assets	1,451,237	64,936	4.47	1,451,299	74,109	5.11	1,349,058	77,960	5.78
Noninterest-earning assets	111,314			115,876			113,957		
Total assets	$ 1,562,551			$ 1,567,175			$ 1,463,015		
Interest-bearing Liabilities:									
Savings deposits	$ 98,338	421	0.43	$ 97,187	495	0.51	$ 98,171	715	0.73
Money market accounts	347,250	3,252	0.94	270,583	4,503	1.66	210,857	5,397	2.56
NOW accounts	295,720	1,441	0.49	284,583	2,178	0.77	311,886	4,844	1.55
Certificates of deposit	405,188	7,219	1.78	421,640	11,325	2.69	324,239	11,077	3.42
Total deposits	1,146,496	12,333	1.08	1,073,993	18,501	1.72	945,153	22,033	2.33
Borrowings	37,653	853	2.27	101,785	2,056	2.02	110,039	3,634	3.30
Total interest-bearing liabilities	1,184,149	13,186	1.11	1,175,778	20,557	1.75	1,055,192	25,667	2.43
Noninterest-bearing deposits	102,294			105,337			104,716		
Noninterest-bearing liabilities	14,003			19,288			19,447		
Total liabilities	1,300,446			1,300,403			1,179,355		
Equity	262,105			266,772			283,660		
Total liabilities and equity	$ 1,562,551			$ 1,567,175			$ 1,463,015		
Net interest income		$ 51,750			$ 53,552			$ 52,293	
Net interest rate spread (1)			3.36%			3.36%			3.35%
Net interest-earning assets (2)	$ 267,088			$ 275,521			$ 293,866		

Net interest margin (3)	3.57%	3.69%	3.88%
Ratio of interest-earning assets to interest-bearing liabilities	122.56%	123.43%	127.85%

(1) Net interest rate spread represents the difference between the yield on average interest-earning assets and the cost of average interest-bearing liabilities.
(2) Net interest-earning assets represents total interest-earning assets less total interest-bearing liabilities.
(3) Net interest margin represents net interest income divided by average total interest-earning assets.

Rate/Volume Analysis

The following table presents the dollar amount of changes in interest income and interest expense for the major categories of our interest-earning assets and interest-bearing liabilities. Information is provided for each category of interest-earning assets and interest-bearing liabilities with respect to changes attributable to changes in volume (i.e., changes in average balances multiplied by the prior-period average rate), and changes attributable to rate (i.e., changes in average rate multiplied by prior-period average balances). For purposes of this table, changes attributable to both rate and volume that cannot be segregated have been allocated proportionately to the change due to volume and the change due to rate.

	Years Ended December 31,					
	2010 vs. 2009			2009 vs. 2008		
	Increase (Decrease) Due to		Total Increase (Decrease)	Increase (Decrease) Due to		Total Increase (Decrease)
	Volume	Rate		Volume	Rate	
	(Dollars in thousands)					
Interest-earning assets:						
Loans	$ (6,989)	$ (1,255)	$ (8,244)	$ 1,725	$ (6,538)	$ (4,813)
Securities	(1,082)	(246)	(1,328)	1,266	(311)	955
Stock in FHLBC						
Other	394	5	399	171	(164)	7
Total interest-earning assets	(7,677)	(1,496)	(9,173)	3,162	(7,013)	(3,851)
Interest-bearing liabilities:						
Savings deposits	6	(80)	(74)	(7)	(213)	(220)
Money market accounts	1,045	(2,296)	(1,251)	1,289	(2,183)	(894)
NOW accounts	83	(820)	(737)	(392)	(2,274)	(2,666)
Certificates of deposit	(425)	(3,681)	(4,106)	2,912	(2,664)	248
Borrowings	(1,431)	228	(1,203)	(255)	(1,323)	(1,578)
Total interest-bearing liabilities	(722)	(6,649)	(7,371)	3,547	(8,657)	(5,110)
Change in net interest income	$ (6,955)	$ 5,153	$ (1,802)	$ (385)	$ 1,644	$ 1,259

Provision for Loan Losses

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

Comparison of Year 2010 to 2009. We recorded a provision for loan losses of $12.1 million for the year ended December 31, 2010, compared to a provision for loan losses of $8.8 million for the year ended December 31, 2009. The 2010 provision for loan losses reflects the combined impact of a $4.4 million increase in the specific portion of the allowance for loan losses that we allocate to impaired loans and $8.5 million in net charge-offs, which were partially offset by a $794,000 decrease in the general portion of the allowance for loan losses.

