

BROADWAY FINANCIAL CORP \DE\  
Form 10-Q  
September 21, 2012  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
Washington D.C. 20549

**FORM 10-Q**

(Mark One)

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

**For the quarterly period ended March 31, 2012**

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

**For transition period from      to**

**Commission file number 000-27464**

**BROADWAY FINANCIAL CORPORATION**

**(Exact name of registrant as specified in its charter)**

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**Delaware**  
(State or other jurisdiction of  
incorporation or organization)

**95-4547287**  
(I.R.S. Employer  
Identification No.)

**4800 Wilshire Boulevard, Los Angeles, California**  
(Address of principal executive offices)

**90010**  
(Zip Code)

**(323) 634-1700**

(Registrant's telephone number, including area code)

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated, or a smaller reporting company. See the definition 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

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: 1,744,565 shares of the Company's Common Stock, par value \$0.01 per share, were outstanding as of September 6, 2012.

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**Explanatory Note**

On May 15, 2012, the Company filed a Current Report on Form 8-K regarding its first quarter 2012 earnings release. The Company has restated results for the first quarter 2012 and issued a press release announcing the revised earnings on September 19, 2012, which is attached to the Company's Current Report on Form 8-K filed on September 19, 2012.

The filing of this Quarterly Report on Form 10-Q ( this Report ) was delayed pending completion of the restatement of our audited consolidated financial statements for the year ended December 31, 2011 as described in the amendment to our Form 10-K Annual Report for that year (Form 10-K/A Amendment No. 2) that we filed with the Securities and Exchange Commission (the SEC ) on September 14, 2012. Except as otherwise indicated herein, this Report speaks as of March 31, 2012 only and does not reflect events or changes in circumstances that have occurred after that date. Certain material changes in facts and circumstances and certain material events have occurred, or may occur, after that date that are described, or may be described, in subsequent filings that we make with the SEC. Each such subsequent filing with the SEC should be read for further information regarding our financial condition, results of operations and circumstances.

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**Table of Contents****BROADWAY FINANCIAL CORPORATION AND SUBSIDIARIES****Consolidated Balance Sheets**

|  | <b>March 31, 2012</b><br><b>(Unaudited)</b><br><i>(Dollars in thousands, except per share amounts)</i> | <b>December 31, 2011</b> |
|--|--|--------------------------|
| <b>Assets</b>  |  |                          |
| Cash   | \$ 13,572  | \$ 12,127                |
| Federal funds sold   | 31,605   | 19,470                   |
| Cash and cash equivalents  | 45,177   | 31,597                   |
| Securities available-for-sale, at fair value   | 18,027   | 18,979                   |
| Loans receivable held for sale, net  | 12,908   | 12,983                   |
| Loans receivable, net of allowance of \$17,752 and \$17,299  | 309,578  | 322,770                  |
| Accrued interest receivable  | 1,601  | 1,698                    |
| Federal Home Loan Bank (FHLB) stock, at cost   | 3,901  | 4,089                    |
| Office properties and equipment, net   | 4,548  | 4,626                    |
| Real estate owned  | 3,958  | 6,699                    |
| Bank owned life insurance  | 2,629  | 2,609                    |
| Investment in affordable housing limited partnership   | 1,629  | 1,675                    |
| Deferred tax assets  | 772  | 850                      |
| Other assets   | 4,132  | 5,162                    |
| <b>Total assets</b>  | <b>\$ 408,860</b>  | <b>\$ 413,737</b>        |
| <b>Liabilities and shareholders equity</b>   |  |                          |
| Deposits   | \$ 290,352   | \$ 294,686               |
| Federal Home Loan Bank advances  | 83,000   | 83,000                   |
| Junior subordinated debentures   | 6,000  | 6,000                    |
| Other borrowings   | 5,000  | 5,000                    |
| Advance payments by borrowers for taxes and insurance  | 335  | 813                      |
| Other liabilities  | 5,904  | 5,962                    |
| <b>Total liabilities</b>   | <b>390,591</b>   | <b>395,461</b>           |
| <b>Shareholders Equity:</b>  |  |                          |
| Senior preferred cumulative and non-voting stock, \$.01 par value, authorized, issued and outstanding 9,000 shares of Series D at March 31, 2012 and December 31, 2011; liquidation preference of \$9,844 at March 31, 2012 and \$9,731 at December 31, 2011   | 8,963  | 8,963                    |
| Senior preferred cumulative and non-voting stock, \$.01 par value, authorized, issued and outstanding 6,000 shares of Series E at March 31, 2012 and December 31, 2011; liquidation preference of \$6,563 at March 31, 2012 and \$6,488 at December 31, 2011   | 5,974  | 5,974                    |
| Preferred non-cumulative and non-voting stock, \$.01 par value, authorized 985,000 shares; issued and outstanding 55,199 shares of Series A, 100,000 shares of Series B and 76,950 shares of Series C at March 31, 2012 and December 31, 2011; liquidation preference of \$552 for Series A, \$1,000 for Series B and \$1,000 for Series C at March 31, 2012 and December 31, 2011 | 3,657  | 3,657                    |
| Preferred stock discount   | (896)  | (994)                    |
| Common stock, \$.01 par value, authorized 8,000,000 shares at March 31, 2012 and December 31, 2011; issued 2,013,942 shares at March 31, 2012 and December 31, 2011; outstanding 1,744,565 shares at March 31, 2012 and December 31, 2011  | 20   | 20                       |
| Additional paid-in capital   | 10,844   | 10,824                   |
| Accumulated deficit  | (7,427)  | (7,295)                  |
|  | 578  | 571                      |

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|   |                   |                   |
|---|-------------------|-------------------|
| Accumulated other comprehensive income, net of taxes of \$400 at March 31, 2012 and December 31, 2011 |                   |                   |
| Treasury stock-at cost, 269,377 shares at March 31, 2012 and December 31, 2011                        | (3,444)           | (3,444)           |
| <b>Total shareholders equity</b>  | <b>18,269</b>     | <b>18,276</b>     |
| <b>Total liabilities and shareholders equity</b>  | <b>\$ 408,860</b> | <b>\$ 413,737</b> |

*See accompanying notes to unaudited consolidated financial statements.*

**Table of Contents****BROADWAY FINANCIAL CORPORATION AND SUBSIDIARIES****Consolidated Statements of Operations and Comprehensive Earnings (Loss)****(Unaudited)**

|   | <b>Three Months Ended March 31,</b>                     |              |
|---|---|--------------|
|   | <b>2012</b>   | <b>2011</b>  |
|   | <i>(Dollars in thousands, except per share amounts)</i> |              |
| Interest and fees on loans receivable                       | \$ 5,330  | \$ 6,384     |
| Interest on mortgage-backed securities and other securities | 148   | 181          |
| Other interest income                                       | 16  | 9            |
| <b>Total interest income</b>                                | <b>5,494</b>  | <b>6,574</b> |
| Interest on deposits  | 975   | 1,239        |
| Interest on borrowings                                      | 833   | 989          |
| <b>Total interest expense</b>                               | <b>1,808</b>  | <b>2,228</b> |
| Net interest income before provision for loan losses        | 3,686   | 4,346        |
| Provision for loan losses                                   | 959   | 1,240        |
| Net interest income after provision for loan losses         | 2,727   | 3,106        |
| <b>Non-interest income:</b>                                 |   |              |
| Service charges   | 153   | 182          |
| Net losses on mortgage banking activities                   | (166)   | (25)         |
| Net gains (losses) on sales of REO                          | 412   | (15)         |
| Other   | 24  | 39           |
| <b>Total non-interest income</b>                            | <b>423</b>  | <b>181</b>   |
| <b>Non-interest expense:</b>                                |   |              |
| Compensation and benefits                                   | 1,589   | 1,809        |
| Occupancy expense, net                                      | 287   | 354          |
| Information services  | 213   | 227          |
| Professional services                                       | 108   | 168          |
| Provision for losses on loans held for sale                 | (2)   | 20           |
| Provision for losses on REO                                 | (19)  | 80           |
| FDIC insurance  | 217   | 283          |
| Office services and supplies                                | 109   | 142          |
| Other   | 419   | 419          |
| <b>Total non-interest expense</b>                           | <b>2,921</b>  | <b>3,502</b> |
| Earnings (loss) before income taxes                         | 229   | (215)        |
| Income tax expense (benefit)                                | 75  | (86)         |
| Net earnings (loss)   | 154   | (129)        |
| Dividends and discount accretion on preferred stock         | (286)   | (283)        |
| Loss available to common shareholders                       | \$ (132)  | \$ (412)     |

|   |           |           |
|---|-----------|-----------|
| Loss per share:   |           |           |
| Basic   | \$ (0.08) | \$ (0.24) |
| Diluted   | \$ (0.08) | \$ (0.24) |
| Other comprehensive income (loss), net of tax:          |           |           |
| Unrealized gain (loss) on securities available-for-sale | \$ 7      | \$ (15)   |
| Income tax effect                                       |           | 6         |
| Other comprehensive income (loss), net of tax           | 7         | (9)       |
| Comprehensive earnings (loss)                           | \$ 161    | \$ (138)  |