Net loan charge-offs for 2010 were $8.5 million, or 0.75% of average loans, compared to $4.9 million, or 0.39% of average loans, in 2009. Our allowance for loan losses was $22.2 million, or 2.07% of total loans, at December 31, 2010, compared to $18.6 million, or 1.51% of total loans, at December 31, 2009. The allowance for loan losses represented 48.5% of nonperforming loans at December 31, 2010. To the best of our knowledge, we have recorded all losses that are both probable and reasonable to estimate for each reporting period.

Comparison of Year 2009 to 2008. We recorded a provision for loan losses of $8.8 million for the year ended December 31, 2009, compared to a provision for loan losses of $5.1 million for the year ended December 31, 2008. The 2009 provision for loan losses reflects a $2.4 million increase in the specific portion of the allowance for loan losses that we allocate to impaired loans, a $1.5 million increase in the general portion of the allowance for loan losses, and $4.9 million in net charge-offs. We increased the general portion of the allowance by $1.5 million based on the continued deterioration in national and local economic risk factors included in our model for determining the proper level of general reserves.

Net loan charge-offs for 2009 were $4.9 million, or 0.39% of average loans, compared to $1.4 million, or 0.11% of average loans, in 2008. Our allowance for loan losses was $18.6 million, or 1.51% of total loans, at December 31, 2009, compared to $14.7 million, or 1.15% of total loans, at December 31, 2008. The allowance for loan losses represented 37.6% of nonperforming loans at December 31, 2009. To the best of our knowledge, we have recorded all losses that are both probable and reasonable to estimate for each reporting period.

Noninterest Income

	Years Ended December 31,			Change	
	2010	2009	2008	2010/2009	2009/2008
			(Dollars in thousands)		
Noninterest Income:					
Deposit service charges and fees	$ 3,020	$ 3,363	$ 3,571	$ (343)	$ (208)
Other fee income	1,868	1,816	1,944	52	(128)
Insurance commissions and annuities income	775	715	794	60	(79)
Gain on sale of loans, net	501	699	118	(198)	581
Gain (loss) on sales of securities	31	(988)	1,385	1,019	(2,373)
Gain on unredeemed VISA stock			1,240		(1,240)
Gain (loss) on disposition of premises and equipment	(19)	(40)	(302)	21	262
Loan servicing fees	604	653	771	(49)	(118)
Amortization and impairment of servicing assets	(475)	(446)	(524)	(29)	78
Earnings (loss) on bank owned life insurance	430	(20)	586	450	(606)
Other	393	1,487	835	(1,094)	652
Total noninterest income	$7,128	$7,239	$10,418	$(111)	$(3,179)

Comparison of Year 2010 to 2009. Our noninterest income decreased by $111,000 to $7.1 million for the year ended December 31, 2010, from $7.2 million for the year ended December 31, 2009. Our noninterest income for 2010 included $31,000 gain on the sale of securities, compared a $988,000 pre-tax loss relating to the sale of our Freddie Mac preferred stocks in 2009. Additional factors affecting the change in noninterest income from year-to-year included a $343,000, or 10.2%, decrease in deposit service charges and fees to $3.0 million, from $3.4 million for 2009. Income from insurance commissions and annuities increased by $60,000, or 8.4%, to $775,000 for the year ended December 31, 2010, compared to $715,000 for 2009. Gains on the sale of loans decreased by $198,000, or 28.3%, to $501,000, compared to $699,000 for 2009. We recognized a net loss of $19,000 on the disposition of premises and equipment during 2010, compared to a net loss of $40,000 in 2009. Loan servicing fees decreased $49,000, or 7.5%, to $604,000 for the year ended December 31, 2010, from $653,000 for the year ended December 31, 2009. Mortgage servicing rights amortization expense increased $67,000 or 13.9%, to $549,000 for the year ended December 31, 2010, compared to $482,000 for 2009. We recorded a reserve recovery of $74,000 on our mortgage servicing rights in 2010, compared to a reserve recovery of $36,000 on our mortgage servicing rights in 2009. Bank-owned life insurance produced earnings of $430,000 for 2010, compared to a loss of $20,000 for 2009. Other income for 2009 included a $1.3 million gain on the sale of our merchant processing operations.