*See accompanying notes to unaudited consolidated financial statements.*



**Table of Contents****BROADWAY FINANCIAL CORPORATION AND SUBSIDIARIES****Consolidated Statements of Cash Flows****(Unaudited)**

|  | <b>Three Months Ended March 31,</b> |             |
|--|-------------------------------------|-------------|
|  | <b>2012</b>                         | <b>2011</b> |
|  | <i>(Dollars in thousands)</i>       |             |
| <b>Cash flows from operating activities:</b>   |                                     |             |
| Net earnings (loss)  | \$ 154                              | \$ (129)    |
| Adjustments to reconcile net earnings (loss) to net cash provided by operating activities: |                                     |             |
| Provision for loan losses  | 959                                 | 1,240       |
| Provision for losses on loans receivable held-for-sale                                     | (2)                                 | 20          |
| Provision for losses on REO  | (19)                                | 80          |
| Depreciation   | 78                                  | 104         |
| Net amortization of deferred loan origination (fees) costs                                 | 27                                  | (3)         |
| Net amortization of premiums on mortgage-backed securities                                 | 15                                  | 36          |
| Amortization of investment in affordable housing limited partnership                       | 46                                  |             |
| Stock-based compensation expense   | 20                                  | 23          |
| Earnings on bank owned life insurance  | (20)                                | (22)        |
| Net (gains) losses on sales of REO   | (412)                               | 15          |
| Net losses on sales of loans   |                                     | 29          |
| Net change in:   |                                     |             |
| Accrued interest receivable  | 97                                  | 216         |
| Deferred tax assets  | 78                                  |             |
| Other assets   | 1,030                               | (1,636)     |
| Other liabilities  | (246)                               | 372         |
| Net cash provided by operating activities  | 1,805                               | 345         |
| <b>Cash flows from investing activities:</b>   |                                     |             |
| Net change in loans receivable   | 11,389                              | 4,593       |
| Proceeds from sales and principal repayments of loans receivable held-for-sale             | 77                                  | 6,480       |
| Available-for-sale securities:   |                                     |             |
| Maturities, prepayments and calls  | 944                                 | 760         |
| Held-to-maturity securities:   |                                     |             |
| Maturities, prepayments and calls  |                                     | 866         |
| Proceeds from sales of REO   | 3,989                               | 130         |
| Net redemption of Federal Home Loan Bank stock   | 188                                 |             |
| Additions to office properties and equipment   |                                     | (18)        |
| Net cash provided by investing activities  | 16,587                              | 12,811      |
| <b>Cash flows from financing activities:</b>   |                                     |             |
| Net change in deposits   | (4,334)                             | (7,522)     |
| Proceeds from FHLB advances  |                                     | 7,000       |
| Repayments on FHLB advances  |                                     | (7,000)     |
| Net change in advance payments by borrowers for taxes and insurance                        | (478)                               | 69          |
| Net cash used in financing activities  | (4,812)                             | (7,453)     |
| Net change in cash and cash equivalents  | 13,580                              | 5,703       |
| Cash and cash equivalents at beginning of period   | 31,597                              | 21,978      |

|  |           |           |
|--|-----------|-----------|
| Cash and cash equivalents at end of period | \$ 45,177 | \$ 27,681 |
|--|-----------|-----------|

**Supplemental disclosures of cash flow information:**

|                        |          |          |
|------------------------|----------|----------|
| Cash paid for interest | \$ 1,608 | \$ 2,037 |
|------------------------|----------|----------|

|                            |    |        |
|----------------------------|----|--------|
| Cash paid for income taxes | \$ | \$ 865 |
|----------------------------|----|--------|

**Supplemental disclosures of non-cash investing and financing activities:**

|                                      |        |          |
|--------------------------------------|--------|----------|
| Transfers of loans receivable to REO | \$ 817 | \$ 1,937 |
|--------------------------------------|--------|----------|

|  |    |        |
|--|----|--------|
| Transfers of loans receivable held-for-sale to REO | \$ | \$ 266 |
|--|----|--------|

|   |    |          |
|---|----|----------|
| Transfers of loans receivable held-for-sale to other assets | \$ | \$ 7,662 |
|---|----|----------|

*See accompanying notes to unaudited consolidated financial statements.*

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**BROADWAY FINANCIAL CORPORATION AND SUBSIDIARIES**

**Notes to Unaudited Consolidated Financial Statements**

**March 31, 2012**

**NOTE (1) Basis of Financial Statement Presentation**

The accompanying unaudited consolidated financial statements include Broadway Financial Corporation (the Company) and its wholly owned subsidiary, Broadway Federal Bank, f.s.b. (the Bank). Also included in the unaudited consolidated financial statements is Broadway Service Corporation, a wholly owned subsidiary of the Bank. All significant intercompany balances and transactions have been eliminated in consolidation.

The unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions for quarterly reports on Form 10-Q. These unaudited consolidated financial statements do not include all disclosures associated with the Company's consolidated annual financial statements included in its Annual Report on Form 10-K for the year ended December 31, 2011 and, accordingly, should be read in conjunction with such audited consolidated financial statements. In the opinion of management, all adjustments (all of which are normal and recurring in nature) considered necessary for a fair presentation have been included. Operating results for the three months ended March 31, 2012 are not necessarily indicative of the results that may be expected for the year ending December 31, 2012.

Some items in the consolidated financial statements for the prior period were reclassified to conform to the current presentation.

**NOTE (2) Recently Issued Accounting Pronouncements**

In May 2011, the FASB issued an amendment to achieve common fair value measurement and disclosure requirements between U.S. and International accounting principles. Overall, the guidance is consistent with existing U.S. accounting principles; however, there are some amendments that change a particular principle or requirement for measuring fair value or for disclosing information about fair value measurements. The amendments in this guidance are effective for interim and annual reporting periods beginning after December 15, 2011. The adoption of this standard did not have a material effect on the Company's consolidated financial statements.

In June 2011, the FASB amended existing guidance and eliminated the option to present the components of other comprehensive income as part of the statement of changes in shareholder's equity. The amendment requires that comprehensive income be presented in either a single continuous statement or in two separate consecutive statements. The amendments in this guidance are effective as of the beginning of a fiscal reporting year, and interim periods within that year, that begins after December 15, 2011. Early adoption is permitted. The adoption of this amendment had no impact on the Company's consolidated financial statements as the prior presentation of comprehensive income was in compliance with this amendment.

**Table of Contents****BROADWAY FINANCIAL CORPORATION AND SUBSIDIARIES****Notes to Unaudited Consolidated Financial Statements (continued)****March 31, 2012****NOTE (3) Loss Per Common Share**

Basic loss per common share is computed by dividing loss available to common shareholders by the weighted average number of shares of common stock outstanding for the period. Diluted loss per common share is computed by dividing loss available to common shareholders by the weighted average number of shares of common stock outstanding for the period, increased for the dilutive effect of common stock equivalents.

The following table shows how the Company computed basic and diluted loss per common share for the three months ended March 31, 2012 and 2011.

|   | <b>For the three months ended March 31,<br/>2012                      2011</b> |              |
|---|--|--------------|
|   | <b>(Dollars in thousands, except per share)</b>                                |              |
| <b>Basic</b>  |  |              |
| Net earnings (loss)   | \$     154   | \$    (129)  |
| Less: Preferred stock dividends and accretion               | (286)  | (283)        |
| Loss available to common shareholders                       | \$    (132)  | \$    (412)  |
| Weighted average common shares outstanding                  | 1,744,565  | 1,743,965    |
| Loss per common share    basic                              | \$    (0.08)   | \$    (0.24) |
| <b>Diluted</b>  |  |              |
| Net earnings (loss)   | \$     154   | \$    (129)  |
| Less: Preferred stock dividends and accretion               | (286)  | (283)        |
| Loss available to common shareholders                       | \$    (132)  | \$    (412)  |
| Weighted average common shares outstanding                  | 1,744,565  | 1,743,965    |
| Add: dilutive effects of assumed exercises of stock options | N/A  | N/A          |
| Average shares and dilutive potential common shares         | 1,744,565  | 1,743,965    |
| Loss per common share    diluted                            | \$    (0.08)   | \$    (0.24) |

Stock options for 227,075 shares of common stock were not considered in computing diluted earnings per common share for the three months ended March 31, 2012 and 2011 because they were anti-dilutive.

**NOTE (4) Securities**

The following table summarizes the amortized cost and fair value of the available-for-sale investment securities portfolios at March 31, 2012 and December 31, 2011 and the corresponding amounts of unrealized gains which are recognized in accumulated other comprehensive income (loss) were as follows:

|                                     | Amortized Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Fair Value |
|-------------------------------------|----------------|------------------------------|-------------------------------|------------|
|                                     | (In thousands) |                              |                               |            |
| <b>March 31, 2012:</b>              |                |                              |                               |            |
| Residential mortgage-backed         | \$ 16,049      | \$ 919                       | \$                            | \$ 16,968  |
| U.S. Government and federal agency  | 1,000          | 59                           |                               | 1,059      |
| Total available-for-sale securities | \$ 17,049      | \$ 978                       | \$                            | \$ 18,027  |

**Table of Contents****BROADWAY FINANCIAL CORPORATION AND SUBSIDIARIES****Notes to Unaudited Consolidated Financial Statements (continued)****March 31, 2012**

|                                     | Amortized Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Fair Value |
|-------------------------------------|----------------|------------------------------|-------------------------------|------------|
|                                     | (In thousands) |                              |                               |            |
| <b>December 31, 2011:</b>           |                |                              |                               |            |
| Residential mortgage-backed         | \$ 17,008      | \$ 902                       | \$                            | \$ 17,910  |
| U.S. Government and federal agency  | 1,000          | 69                           |                               | 1,069      |
| Total available-for-sale securities | \$ 18,008      | \$ 971                       | \$                            | \$ 18,979  |

The amortized cost and fair value of the investment securities portfolios are shown by contractual maturity at March 31, 2012. Expected maturities may differ from contractual maturities if borrowers have the right to call or prepay obligations with or without call or prepayment penalties. Securities not due at a single maturity date, primarily residential mortgage-backed securities, are shown separately.

| Maturity                    | Available-for-Sale |            |
|-----------------------------|--------------------|------------|
|                             | Amortized Cost     | Fair Value |
|                             | (In thousands)     |            |
| Within one year             | \$                 | \$         |
| One to five years           | 1,000              | 1,059      |
| Five to ten years           |                    |            |
| Beyond ten years            |                    |            |
| Residential mortgage-backed | 16,049             | 16,968     |
| Total                       | \$ 17,049          | \$ 18,027  |

Securities pledged at March 31, 2012 and December 31, 2011 had a carrying amount of \$1.5 million and were pledged to secure public deposits. At March 31, 2012 and December 31, 2011, there were no holdings of securities of any one issuer, other than the U.S. Government and its agencies, in an amount greater than 10% of shareholders' equity. There were no sales of securities during the three months ended March 31, 2012 and 2011.

There were no securities with unrealized losses at March 31, 2012 and December 31, 2011. We evaluate securities for other-than-temporary impairment at least quarterly, and more frequently when economic or market concerns warrant such evaluation. Consideration is given to the financial condition and near-term prospects of the issuer, the length of time and the extent to which the fair value has been less than the cost, and our intent and ability to retain our investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value. In analyzing an issuer's financial condition, we consider whether the securities are issued by the federal government or its agencies, whether downgrades by bond rating agencies have occurred, and the results of reviews of the issuer's financial condition.

**NOTE (5) Loans Receivable Held-for-Sale, Net**

Loans receivable held-for-sale at March 31, 2012 and December 31, 2011 were as follows:

|                                | March 31, 2012 | December 31, 2011 |
|--------------------------------|----------------|-------------------|
|                                | (In thousands) |                   |
| Five or more units residential | \$ 6,358       | \$ 6,395          |

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|   |           |           |
|---|-----------|-----------|
| Commercial real estate                    | 1,703     | 1,712     |
| Church                                    | 5,514     | 5,550     |
| Valuation allowance for unrealized losses | (667)     | (674)     |
| Loans receivable, held for sale, net      | \$ 12,908 | \$ 12,983 |

**Table of Contents****BROADWAY FINANCIAL CORPORATION AND SUBSIDIARIES****Notes to Unaudited Consolidated Financial Statements (continued)****March 31, 2012**

Loans receivable held-for-sale, net, consisted of five or more units residential, commercial real estate and church loans originated for sale and five or more units residential loans transferred from our loan portfolio. Non-performing loans receivable held-for-sale included in loans receivable held-for-sale, net, totaled \$4.2 million, net of charge-offs of \$958 thousand and a \$375 thousand valuation allowance, as of March 31, 2012 and totaled \$5.2 million, net of charge-offs of \$953 thousand and a \$382 thousand valuation allowance, as of December 31, 2011. Restructured loans receivable held-for-sale on which the borrowers have complied with the terms of their restructured agreements for a satisfactory period of time and certain performing loans receivable held-for-sale with delinquency or other weaknesses totaled \$2.2 million, net of a \$292 thousand valuation allowance, as of March 31, 2012 and December 31, 2011. During the first quarter of 2012, no loans receivable held-for-sale were transferred to REO. A loan receivable held-for-sale secured by a church building, which had a carrying amount of \$266 thousand, net of a charge-off of \$292 thousand, was transferred to REO during the first quarter of 2011.

Net lower of cost or market recovery on non-performing loans receivable held-for-sale totaled \$1 thousand for the three months ended March 31, 2012, compared to \$0 for the same period in 2011. Additionally, during the first quarter of 2012, and 2011, we increased our valuation allowance by \$1 thousand and \$20 thousand, respectively, on some of our loans held for sale that are still considered performing loans.

**NOTE (6) Loans Receivable**

Loans at March 31, 2012 and December 31, 2011 were as follows:

|                                     | March 31, 2012    | December 31, 2011 |
|-------------------------------------|-------------------|-------------------|
|                                     | (In thousands)    |                   |
| Real estate:                        |                   |                   |
| One to four units                   | \$ 76,168         | \$ 76,682         |
| Five or more units                  | 103,617           | 108,161           |
| Commercial real estate              | 49,445            | 54,259            |
| Church                              | 87,413            | 89,099            |
| Construction                        | 3,746             | 3,790             |
| Commercial:                         |                   |                   |
| Sports                              | 1,990             | 1,996             |
| Other                               | 4,638             | 4,900             |
| Consumer:                           |                   |                   |
| Loan on savings                     | 13                | 821               |
| Other                               | 107               | 108               |
| <b>Total gross loans receivable</b> | <b>327,137</b>    | <b>339,816</b>    |
| Less:                               |                   |                   |
| Loans in process                    | 117               | 202               |
| Net deferred loan fees (costs)      | (328)             | (473)             |
| Unamortized discounts               | 18                | 18                |
| Allowance for loan losses           | 17,752            | 17,299            |
| <b>Loans receivable, net</b>        | <b>\$ 309,578</b> | <b>\$ 322,270</b> |

The following table presents the activity in the allowance for loan losses by portfolio segment for the three months ended March 31, 2012 and 2011:



## For the three months ended March 31, 2012

|                           | One to four<br>units | Five or<br>more<br>units | Commercial<br>real estate | Church   | Construction | Commercial | Consumer | Total     |
|---------------------------|----------------------|--------------------------|---------------------------|----------|--------------|------------|----------|-----------|
|                           | (In thousands)       |                          |                           |          |              |            |          |           |
| Beginning balance         | \$ 4,855             | \$ 2,972                 | \$ 3,108                  | \$ 5,742 | \$ 249       | \$ 247     | \$ 126   | \$ 17,299 |
| Provision for loan losses | 336                  | 41                       | (206)                     | 979      | (16)         | (133)      | (42)     | 959       |
| Recoveries                |                      |                          | 15                        | 4        |              | 117        | 2        | 138       |
| Loans charged off         | (355)                |                          | (58)                      | (231)    |              |            |          | (644)     |
| Ending balance            | \$ 4,836             | \$ 3,013                 | \$ 2,859                  | \$ 6,494 | \$ 233       | \$ 231     | \$ 86    | \$ 17,752 |

**Table of Contents****BROADWAY FINANCIAL CORPORATION AND SUBSIDIARIES****Notes to Unaudited Consolidated Financial Statements (continued)****March 31, 2012****For the three months ended March 31, 2011**

|                           | <b>One to four<br/>units</b> | <b>Five or<br/>more units</b> | <b>Commercial</b> | <b>Church</b> | <b>Construction</b> | <b>Commercial</b> | <b>Consumer</b> | <b>Total</b> |
|---------------------------|------------------------------|-------------------------------|-------------------|---------------|---------------------|-------------------|-----------------|--------------|
|                           | <b>(In thousands)</b>        |                               |                   |               |                     |                   |                 |              |
| Beginning balance         | \$ 4,579                     | \$ 2,469                      | \$ 3,493          | \$ 6,909      | \$ 74               | \$ 1,300          | \$ 1,634        | \$ 20,458    |
| Provision for loan losses | (564)                        | 153                           | 646               | 523           | (20)                | 298               | 204             | 1,240        |
| Recoveries                | 0                            | 0                             | 0                 | 0             | 0                   | 0                 | 2               | 2            |
| Loans charged off         | (38)                         | 0                             | (609)             | (45)          | 0                   | 0                 | (17)            | (709)        |
| Ending balance            | \$ 3,977                     | \$ 2,622                      | \$ 3,530          | \$ 7,387      | \$ 54               | \$ 1,598          | \$ 1,823        | \$ 20,991    |