Comparison of Year 2009 to 2008. Our noninterest income decreased by $3.2 million to $7.2 million for the year ended December 31, 2009, from $10.4 million for the year ended December 31, 2008. Our noninterest income for 2009 included a $988,000 pre-tax loss relating to the sale of our Freddie Mac preferred stocks, compared to $2.6 million in pre-tax gains relating to the redeemed and unredeemed shares of Visa, Inc. Class B common stock that were allocated to us in the initial public offering that Visa, Inc. conducted in March of 2008. Additional factors affecting the change in noninterest income from year-to-year included a $208,000, or 5.8%, decrease in deposit service charges and fees to $3.3 million, from $3.6 million for 2008. Other fee income decreased $128,000, or 6.6%, to $1.8 million, compared to $1.9 million for 2008. Income from insurance commissions and annuities decreased by $79,000, or 10.0%, to $715,000 for the year ended December 31, 2009, compared to $794,000 for 2008, due to decreased sales activity. Gains on the sale of loans increased by $581,000 to $699,000, compared to $118,000 for 2008. We recognized a net loss of $40,000 on the disposition of premises and equipment during 2009, compared to a net loss of $302,000 in 2008. Loan servicing fees decreased $118,000, or 15.3%, to $653,000 for the year ended December 31, 2009, from $771,000 for 2008. Mortgage servicing rights amortization expense increased $68,000 or 16.4%, to $482,000 for the year ended December 31, 2009, compared to $414,000 for 2008. We recorded a reserve recovery of $36,000 on our mortgage servicing rights in 2009, compared to a $110,000 reserve that we recorded for 2008. Bank-owned life insurance produced a loss of $20,000 for 2009, compared to income of $586,000 for 2008, due to our decision to temporarily move investable policy funds into a low-yielding money market sub-account at the end of 2008 as a means of protecting the underlying value of the policy. Other income totaled $1.5 million for the year ended December 31, 2009, compared to $835,000 for 2008, due primarily to the recording of a $1.3 million gain on the sale of our merchant processing operations in the fourth quarter of 2009.

Noninterest Expense

	Years Ended December 31, 2010	2009	2008	Change 2010/2009	2009/2008
	(Dollars in thousands)				
Noninterest Expense:					
Compensation and benefits	$ 26,339	$ 29,046	$ 30,535	$ (2,707)	$ (1,489)
Office occupancy and equipment	6,380	6,845	6,874	(465)	(29)
Advertising and public relations	1,277	1,321	1,361	(44)	(40)
Information technology	3,733	3,637	3,662	96	(25)
Supplies, telephone and postage	1,596	1,819	2,070	(223)	(251)
Amortization of intangibles	1,595	1,690	1,784	(95)	(94)
Nonperforming asset management	3,342	770		2,572	770
Operations of other real estate owned	3,972	1,273	434	2,699	839
Loss on impairment of securities		401	35,919	(401)	(35,518)
Loss on early extinguishment of borrowings			1,975		(1,975)
FDIC insurance premiums	2,126	2,225	162	(99)	2,063
Other	3,489	3,704	4,280	(215)	(576)
Total noninterest expense	$ 53,849	$ 52,731	$ 89,056	$ 1,118	$ (36,325)

Comparison of Year 2010 to 2009. For the year ended December 31, 2010, noninterest expense increased by $1.1 million, or 2.1%, to $53.8 million, from $52.7 million for the year ended December 31, 2009. Noninterest expense for 2010 included $7.3 million in expenses for nonperforming asset management and operations of other real estate owned. Noninterest expense for 2009 included a $401,000 pre-tax impairment loss that we recorded on our holdings of Freddie Mac preferred stocks. Additional factors affecting the change in noninterest expense from year-to-year included a $2.7 million, or 9.3%, decrease in compensation expense to $26.3 million for the year ended December 31, 2010, from $29.0 million for the year ended December 31, 2009. The decrease was due in part to a decrease of 44 full-time equivalent employees from 372 in 2009 to 328 in 2010. Supplies, telephone and postage expenses decreased $223,000, or 12.3%, to $1.6 million, and intangible amortization expense decreased by $95,000. Net expenses for nonperforming asset management for 2010 included legal expenses of $876,000, receiver fees of $372,000, and real estate taxes and insurance of $1.9 million. Net expenses for operations of other real estate owned totaled $4.0 million for 2010, compared to $1.3 million for the same period in 2009. Net expenses for operations of other real estate owned included $2.4 million in write-downs on OREO and $415,000 of losses upon sale of OREO.