The following table presents the balance in the allowance for loan losses and the recorded investment in loans by portfolio segment and based on impairment method as of March 31, 2012 and December 31, 2011:

|   | <b>March 31, 2012</b>        |                                   |                                   |               |                     |                   |                 |              |
|---|------------------------------|-----------------------------------|-----------------------------------|---------------|---------------------|-------------------|-----------------|--------------|
|   | <b>One to<br/>four units</b> | <b>Five or<br/>more<br/>units</b> | <b>Commercial<br/>real estate</b> | <b>Church</b> | <b>Construction</b> | <b>Commercial</b> | <b>Consumer</b> | <b>Total</b> |
|   | <b>(In thousands)</b>        |                                   |                                   |               |                     |                   |                 |              |
| <b>Allowance for loan losses:</b>               |                              |                                   |                                   |               |                     |                   |                 |              |
| Ending allowance balance attributable to loans: |                              |                                   |                                   |               |                     |                   |                 |              |
| Individually evaluated for impairment           | \$ 1,564                     | \$ 157                            | \$ 250                            | \$ 1,781      | \$ 91               | \$                | \$ 70           | \$ 3,913     |
| Collectively evaluated for impairment           | 3,272                        | 2,856                             | 2,609                             | 4,713         | 142                 | 231               | 16              | 13,839       |
| Total ending allowance balance                  | \$ 4,836                     | \$ 3,013                          | \$ 2,859                          | \$ 6,494      | \$ 233              | \$ 231            | \$ 86           | \$ 17,752    |
| <b>Loans:</b>                                   |                              |                                   |                                   |               |                     |                   |                 |              |
| Loans individually evaluated for impairment     | \$ 14,035                    | \$ 3,814                          | \$ 7,839                          | \$ 32,901     | \$ 296              | \$                | \$ 70           | \$ 58,955    |
| Loans collectively evaluated for impairment     | 62,133                       | 99,803                            | 41,606                            | 54,512        | 3,450               | 6,628             | 50              | 268,182      |
| Total ending loans balance                      | \$ 76,168                    | \$ 103,617                        | \$ 49,445                         | \$ 87,413     | \$ 3,746            | \$ 6,628          | \$ 120          | \$ 327,137   |

**December 31, 2011**

|   | <b>One to<br/>four units</b> | <b>Five or<br/>more<br/>units</b> | <b>Commercial<br/>real estate</b> | <b>Church</b> | <b>Construction</b> | <b>Commercial</b> | <b>Consumer</b> | <b>Total</b> |
|---|------------------------------|-----------------------------------|-----------------------------------|---------------|---------------------|-------------------|-----------------|--------------|
|   | <b>(In thousands)</b>        |                                   |                                   |               |                     |                   |                 |              |
| <b>Allowance for loan losses:</b>               |                              |                                   |                                   |               |                     |                   |                 |              |
| Ending allowance balance attributable to loans: |                              |                                   |                                   |               |                     |                   |                 |              |

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|                                       |          |          |          |          |        |        |        |           |
|---------------------------------------|----------|----------|----------|----------|--------|--------|--------|-----------|
| Individually evaluated for impairment | \$ 1,678 | \$ 161   | \$ 255   | \$ 1,683 | \$ 97  | \$     | \$ 70  | \$ 3,944  |
| Collectively evaluated for impairment | 3,177    | 2,811    | 2,853    | 4,059    | 152    | 247    | 56     | 13,355    |
| Total ending allowance balance        | \$ 4,855 | \$ 2,972 | \$ 3,108 | \$ 5,742 | \$ 249 | \$ 247 | \$ 126 | \$ 17,299 |

**Loans:**

|   |           |            |           |           |          |          |        |            |
|---|-----------|------------|-----------|-----------|----------|----------|--------|------------|
| Loans individually evaluated for impairment | \$ 13,246 | \$ 3,837   | \$ 7,396  | \$ 31,494 | \$ 302   | \$       | \$ 70  | \$ 56,345  |
| Loans collectively evaluated for impairment | 63,436    | 104,324    | 46,863    | 57,605    | 3,488    | 6,896    | 859    | 283,471    |
| Total ending loans balance                  | \$ 76,682 | \$ 108,161 | \$ 54,259 | \$ 89,099 | \$ 3,790 | \$ 6,896 | \$ 929 | \$ 339,816 |

**Table of Contents****BROADWAY FINANCIAL CORPORATION AND SUBSIDIARIES****Notes to Unaudited Consolidated Financial Statements (continued)****March 31, 2012**

The following table presents information related to impaired loans by class of loans as of and for the three months ended March 31, 2012 and 2011:

|  | March 31, 2012                 |                        |  |                                   |   |
|--|--------------------------------|------------------------|--|-----------------------------------|---|
|  | Unpaid<br>Principal<br>Balance | Recorded<br>Investment | Allowance<br>for Loan<br>Losses<br>Allocated<br>(In thousands) | Average<br>Recorded<br>Investment | Cash<br>Basis<br>Interest<br>Income<br>Recognized |
| <b>With no related allowance recorded:</b> |                                |                        |  |                                   |   |
| One to four units                          | \$ 9,938                       | \$ 7,842               | \$   | \$ 7,687                          | \$ 40   |
| Five or more units                         | 2,940                          | 2,852                  |  | 2,862                             | 6   |
| Commercial real estate                     | 9,640                          | 5,902                  |  | 5,535                             | 60  |
| Church                                     | 26,154                         | 21,979                 |  | 21,479                            | 128   |
| Commercial:                                |                                |                        |  |                                   |   |
| Sports                                     | 4,000                          |                        |  |                                   |   |
| Other                                      | 285                            |                        |  |                                   |   |
| <b>With an allowance recorded:</b>         |                                |                        |  |                                   |   |
| One to four units                          | 6,302                          | 6,194                  | 1,564  | 5,790                             | 84  |
| Five or more units                         | 962                            | 962                    | 157  | 964                               | 16  |
| Commercial real estate                     | 1,936                          | 1,936                  | 250  | 1,941                             | 24  |
| Church                                     | 10,922                         | 10,922                 | 1,781  | 10,289                            | 163   |
| Construction                               | 296                            | 296                    | 91   | 300                               | 5   |
| Commercial:                                |                                |                        |  |                                   |   |
| Other                                      | 70                             | 70                     | 70   | 70                                | 1   |
| <b>Total</b>                               | <b>\$ 73,445</b>               | <b>\$ 58,955</b>       | <b>\$ 3,913</b>  | <b>\$ 56,917</b>                  | <b>\$ 527</b>                                     |

|  | March 31, 2011                 |                        |  |                                   |   |
|--|--------------------------------|------------------------|--|-----------------------------------|---|
|  | Unpaid<br>Principal<br>Balance | Recorded<br>Investment | Allowance<br>for Loan<br>Losses<br>Allocated<br>(In thousands) | Average<br>Recorded<br>Investment | Cash<br>Basis<br>Interest<br>Income<br>Recognized |
| <b>With no related allowance recorded:</b> |                                |                        |  |                                   |   |
| One to four units                          | \$ 6,920                       | \$ 5,758               | \$   | \$ 5,762                          | \$ 15   |
| Five or more units                         | 205                            | 205                    |  | 194                               |   |
| Commercial real estate                     | 7,734                          | 7,320                  |  | 7,620                             | 20  |
| Church                                     | 14,367                         | 13,847                 |  | 11,857                            | 50  |
| Construction                               | 320                            | 320                    |  | 320                               |   |
| <b>With an allowance recorded:</b>         |                                |                        |  |                                   |   |
| One to four units                          | 6,808                          | 3,641                  | 475  | 3,603                             | 50  |
| Five or more units                         | 1,673                          | 1,673                  | 69   | 1,674                             |   |

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|                        |                  |                  |                 |                  |               |
|------------------------|------------------|------------------|-----------------|------------------|---------------|
| Commercial real estate | 5,193            | 4,998            | 812             | 4,538            | 32            |
| Church                 | 16,943           | 16,806           | 3,086           | 16,097           | 181           |
| Commercial:            |                  |                  |                 |                  |               |
| Sports                 | 4,000            | 3,698            | 948             | 3,751            |               |
| Other                  | 288              | 288              | 288             | 218              |               |
| Consumer:              |                  |                  |                 |                  |               |
| Loan on savings        | 1,778            | 1,778            | 1,778           | 2,131            |               |
| <b>Total</b>           | <b>\$ 63,229</b> | <b>\$ 60,332</b> | <b>\$ 7,456</b> | <b>\$ 57,765</b> | <b>\$ 348</b> |