Comparison of Year 2009 to 2008. For the year ended December 31, 2009, noninterest expense decreased by $36.3 million, or 40.8%, to $52.7 million, from $89.1 million for the year ended December 31, 2008. Noninterest expense for 2008 included a $35.9 million pre-tax impairment loss that we recorded on our holdings of Freddie Mac preferred stocks and a $2.0 million pre-tax expense that we recorded in connection with the prepayment of a $25 million FHLBC term advance. Additional factors affecting the change in noninterest expense from year-to-year included a $1.5 million, or 4.9%, decrease in compensation expense to $29.0 million for the year ended December 31, 2009, from $30.5 million for the year ended December 31, 2008. The decrease was due in part to a decrease of 21 full-time equivalent employees from 393 in 2008 to 372 in 2009, resulting from the implementation of functional staffing reviews. Expense relating to equity-based compensation and benefits totaled $3.0 million in 2009, compared to $4.6 million during 2008. Supplies, telephone and postage expenses decreased $251,000, or 12.1%, to $1.8 million, and intangible amortization expense decreased by $94,000. These expense reductions were partially offset by an increase in our net expense from other real estate owned operations to $1.3 million for the year ended December 31, 2009, compared to $434,000 for 2008. Net operations from other real estate owned for the current year included $973,000 in write-downs or losses on other real estate owned, compared to $289,000 in write-downs or losses in 2008. Our expense for FDIC deposit insurance increased to $2.2 million during the year ended December 31, 2009, compared to $162,000 during the same period of 2008. The increase in our expense for FDIC deposit insurance was due to the combined effect of the FDIC s increase in its quarterly assessment rate, the FDIC s imposition of a special assessment against all insured depository institutions and the full utilization of the FDIC assessment credits that we previously had available to offset or reduce FDIC quarterly assessments. Other expenses increased by $194,000, or 4.5%, to $4.5 million in 2009.

Income Tax Benefit

Comparison of Year 2010 to 2009. For the year ended December 31, 2010, we recorded an income tax benefit of $2.7 million, compared to an income tax benefit of $13,000 for the year ended December 31, 2009. The effective tax rates were 38.94% and 1.73% for the years ended December 31, 2010 and 2009, respectively. For 2009, the difference between the GAAP basis (fair market value at the date of grant) and the tax basis (fair market value at the date of vesting) of equity-based compensation granted in prior years reduced our income tax benefit.

Comparison of Year 2009 to 2008. For the year ended December 31, 2009, we recorded an income tax benefit of $13,000, compared to an income tax benefit of $12.0 million for the year ended December 31, 2008. For 2009, the difference between the GAAP basis (fair market value at the date of grant) and the tax basis (fair market value at the date of vesting) of equity-based compensation granted in prior years reduced our income tax benefit. The income tax benefit for 2008 was primarily due to the impairment loss that we recorded on our Freddie Mac preferred stocks.

Impact of Inflation and Changing Prices

The Company s financial statements and the related notes have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP). GAAP generally requires the measurement of financial position and operating results in terms of historical dollars without considering changes in the relative purchasing power of money over time due to inflation. The impact of inflation, if any, is reflected in the increased cost of our operations. Unlike industrial companies, our assets and liabilities are primarily monetary in nature. As a result, changes in market interest rates have a greater impact on performance than the effects of inflation.

Management of Interest Rate Risk

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

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

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

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

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

Our dynamic GAP analysis determines the relative balance between the repricing of assets and liabilities over multiple periods of time (ranging from overnight to five years). Dynamic GAP analysis includes expected cash flows from loans and mortgage-backed securities, applying prepayment rates based on the differential between the current interest rate and the market interest rate for each loan and security type. This analysis identifies mismatches in the timing of asset and liability repricing but does not necessarily provide an accurate indicator of interest rate risk because it omits the factors incorporated into the net interest income analysis.

Quantitative Analysis. The following table sets forth, as of December 31, 2010, the estimated changes in the Bank s NPV and net interest income that would result from the designated instantaneous parallel shift in the U.S. Treasury yield curve. Computations of prospective effects of hypothetical interest rate changes are based on numerous assumptions including relative levels of market interest rates, loan prepayments and deposit decay, and should not be relied upon as indicative of actual results.

	Estimated Increase in NPV		**Increase (decrease) in Estimated Net Interest Income**	
Change in Interest Rates (basis points)	**Amount**	**Percent**	**Amount**	**Percent**
+400	$ 28,874	12.33%	$ (687)	(1.45)%
+300	22,421	9.58	(306)	(0.64)
+200	16,367	6.99	(97)	(0.20)
+100	8,836	3.77	275	0.58
0				

The Company has opted not to include an estimate for a decrease in rates at December 31, 2010 as the results are not relevant given the current targeted fed funds rate of the Federal Open Market Committee. The table set forth above indicates that at December 31, 2010, in the event of an immediate 200 basis point increase in interest rates, the Bank would be expected to experience a 6.99% increase in NPV and a $97,000 decrease in net interest income. This data does not reflect any actions that we may undertake in response to changes in interest rates, such as changes in rates paid on certain deposit accounts based on local competitive factors, which could reduce the actual impact on NPV and net interest income, if any.