**Table of Contents****BROADWAY FINANCIAL CORPORATION AND SUBSIDIARIES****Notes to Unaudited Consolidated Financial Statements (continued)****March 31, 2012**

The following table presents information related to impaired loans by class of loans as of and for year ended December 31, 2011:

|  | December 31, 2011              |                        |  |                                   | Cash<br>Basis<br>Interest<br>Income<br>Recognized |
|--|--------------------------------|------------------------|--|-----------------------------------|---|
|  | Unpaid<br>Principal<br>Balance | Recorded<br>Investment | Allowance<br>for Loan<br>Losses<br>Allocated<br>(In thousands) | Average<br>Recorded<br>Investment |   |
| <b>With no related allowance recorded:</b> |                                |                        |  |                                   |   |
| One to four units                          | \$ 6,904                       | \$ 4,636               | \$   | \$ 5,329                          | \$ 79   |
| Five or more units                         | 2,946                          | 2,871                  |  | 2,405                             | 89  |
| Commercial real estate                     | 9,105                          | 5,449                  |  | 9,724                             | 386   |
| Church                                     | 24,680                         | 20,560                 |  | 20,757                            | 740   |
| Commercial:                                |                                |                        |  |                                   |   |
| Sports                                     | 4,000                          |                        |  | 2,566                             |   |
| Other                                      | 285                            |                        |  | 243                               | 10  |
| Consumer:                                  |                                |                        |  |                                   |   |
| Loan on savings                            |                                |                        |  | 796                               |   |
| <b>With an allowance recorded:</b>         |                                |                        |  |                                   |   |
| One to four units                          | 8,610                          | 8,610                  | 1,678  | 5,507                             | 407   |
| Five or more units                         | 966                            | 966                    | 161  | 794                               | 64  |
| Commercial real estate                     | 1,947                          | 1,947                  | 255  | 1,963                             | 97  |
| Church                                     | 10,934                         | 10,934                 | 1,683  | 9,391                             | 705   |
| Construction                               | 302                            | 302                    | 97   | 314                               | 23  |
| Commercial:                                |                                |                        |  |                                   |   |
| Other                                      | 70                             | 70                     | 70   | 54                                | 6   |
| <b>Total</b>                               | <b>\$ 70,749</b>               | <b>\$ 56,345</b>       | <b>\$ 3,944</b>  | <b>\$ 59,843</b>                  | <b>\$ 2,606</b>                                   |

The recorded investment in loans excludes accrued interest receivable and loan origination fees, net due to immateriality. For purposes of this disclosure, the unpaid principal balance is not reduced for net charge-offs. Cash-basis interest income recognized represents cash received for interest payments on accruing impaired loans. Interest income that would have been recognized for the three months ended March 31, 2012 had loans performed in accordance with their original terms was \$1.2 million.

The following table presents the recorded investment in non-accrual loans by class of loans as of March 31, 2012 and December 31, 2011:

|   | March 31, 2012 | December 31, 2011 |
|---|----------------|-------------------|
|   | (In thousands) |                   |
| <b>Loans receivable, held for sale:</b> |                |                   |
| Five or more units                      | \$ 2,473       | \$ 2,496          |
| Commercial real estate                  | 333            | 338               |
| Church                                  | 2,749          | 2,778             |
| <b>Loans receivable, net:</b>           |                |                   |

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|                                |                  |                  |
|--------------------------------|------------------|------------------|
| One to four-units              | 8,792            | 7,974            |
| Five or more units             | 3,429            | 3,450            |
| Commercial real estate         | 5,902            | 5,449            |
| Church                         | 23,388           | 21,891           |
| Construction                   | 296              | 302              |
| Consumer:                      |                  |                  |
| Other                          | 70               | 70               |
| <b>Total non-accrual loans</b> | <b>\$ 47,432</b> | <b>\$ 44,748</b> |

There were no loans 90 days or more delinquent that were accruing interest as of March 31, 2012 or December 31, 2011.

**Table of Contents****BROADWAY FINANCIAL CORPORATION AND SUBSIDIARIES****Notes to Unaudited Consolidated Financial Statements (continued)****March 31, 2012**

The following tables present the aging of the recorded investment in past due loans, including loans held for sale, as of March 31, 2012 and December 31, 2011 by class of loans:

|   | March 31, 2012            |                           |   |                   |                             |
|---|---------------------------|---------------------------|---|-------------------|-----------------------------|
|   | 30-59<br>Days<br>Past Due | 60-89<br>Days<br>Past Due | Greater than<br>90 Days<br>Past Due<br>(In thousands) | Total<br>Past Due | Total Loans<br>Not Past Due |
| <b>Loans receivable, held for sale:</b> |                           |                           |   |                   |                             |
| Five or more units                      | \$ 658                    | \$                        | \$ 2,473  | \$ 3,131          | \$ 3,227                    |
| Commercial real estate                  |                           |                           | 333   | 333               | 1,370                       |
| Church                                  |                           |                           | 2,749   | 2,749             | 2,765                       |
| <b>Loans receivable, net:</b>           |                           |                           |   |                   |                             |
| One to four units                       | 2,804                     |                           | 8,792   | 11,596            | 64,572                      |
| Five or more units                      | 499                       |                           | 3,429   | 3,928             | 99,689                      |
| Commercial real estate                  | 991                       | 835                       | 5,902   | 7,728             | 41,717                      |
| Church                                  | 936                       | 383                       | 23,388  | 24,707            | 62,706                      |
| Construction                            |                           |                           | 296   | 296               | 3,450                       |
| <b>Commercial:</b>                      |                           |                           |   |                   |                             |
| Sports                                  |                           |                           |   |                   | 1,990                       |
| Other                                   |                           | 98                        |   | 98                | 4,540                       |
| <b>Consumer:</b>                        |                           |                           |   |                   |                             |
| Loan on savings                         |                           |                           |   |                   | 13                          |
| Other                                   |                           |                           | 70  | 70                | 37                          |
| <b>Total</b>                            | <b>\$ 5,888</b>           | <b>\$ 1,316</b>           | <b>\$ 47,432</b>                                      | <b>\$ 54,636</b>  | <b>\$ 286,076</b>           |

|   | December 31, 2011         |                           |   |                   |                             |
|---|---------------------------|---------------------------|---|-------------------|-----------------------------|
|   | 30-59<br>Days<br>Past Due | 60-89<br>Days<br>Past Due | Greater than<br>90 Days<br>Past Due<br>(In thousands) | Total<br>Past Due | Total Loans<br>Not Past Due |
| <b>Loans receivable, held for sale:</b> |                           |                           |   |                   |                             |
| Five or more units                      | \$                        | \$                        | \$ 2,496  | \$ 2,496          | \$ 3,899                    |
| Commercial real estate                  |                           |                           | 338   | 338               | 1,374                       |
| Church                                  |                           |                           | 2,778   | 2,778             | 2,772                       |
| <b>Loans receivable, net:</b>           |                           |                           |   |                   |                             |
| One to four units                       | 921                       | 2,464                     | 7,974   | 11,359            | 65,323                      |
| Five or more units                      | 1,324                     | 63                        | 3,450   | 4,837             | 103,324                     |
| Commercial real estate                  | 2,247                     | 525                       | 5,449   | 8,221             | 46,038                      |
| Church                                  | 2,647                     | 1,440                     | 21,891  | 25,978            | 63,121                      |
| Construction                            |                           | 264                       | 302   | 566               | 3,224                       |
| <b>Commercial:</b>                      |                           |                           |   |                   |                             |
| Sports                                  |                           |                           |   |                   | 1,996                       |



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|                 |          |          |           |           |            |
|-----------------|----------|----------|-----------|-----------|------------|
| Other           | 125      |          |           | 125       | 4,775      |
| Consumer:       |          |          |           |           |            |
| Loan on savings |          |          |           |           | 821        |
| Other           |          |          | 70        | 70        | 38         |
| Total           | \$ 7,264 | \$ 4,756 | \$ 44,748 | \$ 56,768 | \$ 296,705 |

**Table of Contents****BROADWAY FINANCIAL CORPORATION AND SUBSIDIARIES****Notes to Unaudited Consolidated Financial Statements (continued)****March 31, 2012****Troubled Debt Restructurings**

The Company has allocated \$2.6 million of specific reserves for loans the terms of which have been modified in troubled debt restructurings and were performing as of March 31, 2012 and December 31, 2011. At March 31, 2012, loans classified as a TDR totaled \$38.1 million, of which \$20.5 million were included in non-accrual loans and \$17.6 million were on accrual status. At December 31, 2011, loans classified as a TDR totaled \$37.1 million, of which \$19.4 million were included in non-accrual loans and \$17.7 million were on accrual status. TDRs on accrual status are comprised of loans that were accruing at the time of restructuring or loans that have complied with the terms of their restructured agreements for a satisfactory period of time, and for which the Bank anticipates full repayment of both principal and interest. TDRs that are on non-accrual can be returned to accrual status after a period of sustained performance, generally determined to be six months of timely payments as modified. As of March 31, 2012 and December 31, 2011, the Company has no commitment to lend additional amounts to customers with outstanding loans that are classified as troubled debt restructurings.