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

Liquidity Management

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

Our primary sources of funds are deposits, principal and interest payments on loans and securities, and, to a lesser extent, wholesale borrowings, the proceeds from maturing securities and short-term investments, and the proceeds from the sales of loans and securities. The scheduled amortization of loans and securities, as well as proceeds from borrowings, are predictable sources of funds. Other funding sources, however, such as deposit inflows, mortgage prepayments and mortgage loan sales are greatly influenced by market interest rates, economic conditions and competition.

Our cash flows are derived from operating activities, investing activities and financing activities as reported in the Consolidated Statements of Cash Flows in our Consolidated Financial Statements. Our primary investing activities are the origination for investment or sale of one-to-four family residential mortgage loans, the origination for investment of multi-family mortgage, nonresidential real estate, commercial leases, construction and land, and commercial loans and the purchase of investment securities and mortgage-backed securities. During the years ended December 31, 2010, 2009 and 2008 our loans originated for sale totaled $19.7 million, $40.8 million and $23.4 million, respectively. During the years ended December 31, 2010, 2009 and 2008, our loans originated for investment totaled $676.4 million, $796.3 million and $818.7 million, respectively. Purchases of loans totaled $2.7 million, $19.4 million and $12.7 million for the years ended December 31, 2010, 2009 and 2008, respectively. Purchases of securities totaled $50.5 million and $103.0 million for the years ended December 31, 2010 and 2008, respectively. There were no purchases of securities in 2009.

These activities were funded primarily by principal repayments on loans and securities, and the sale of loans and securities. During the years ended December 31, 2010, 2009 and 2008, principal repayments on loans totaled $817.4 million, $852.1 million and $810.6 million, respectively. During the years ended December 31, 2010, 2009 and 2008, principal repayments on securities totaled $30.1 million, $22.7 million and $9.1 million, respectively. During the years ended December 31, 2010, 2009 and 2008, proceeds from maturities and sales of securities totaled $1.8 million, $2.8 million and $17.5 million, respectively. During the years ended December 31, 2010, 2009 and 2008, the proceeds from the sale of loans totaled $17.5 million, $42.4 million and $22.8 million, respectively.

Loan origination commitments totaled $16.7 million at December 31, 2010, and consisted of $14.3 million of fixed-rate loans and $2.4 million of adjustable-rate loans. Unused lines of credit and standby letters of credit granted to customers totaled $138.2 million and $1.7 million, respectively, at December 31, 2010. At December 31, 2010, commitments to sell mortgages totaled $3.2 million.

Deposit flows are generally affected by the level of market interest rates, the interest rates and other terms and conditions on deposit products offered by our banking competitors, and other factors. We had a net deposit increase of $2.0 million for the year ended December 31, 2010, compared to a net increase of $163.5 million for the year ended December 31, 2009 and net outflows of $3.8 million for the year ended December 31, 2008. At times during recent periods, we have not actively competed for higher cost deposit accounts, including certificates of deposit, choosing instead to fund loan growth from the loan and lease repayments. Certificates of deposit that are scheduled to mature in one year or less from December 31, 2010 totaled $271.2 million. Based upon prior experience and our current pricing strategy, we believe that we will retain a significant portion of these deposits upon their maturities.

We anticipate that we will have sufficient funds available to meet current loan commitments and lines of credit and maturing certificates of deposit that are not renewed or extended. We generally remain fully invested and utilize additional sources of funds through FHLBC advances, of which $16.0 million were outstanding at December 31, 2010. At December 31, 2010 we had the ability to borrow an additional $240.5 million under our credit facilities with the FHLBC. Furthermore, we have unpledged securities that could be used to support borrowings in excess of $71.4 million. Finally, at December 31, 2010 we had available pre-approved overnight federal funds borrowing lines of $28.0 million and a line of credit available with the Federal Reserve Bank of Chicago of $425,000. At December 31, 2010, there was no outstanding balance on these credit lines.

We minimize the funds required to originate one-to-four family residential mortgage loans in two ways. We sell in the secondary market virtually all of our eligible fixed-rate one-to-four family residential mortgage loans. From time to time, we also securitize the conforming adjustable-rate one-to-four family residential mortgage loans that we originate and hold the securities we receive in exchange. The resulting mortgage-backed securities that we retain on our balance sheet can be sold more readily to meet our liquidity or interest rate management needs. Because the securities carry a lower risk-weighting than the underlying loans, the securitizations also lower our regulatory capital requirements. We did not securitize any loans during 2010 and 2009.