During the three months ended March 31, 2012, the terms of certain loans were modified as troubled debt restructurings. The modification of the terms of such loans included one of the following: a reduction of the stated interest rate of the loan or an extension of the maturity date at a stated rate of interest lower than the current market rate for new debt with similar risk.

Modifications involving a reduction of the stated interest rate of the loan were for periods ranging from 2 years to 5 years. The modification involving an extension of the maturity date was for a 2 year period.

The following table presents loans by class modified as troubled debt restructurings that occurred during the three months ended March 31, 2012:

|                        | Number of<br>Loans | Pre-Modification<br>Outstanding<br>Recorded<br>Investment<br>(Dollars in thousands) | Post-Modification<br>Outstanding<br>Recorded<br>Investment |
|------------------------|--------------------|---|--|
| Commercial real estate | 1                  | \$ 229  | \$ 229   |
| Church                 | 3                  | 1,013   | 1,013  |
| <b>Total</b>           | <b>4</b>           | <b>\$ 1,242</b>   | <b>\$ 1,242</b>  |

The troubled debt restructurings described above increased the allowance for loan losses by \$87 thousand during the three months ended March 31, 2012.

A loan is considered to be in payment default once it is 90 days contractually past due under the modified terms. The following table presents loans by class modified as troubled debt restructurings for which there was a payment default within twelve months following the modification during the three months ended March 31, 2012:

| Number of<br>Loans | Pre-Modification<br>Outstanding<br>Recorded<br>Investment<br>(Dollars in thousands) |
|--------------------|---|
|--------------------|---|

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|        |   |    |     |
|--------|---|----|-----|
| Church | 1 | \$ | 100 |
| Total  | 1 | \$ | 100 |

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**BROADWAY FINANCIAL CORPORATION AND SUBSIDIARIES**

**Notes to Unaudited Consolidated Financial Statements (continued)**

**March 31, 2012**

The terms of certain other loans were modified during the three months ended March 31, 2012 that did not meet the definition of a troubled debt restructuring. These loans have a total recorded investment as of March 31, 2012 of \$3.2 million. The modification of these loans involved either a modification of the terms of a loan to borrowers who were not experiencing financial difficulties or a delay in a payment that was considered to be insignificant.

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

**Credit Quality Indicators**

The Company categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. For one-to-four family residential, consumer and other smaller balance homogenous loans, a credit grade is established at inception, and generally only adjusted based on performance. Information about payment status is disclosed elsewhere. The Company analyzes all other loans individually by classifying the loans as to credit risk. This analysis is performed at least on a quarterly basis. The Company uses the following definitions for risk ratings:

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

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

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

***Loss.*** Loans classified as loss are considered uncollectible and of such little value that to continue to carry the loan as an active asset is no longer warranted.

**Table of Contents****BROADWAY FINANCIAL CORPORATION AND SUBSIDIARIES****Notes to Unaudited Consolidated Financial Statements (continued)****March 31, 2012**

Loans not meeting the criteria above that are analyzed individually as part of the above described process are considered to be pass rated loans. Based on the most recent analysis performed, the risk category of loans by class of loans as of March 31, 2012 and December 31, 2011 is as follows:

|                        | <b>March 31, 2012</b> |                        |                    |                 |             |
|------------------------|-----------------------|------------------------|--------------------|-----------------|-------------|
|                        | <b>Pass</b>           | <b>Special Mention</b> | <b>Substandard</b> | <b>Doubtful</b> | <b>Loss</b> |
|                        | <b>(In thousands)</b> |                        |                    |                 |             |
| One to four units      | \$ 62,183             | \$ 3,025               | \$ 10,784          | \$ 176          | \$          |
| Five or more units     | 90,876                | 5,710                  | 6,882              | 149             |             |
| Commercial real estate | 31,290                | 6,305                  | 11,778             | 72              |             |
| Church                 | 36,342                | 10,723                 | 39,842             | 506             |             |
| Construction           | 489                   | 2,961                  | 296                |                 |             |
| Commercial:            |                       |                        |                    |                 |             |
| Sports                 |                       | 1,990                  |                    |                 |             |
| Other                  | 2,303                 | 2,237                  | 98                 |                 |             |
| Consumer:              |                       |                        |                    |                 |             |
| Loan on savings        | 13                    |                        |                    |                 |             |
| Other                  | 37                    |                        | 70                 |                 |             |
| Total                  | \$ 223,533            | \$ 32,951              | \$ 69,750          | \$ 903          | \$          |

|                        | <b>December 31, 2011</b> |                        |                    |                 |             |
|------------------------|--------------------------|------------------------|--------------------|-----------------|-------------|
|                        | <b>Pass</b>              | <b>Special Mention</b> | <b>Substandard</b> | <b>Doubtful</b> | <b>Loss</b> |
|                        | <b>(In thousands)</b>    |                        |                    |                 |             |
| One to four units      | \$ 63,483                | \$ 3,044               | \$ 9,846           | \$ 309          | \$          |
| Five or more units     | 95,621                   | 7,450                  | 4,939              | 151             |             |
| Commercial real estate | 36,098                   | 6,721                  | 11,364             | 76              |             |
| Church                 | 37,532                   | 13,100                 | 37,873             | 594             |             |
| Construction           | 500                      | 2,988                  | 302                |                 |             |
| Commercial:            |                          |                        |                    |                 |             |
| Sports                 |                          | 1,996                  |                    |                 |             |
| Other                  | 2,363                    | 2,369                  | 168                |                 |             |
| Consumer:              |                          |                        |                    |                 |             |
| Loan on savings        | 821                      |                        |                    |                 |             |
| Other                  | 108                      |                        |                    |                 |             |
| Total                  | \$ 236,526               | \$ 37,668              | \$ 64,492          | \$ 1,130        | \$          |

**Table of Contents****BROADWAY FINANCIAL CORPORATION AND SUBSIDIARIES****Notes to Unaudited Consolidated Financial Statements (continued)****March 31, 2012****NOTE (7) Junior Subordinated Debentures, Other Borrowings and Management's Capital Plan**

On March 17, 2004, the Company issued \$6.0 million of Floating Rate Junior Subordinated Debentures in a private placement. The debentures mature in 10 years and interest is payable quarterly at a rate per annum equal to the 3-month LIBOR plus 2.54%. The interest rate is determined as of each March 17, June 17, September 17, and December 17, and was 3.01% at March 31, 2012. The Company stopped paying interest on the debentures and the senior line of credit discussed below in September 2010. Under the cease and desist order applicable to the Company discussed in Note 10, the Company is not permitted to make payments on its debt without prior notice to and receipt of written notice of non-objection from the Board of Governors of the Federal Reserve System, acting through the Federal Reserve Bank of San Francisco, (the FRB ). In addition, under the terms of the subordinated debentures, the Company is not allowed to make payments on the subordinated debentures if the Company is in default on any of its senior indebtedness, which term includes the senior line of credit described below.

On February 28, 2010, the Company borrowed an aggregate of \$5.0 million under its \$5.0 million line of credit with another financial institution, and invested all of the proceeds in the equity capital of the Bank. The interest rate on the line of credit adjusts annually, subject to a minimum of 6.00% and increases by an additional 5% in the event of default. Borrowings under this line of credit are secured by the Company's assets. The full amount of this borrowing became due and payable on July 31, 2010. This senior line of credit has not been repaid and the Company is now in default under the line of credit agreement. On April 7, 2011, the lender agreed to forbear from exercising its rights (other than increasing the interest rate by the default rate margin) pursuant to the line of credit agreement until January 1, 2012 subject to certain conditions. The lender has informed the Company that it does not intend to extend the forbearance agreement.

The Company is pursuing a comprehensive recapitalization plan to improve the Company's capital structure. To date, the Company has entered into a written agreement with the U.S. Department of the Treasury pursuant to which the U.S. Treasury will exchange its holdings of the Company's Series D and Series E Fixed Rate Cumulative Perpetual Preferred Stock for common stock at a discount of 50% of the liquidation amount, plus an undiscounted exchange of the accumulated but unpaid dividends on such preferred stock for common stock. The exchange by the U.S. Treasury is subject to various conditions, including the exchange of the Company's other outstanding series of preferred stock at discounts of 50% of the aggregate liquidation values, the placement of at least \$5 million of new common equity capital, and other conditions. The Exchange is expected to close contemporaneously with the closing of the private placement and the other exchange transactions. In addition, the Company has entered into a written agreement with the holder of Series A Perpetual Preferred Stock pursuant to which the holder will exchange its holdings of Series A Preferred for common stock at a discount of 50% of the liquidation amount. This exchange is subject to various conditions, including the exchange of the Company's other outstanding series of preferred stock, the placement of new common equity capital, and other conditions. The Company is in discussions with the holders of its Series B Perpetual Preferred Stock and Series C Noncumulative Perpetual Convertible Preferred Stock to exchange their holdings for common stock at a discount of 50% of the liquidation amount. The Company has also proposed to the line of credit lender that it exchange a portion of the line of credit, which is currently in default, for common stock at 100% of the face amount to be exchanged; to forgive the accrued interest on the entire amount of the line of credit to the date of the exchange; and enter into a modified credit agreement for the remainder of the facility that would be outstanding after the exchange.

As a condition to consummating these exchanges, the Company plans to concurrently complete private placements or other sales of the Company's common stock aggregating \$5 million, or \$3.5 million if approved by the U.S. Department of the Treasury, or more in gross proceeds. The Company anticipates that these exchanges and placements and sales of common stock would, if completed, result in the issuance of approximately 17.1 million new shares of the Company's common stock, which would constitute approximately 91% of the pro forma outstanding shares of the Company's common stock. The 17.1 million new shares of common stock exceed the Company's current unissued and authorized shares. The Company plans to seek shareholder approval to increase the Company's authorized shares, and issue a portion of such shares in the recapitalization.

There can be no assurance that management's capital plan will be achieved. If the Company is unable to raise capital, management plans to continue to shrink assets, sell the Bank's headquarters building, decrease nonperforming assets and implement strategies to increase earnings. The sale of the Bank's headquarters building was completed in the second quarter of 2012. Failure to maintain capital sufficient to meet the higher capital requirements could result in further regulatory action, which could include the appointment of a conservator or receiver for the Bank. For further information relating to the cash position and requirements of the Company, see Note 12 Going Concern.



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**BROADWAY FINANCIAL CORPORATION AND SUBSIDIARIES**

**Notes to Unaudited Consolidated Financial Statements (continued)**

**March 31, 2012**

**NOTE (8) Fair Value**

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

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

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

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

The Company used the following methods and significant assumptions to estimate fair value:

The fair values of securities available-for-sale are determined by obtaining quoted prices on nationally recognized securities exchanges (Level 1 inputs) or matrix pricing, which is a mathematical technique to value debt securities without relying exclusively on quoted prices for the specific securities, but rather by relying on the securities' relationship to other benchmark quoted securities (Level 2 inputs).

The fair value of non-performing loans receivable held-for-sale is generally based upon the fair value of the collateral which is obtained from recent real estate appraisals. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the independent appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are typically significant and result in a Level 3 classification of the inputs for determining fair value. Non-performing loans held for sale are evaluated on a quarterly basis for additional impairment and adjusted accordingly.

At the time a loan is considered impaired, it is valued at the lower of cost or fair value. Impaired loans carried at fair value generally receive specific allocations of the allowance for loan losses. For collateral dependent loans, fair value is commonly based on recent real estate appraisals. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the independent appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are usually significant and typically result in a Level 3 classification of the inputs for determining fair value. Impaired loans are evaluated on a quarterly basis for additional impairment and adjusted accordingly.

Assets acquired through or instead of loan foreclosure are initially recorded at fair value less costs to sell when acquired, establishing a new cost basis. These assets are subsequently accounted for at lower of cost or fair value less estimated costs to sell. Fair value is commonly based on recent real estate appraisals. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the independent appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are usually significant and typically result in a Level 3 classification of the inputs for determining fair value. Real estate owned is reviewed and evaluated on at least an annual basis for additional impairment and adjusted accordingly.

On a quarterly basis, fair value is determined based on a valuation model that calculates the present value of estimated future net servicing income (Level 3 inputs).





**Table of Contents****BROADWAY FINANCIAL CORPORATION AND SUBSIDIARIES****Notes to Unaudited Consolidated Financial Statements (continued)****March 31, 2012****Assets Measured on a Recurring Basis**

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

|  | Fair Value Measurements at March 31, 2012 Using                       |   |  | Total     |
|--|---|---|--|-----------|
|  | Quoted Prices   |   |  |           |
|  | in<br>Active<br>Markets<br>for<br>Identical<br>Assets<br>(Level<br>1) | Significant<br>Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) |           |
|  |   |   |  |           |
| <b>Assets:</b>   |   |   |  |           |
| Securities available-for-sale - residential mortgage-backed      | \$  | \$ 16,968   | \$   | \$ 16,968 |
| Securities available-for-sale U.S. government and federal agency |   | 1,059   |  | 1,059     |
| Mortgage servicing rights  |   |   | 183  | 183       |

|  | Fair Value Measurements at December 31, 2011 Using                    |   |  | Total     |
|--|---|---|--|-----------|
|  | Quoted Prices   |   |  |           |
|  | in<br>Active<br>Markets<br>for<br>Identical<br>Assets<br>(Level<br>1) | Significant<br>Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) |           |
|  |   |   |  |           |
| <b>Assets:</b>   |   |   |  |           |
| Securities available-for-sale - residential mortgage-backed      | \$  | \$ 17,910   | \$   | \$ 17,910 |
| Securities available-for-sale U.S. government and federal agency |   | 1,069   |  | 1,069     |
| Mortgage servicing rights  |   |   | 363  | 363       |

There were no transfers between Level 1 and Level 2 during the first quarter of 2012 and 2011.

The table below presents a reconciliation of the mortgage servicing rights asset which is measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the three months ended March 31, 2012 and 2011:

|                             | 2012           | 2011   |
|-----------------------------|----------------|--------|
|                             | (In thousands) |        |
| Balance at January 1,       | \$ 363         | \$ 487 |
| Other changes in fair value | (180)          | (62)   |

|                      |        |        |
|----------------------|--------|--------|
| Balance at March 31, | \$ 183 | \$ 425 |
|----------------------|--------|--------|

**Table of Contents****BROADWAY FINANCIAL CORPORATION AND SUBSIDIARIES****Notes to Unaudited Consolidated Financial Statements (continued)****March 31, 2012****Assets Measured on a Non-Recurring Basis**

The following table provides information regarding the carrying values of our assets measured at fair value on a non-recurring basis at the dates indicated. The fair value measurement for all of these assets falls within Level 3 of the fair value hierarchy.

|   | March 31, 2012 | December 31, 2011 |
|---|----------------|-------------------|
|   | (In thousands) |                   |
| <b>Assets:</b>                                      |                |                   |
| Non-performing loans receivable held-for-sale, net: |                |                   |
| Five or more units                                  | \$ 2,098       | \$ 2,114          |
| Commercial real estate                              | 333            | 338               |
| Church  | 2,749          | 2,778             |
| Impaired loans carried at fair value of collateral: |                |                   |
| One to four units                                   | 4,222          | 6,201             |
| Five or more units                                  | 867            | 874               |
| Commercial real estate                              | 3,531          | 2,869             |
| Church  | 13,705         | 13,153            |
| Construction  | 205            | 205               |
| Real estate owned:                                  |                |                   |
| One to four units                                   | 603            | 718               |
| Commercial real estate                              | 391            | 3,126             |
| Church  | 2,964          | 2,855             |

Collateral-dependent impaired loans and non-performing loans held for sale are measured for impairment using the fair value of the collateral. To determine the fair value of collateral, the Company primarily relies on third party appraisals, which is generally obtained every six to nine months. For one-to-four family residential loans, appraised values are based on comparative sales approach. A significant unobservable input in the sales approach is the adjustment for the differences between the comparable sales. At March 31, 2012, these adjustments ranged from an upward adjustment of 11% to a discount of 18%. For five or more units residential, commercial real estate and church loans, appraisers may use a single valuation approach or a combination of approaches such as comparative sales, cost or income approach. At March 31, 2012, adjustments made on five or more units residential, commercial real estate and church loans valued using the comparable sales approach ranged from an upward adjustment of 11% to a discount of 45%. A significant unobservable input in the income approach is the estimated income capitalization rate. At March 31, 2012, capitalization rates of 6.50% to 12% were utilized to determine the fair value of the underlying collateral of three commercial real estate loans and a capitalization rate of 7% was utilized to determine the fair value of the underlying collateral of a church loan. The Company's calculation of net realizable value considers any liens in place on the underlying collateral.