Liquidity Management - Company. The liquidity needs of the Company on an unconsolidated basis consist primarily of operating expenses, dividends to stockholders and stock repurchases. The primary sources of liquidity for the Company currently are $16.4 million of cash and cash equivalents and periodic cash dividends from the Bank.

Under the rules of the OTS, the Bank is not permitted to pay dividends on its capital stock to the Company, its sole stockholder, if the dividend would reduce the Bank s stockholder s equity below the amount of the liquidation account established in connection with the Company s mutual-to-stock conversion. The Bank may pay dividends without the approval of the OTS only if the Bank meets its applicable regulatory capital requirements before and after the payment of the dividends and its total dividends do not exceed its net income to date over the calendar year in which the dividend is paid plus retained net income over the preceding two years. The OTS has discretion to prohibit permissible capital distributions on general safety and soundness grounds and must be given 30 days advance notice of all capital distributions from the Bank to the Company, including dividends.

During 2010, we used $3.1 million of existing cash and cash equivalents to repurchase shares of our common stock and $6.0 million of existing cash and cash equivalents to pay cash dividends to our stockholders.

As of December 31, 2010, we were not aware of any known trends, events or uncertainties that had or were reasonably likely to have a material impact on our liquidity. As of December 31, 2010, we had no other material commitments for capital expenditures.

Capital Management

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

The Bank is subject to regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory, and possibly additional discretionary, actions by the OTS that, if undertaken, could have a direct material effect on the Bank s financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of the Bank s assets, liabilities, and certain off-balance-sheet items as calculated under regulatory accounting practices. The Bank s capital amounts and classification are also subject to qualitative judgments by regulators about components, risk weightings, and other factors.

The prompt corrective action regulations provide five classifications, including well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized, although these terms are not used to represent overall financial condition. Adequately capitalized institutions require regulatory approval to accept brokered deposits. If undercapitalized, a financial institution s capital distributions, asset growth and expansion are limited, and for the submission of a capital restoration is required.

At year-end, actual capital ratios and minimum required ratios for the Bank were:

	Actual Ratio	Minimum Required for Capital Adequacy Purposes	Minimum Required to Be Well Capitalized Under Prompt Corrective Action Provisions
December 31, 2010			
Total capital (to risk-weighted assets)	18.38%	8.00%	10.00%
Tier 1 (core) capital (to risk-weighted assets)	17.20	4.00	6.00
Tier 1 (core) capital (to adjusted total assets)	12.48	4.00	5.00
December 31, 2009			
Total capital (to risk-weighted assets)	16.40%	8.00%	10.00%
Tier 1 (core) capital (to risk-weighted assets)	15.31	4.00	6.00
Tier 1 (core) capital (to adjusted total assets)	12.44	4.00	5.00

See Note 11 Regulatory Matters in our Consolidated Financial Statements for a reconciliation of the Bank s equity under GAAP to regulatory capital.

As of December 31, 2010 and 2009, the OTS categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. There are no conditions or events since those notifications that management believes have changed the institution s capitalization category.

Capital Management - Company. On June 23, 2005, the Company completed its mutual-to-stock conversion and sold 24,466,250 shares of common stock in a subscription offering at $10.00 per share and raised $240.3 million in offering proceeds, net of offering expenses. The Company contributed $120.9 million of the net proceeds to the Bank, paid off $30 million of term borrowings, loaned $19.6 million to our ESOP and retained the remaining net proceeds of $72 million. As a result of the offering, the Company has capital levels substantially above those required to support the current size and risk profile of the Company and its subsidiary, the Bank.

Total stockholders equity totaled $253.3 million at December 31, 2010, compared to $263.6 million at December 31, 2009. The decrease in total stockholders equity was primarily due to the combined impact of our repurchase of 356,411 shares of our common stock during 2010 at a total cost of $3.1 million, and our declaration and payment of cash dividends totaling $5.9 million, the $4.3 million net loss that we recorded for 2010 and a $50,000 decrease accumulated other comprehensive income. These items were partially offset by a $3.1 million increase in total stockholders equity that resulted from the vesting of stock-based compensation and ESOP shares earned

The OTS has no specific quantitative capital regulations for savings and loan holding companies on either a consolidated or unconsolidated basis. There are several capital measurements that the OTS uses to evaluate the adequacy of a savings and loan holding company s capital. One measurement is the tangible capital ratio. The tangible capital ratio (the ratio of tangible capital to tangible total assets (stockholders equity less goodwill and intangible assets divided by total assets less goodwill and intangible assets)) for the Company on a consolidated basis measures the percentage of consolidated tangible equity capital supporting our consolidated tangible total assets. The Company s tangible capital ratio was 14.74% at December 31, 2010, compared to 15.14% at December 31, 2009.

Our strategy for utilizing the capital encompasses several components, including debt reduction, funding our ESOP, financing acquisitions, paying dividends to stockholders, repurchasing shares of our common stock and for other general corporate purposes.

Our Board of Directors has authorized the repurchase of up to 5,047,423 shares of our common stock. The authorization permits shares to be repurchased in open market or negotiated transactions, and pursuant to any trading plan that may be adopted in accordance with Rule 10b5-1 of the Securities and Exchange Commission. The authorization may be utilized at management s discretion, subject to the limitations set forth in Rule 10b-18 of the Securities and Exchange Commission and other applicable legal requirements, and to price and other internal limitations established by the Board of Directors. The repurchase authorization will expire on May 16, 2011, unless extended by the Board of Directors. As of December 31, 2010, the Company had repurchased 4,239,134 shares of its common stock out of the 5,047,423 shares that have been authorized for repurchase.

Off-Balance Sheet Arrangements and Aggregate Contractual Obligations

Commitments. As a financial services provider, we routinely are a party to various financial instruments with off-balance-sheet risks, such as commitments to extend credit, standby letters of credit, unused lines of credit and commitments to sell loans. While these contractual obligations represent our future cash requirements, a significant portion of commitments to extend credit may expire without being drawn upon. Such commitments are subject to the same credit policies and approval process afforded to loans that we make. Although we consider commitments to extend credit in determining our allowance for loan losses, at December 31, 2010, we had made no provision for losses on commitments to extend credit, and had no specific or general allowance for losses on such commitments, as we have had no historical loss experience with commitments to extend credit and we believed that no probable and reasonably estimable losses were inherent in our portfolio as a result of our commitments to extend credit. For additional information, see Note 14 - Loan Commitments and Other Off-Balance Sheet Activities in our Consolidated Financial Statements.

Contractual Obligations. In the ordinary course of our operations, we enter into certain contractual obligations. Such obligations include operating leases for premises and equipment.

The following table summarizes our significant fixed and determinable contractual obligations and other funding needs by payment date at December 31, 2010. The payment amounts represent those amounts due to the recipient and do not include any unamortized premiums or discounts or other similar carrying amount adjustments.

	Payments Due by Period				
Contractual Obligations	**Less than One Year**	**One to Three Years**	**Three to Five Years**	**More than Five Years**	**Total**
			(Dollars in thousands)		
Certificates of deposit	$ 271,243	$ 94,877	$ 13,954	$	$ 380,074
Borrowings	20,749	3,000			23,749
Standby letters of credit	1,599	100			1,699
Operating leases	560	1,084	960	6,576	9,180
Total	$ 294,151	$ 99,061	$ 14,914	$ 6,576	$ 414,702
Commitments to extend credit	$ 154,931	$	$	$	$ 154,931

Pending Acquisition

On September 13, 2010, the Company signed a definitive Merger Agreement to acquire DG Bancorp, Inc. and its wholly-owned subsidiary, Downers Grove National Bank. Founded in 1955, Downers Grove National Bank is a privately held community bank with $219 million in assets and $213 million in deposits as of December 31, 2010. Downers Grove National Bank has two banking locations in Downers Grove and Westmont, IL communities. The transaction has been approved by the Bank s primary federal regulator, the Office of Thrift Supervision, and is expected to close in the first quarter of 2011, subject to customary closing conditions.

The following represents financial statements of DG Bancorp as of December 31, 2010 and 2009 and the results of their operations in the two years ended December 31, 2010. These results have been audited in accordance with the auditing standards generally accepted in the United States of America, with an opinion thereon February 23, 2011.

DG Bancorp, Inc and Subsidiary

Consolidated Balance Sheet

December 31,

(In thousands)

	2010	2009
ASSETS		
Cash and cash equivalents - cash and due from banks	$ 45,558	$ 38,462
Securities,	20,937	10,164
Loans receivable, net of allowance for loan losses of $6,500 ($5,600 in 2009)	134,947	188,218
Income tax receivable	928	2,906
Other real estate owned	13,233	6,360
Premises and equipment, net	1,758	2,035
Other assets	1,777	4,809
Total assets	$ 219,138	$ 252,954
LIABILITIES AND STOCKHOLDERS EQUITY		
Deposit accounts	$ 212,610	$ 226,083
Borrowed funds		8,000
Accrued expenses and other liabilities	1,056	1,351
Total liabilities	213,666	235,434
Total stockholders equity	5,472	17,520
Total liabilities and stockholders equity	$ 219,138	$ 252,954

DG Bancorp, Inc and Subsidiary

Consolidated Statement of Operations

For the Years Ended December 31,

(In thousands, except per share amounts)

	2010	2009
Interest and dividend income		
Loans, including fees	$ 9,119	$ 12,497
Securities	402	728
Other	122	48
Total interest income	9,643	13,273
Interest expense		
Deposits	1,913	3,217
Borrowings	90	279
Total interest expense	2,003	3,496
Net interest income	7,640	9,777
Provision for loan losses	10,987	12,208
Net interest loss after provision for loan losses	(3,347)	(2,431)
Noninterest income		
Trust income	874	881
Deposit service charges and fees	316	368
Mortgage brokerage fees	13	67
Other service charges , commissions, and fees	263	258
Gain on sale or call of securities	2	6
Gain on sale of other real estate owned	274	135
Other	164	155
Total noninterest income	1,906	1,870
Noninterest expense		
Compensation and benefits	4,106	4,339
Office occupancy	609	593
Furniture and equipment	302	372
Professional fees	1,004	1,009
Data processing	419	418
Insurance	980	804
Examination and audit fees	170	292
Impairment of goodwill		600
Impairment of other real estate owned	219	917
Other	1,418	1,335
Total noninterest expense	9,227	10,679
Loss before income taxes	(10,668)	(11,240)
Income tax provision (benefit)	1,401	(3,775)

Net loss	$ (12,069)	$ (7,465)
Basic and diluted loss per share	$ (137.15)	$ (84.83)

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK

For information regarding market risk see Item 7 - Management s Discussion and Analysis of Financial Condition and Results of Operations - Management of Interest Rate Risk.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

REPORT OF MANAGEMENT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

Management of BankFinancial Corporation is responsible for establishing and maintaining effective internal control over financial reporting.

Management evaluates the effectiveness of internal control over financial reporting and tests for reliability of recorded financial information through a program of ongoing internal audits. Any system of internal control, no matter how well designed, has inherent limitations, including the possibility that a control can be circumvented or overridden and misstatements due to error or fraud may occur and not be detected. Also, because of changes in conditions, internal control effectiveness may vary over time. Accordingly, even an effective system of internal control will provide only reasonable assurance with respect to financial statement preparation.

The Company s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with accounting principles generally accepted in the United States of America. The Company s internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the Company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with accounting principles generally accepted in the United States of America, and that receipts and expenditures of the Company are being made only in accordance with authorizations of management and directors of the Company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the Company s assets that could have a material effect on the financial statements.

Management assessed the Company s internal control over financial reporting as of December 31, 2010, as required by Section 404 of the Sarbanes-Oxley Act of 2002, based on the criteria for effective internal control over financial reporting described in the Internal Control-Integrated Framework, adopted by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on this assessment, management concludes that, as of December 31, 2010, the Company s internal control over financial reporting is effective.

The Company s independent registered public accounting firm has issued their report on the effectiveness of the Company s internal control over financial reporting. That report follows under the heading, Report of Independent Registered Public Accounting Firm.

/s/ F. Morgan Gasior	/s/ Paul A. Cloutier
F. Morgan Gasior	Paul A. Cloutier
Chairman of the Board, Chief Executive Officer and President	Executive Vice President and Chief Financial Officer

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We have audited the accompanying statements of financial condition of BankFinancial Corporation (the Company) as of December 31, 2010 and 2009, and the related statements of operations, changes in stockholders equity and comprehensive income (loss), and cash flows for each of the years in the three-year period ended December 31, 2010. We also have audited the Company s internal control over financial reporting as of December 31, 2010, based on criteria established in *Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).* The Company s management is responsible for these financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management s Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on these financial statements and an opinion on the Company s internal control over financial reporting based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design, and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company s assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of BankFinancial Corporation as of December 31, 2010 and 2009, and the results of its operations and its cash flows for each of the years in the three-year period ended December 31, 2010 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2010, based on criteria established in *Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).*

Crowe Horwath LLP

Oak Brook, Illinois

March 8, 2011

BANKFINANCIAL CORPORATION

CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION

December 31, 2010 and 2009

(In thousands, except share and per share data)

	December 31, 2010	December 31,