Real estate owned is measured at fair value less estimated costs to sell. The fair value of REO is determined using a third party appraisal and is based on comparative sales, cost or income approach, or a combination of these approaches. A significant unobservable input in the sales approach is the adjustment for the differences between the comparable sales. At March 31, 2012, these adjustments ranged from an upward adjustment of 3% to a discount of 34%. A significant unobservable input in the income approach is the estimated income capitalization rate. At March 31, 2012, a capitalization rate of 9% was utilized to determine the fair value of the underlying collateral of a commercial real estate loan and 8% and 11.50% capitalization rates were utilized to determine the fair value of the underlying collateral of two church loans.

**Table of Contents****BROADWAY FINANCIAL CORPORATION AND SUBSIDIARIES****Notes to Unaudited Consolidated Financial Statements (continued)****March 31, 2012**

The following table provides information regarding our assets measured at fair value on a non-recurring basis at March 31, 2012 and 2011, and the losses recognized on these assets for the three months ended March 31, 2012 and 2011.

|  | Principal<br>Amount<br>at | Valuation<br>Allowance<br>at<br>March 31, 2012 | Losses for the<br>three<br>months<br>ended | Principal<br>Amount<br>at | Valuation<br>Allowance<br>at<br>March 31, 2011 | Losses for the<br>three<br>months<br>ended |
|--|---------------------------|--|--|---------------------------|--|--|
|  | (In thousands)            |  |  |                           |  |  |
| Non-performing loans receivable held-for-sale, net (1) | \$ 5,555                  | \$ 375   | \$ (1)                                     | \$ 5,982                  | \$ 769   | \$   |
| Impaired loans carried at fair value of collateral (2) | 23,781                    | 1,251  | 1,090                                      | 26,219                    | 6,415  | 2,112                                      |
| Real estate owned (3)                                  | 4,146                     | 188  | (19)                                       | 5,175                     | 52   | 80   |
| Total  | \$ 33,482                 | \$ 1,814                                       | \$ 1,070                                   | \$ 37,376                 | \$ 7,236                                       | \$ 2,192                                   |

- (1) Losses are charged to provision for losses on loans receivable held-for-sale.
- (2) Losses are charged against the allowance for loan losses. Includes \$20.0 million and \$5.0 million of loans that were carried at cost at March 31, 2012 and 2011 as the fair value of the collateral on these loans exceeded the book value as a result of charge-offs.
- (3) Losses are charged against the allowance for loan losses in the case of a write-down upon the transfer of a loan to REO. Losses subsequent to the transfer of a loan to REO are charged to provision for losses on REO.

The following table provides information regarding our assets measured at fair value on a non-recurring basis at December 31, 2011, and the losses recognized on these assets for the year ended December 31, 2011.

|  | Principal<br>Amount<br>at<br>December 31,<br>2011 | Valuation<br>Allowance<br>at<br>December 31,<br>2011 | Losses for the<br>year ended<br>December 31,<br>2011 |
|--|---|--|--|
|  | (In thousands)                                    |  |  |
| Non-performing loans receivable held-for-sale, net (1) | \$ 5,612  | \$ 382   | \$ 1,563   |
| Impaired loans carried at fair value of collateral (2) | 24,669  | 1,367  | 11,548   |
| Real estate owned (3)                                  | 7,046   | 347  | 2,654  |
| Total  | \$ 37,327   | \$ 2,096   | \$ 15,765  |

- (1) Losses are charged to provision for losses on loans receivable held-for-sale.
- (2) Losses are charged against the allowance for loan losses. Includes \$18.6 million of loans that were carried at cost as the fair value of the collateral on these loans exceeded the book value as a result of charge-offs.
- (3)

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Losses are charged against the allowance for loan losses in the case of a write-down upon the transfer of a loan to REO. Losses subsequent to the transfer of a loan to REO are charged to provision for losses on REO.

### Fair Values of Financial Instruments

The carrying amounts and estimated fair values of financial instruments, at March 31, 2012 and December 31, 2011 were as follows:

|                                     | Carrying Value | Fair Value Measurements at March 31, 2012 Using |                           |         |              |
|-------------------------------------|----------------|---|---------------------------|---------|--------------|
|                                     |                | Level 1   | Level 2<br>(In thousands) | Level 3 | Total        |
| <b>Financial Assets:</b>            |                |   |                           |         |              |
| Cash and cash equivalents           | \$ 45,177      | \$ 45,177                                       | \$                        | \$      | \$ 45,177    |
| Securities available-for-sale       | 18,027         |   | 18,027                    |         | 18,027       |
| Loans receivable held for sale, net | 12,908         |   |                           | 12,908  | 12,908       |
| Loans receivable, net               | 309,578        |   |                           | 309,693 | 309,693      |
| Federal Home Loan Bank stock        | 3,901          |   |                           | N/A     | N/A          |
| Accrued interest receivable         | 1,601          |   | 70                        | 1,531   | 1,601        |
| <b>Financial Liabilities:</b>       |                |   |                           |         |              |
| Deposits                            | \$ (290,352)   | \$  | \$ (289,516)              | \$      | \$ (289,516) |
| Federal Home Loan Bank advances     | (83,000)       |   | (88,529)                  |         | (88,529)     |
| Junior subordinated debentures      | (6,000)        |   |                           | (5,391) | (5,391)      |
| Other borrowings                    | (5,000)        |   |                           | (4,493) | (4,493)      |
| Accrued interest payable            | (1,502)        |   | (206)                     | (1,296) | (1,502)      |

**Table of Contents****BROADWAY FINANCIAL CORPORATION AND SUBSIDIARIES****Notes to Unaudited Consolidated Financial Statements (continued)****March 31, 2012**

|   | <b>December 31, 2011</b>   |                                 |
|---|----------------------------|---------------------------------|
|   | <b>Carrying<br/>Amount</b> | <b>Estimated<br/>Fair Value</b> |
| <b>Financial Assets:</b>                              |                            |                                 |
| Cash and cash equivalents                             | \$ 31,597                  | \$ 31,597                       |
| Securities available-for-sale                         | 18,979                     | 18,979                          |
| Loans receivable held for sale, net                   | 12,983                     | 12,983                          |
| Loans receivable, net                                 | 322,770                    | 323,090                         |
| Federal Home Loan Bank stock                          | 4,089                      | N/A                             |
| Accrued interest receivable                           | 1,698                      | 1,698                           |
| <b>Financial Liabilities:</b>                         |                            |                                 |
| Deposits  | \$ (294,686)               | \$ (294,313)                    |
| Federal Home Loan Bank advances                       | (83,000)                   | (88,911)                        |
| Junior subordinated debentures                        | (6,000)                    | (5,319)                         |
| Other borrowings                                      | (5,000)                    | (4,434)                         |
| Advance payments by borrowers for taxes and insurance | (813)                      | (813)                           |
| Accrued interest payable                              | (1,302)                    | (1,302)                         |

The methods and assumptions, not previously presented, used to estimate fair values are described as follows:

*(a) Cash and Cash Equivalents*

The carrying amounts of cash and cash equivalents approximate fair values and are classified as Level 1.

*(b) Loans receivable held for sale*

The fair value of loans held for sale is estimated based on quoted prices from third party sale analyses, existing sale agreements or appraisal reports adjusted by sales commission assumptions resulting in a Level 3 classification.

*(c) Loans receivable*

Fair values of loans, excluding loans held for sale, are estimated as follows: For variable rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying values resulting in a Level 3 classification. Fair values for other loans are estimated using discounted cash flow analyses, using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality resulting in a Level 3 classification. Impaired loans are valued at the lower of cost or fair value as described previously. The methods utilized to estimate the fair value of loans do not necessarily represent an exit price.

*(d) FHLB Stock*

It is not practical to determine the fair value of FHLB stock due to restrictions placed on its transferability.

*(e) Deposits*

The fair values disclosed for demand deposits (e.g., interest and non-interest checking, passbook savings, and certain types of money market accounts) are, by definition, equal to the amount payable on demand at the reporting date (i.e., their carrying amount) resulting in Level 2 classification. Fair values for fixed rate certificates of deposit are estimated using discounted cash flow calculations that apply interest rates currently being offered on certificates to a schedule of aggregated expected monthly maturities on time deposits resulting in a Level 2 classification.





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**BROADWAY FINANCIAL CORPORATION AND SUBSIDIARIES**

**Notes to Unaudited Consolidated Financial Statements (continued)**

**March 31, 2012**

*(f) Federal Home Loan Bank Advances*

The fair values of the Federal Home Loan Bank advances are estimated using discounted cash flow analyses based on the current borrowing rates for similar types of borrowing arrangements resulting in a Level 2 classification.

*(g) Subordinated Debentures and Other Borrowings*

The fair values of the Company's Subordinated Debentures and other borrowings are estimated using discounted cash flow analyses based on the current borrowing rates for similar types of borrowing arrangements resulting in a Level 3 classification.

*(h) Accrued Interest Receivable/Payable*

The carrying amounts of accrued interest are classified the same as the related asset / liability.

**NOTE (9) Stock-based Compensation**

In 2008, we adopted the 2008 Long-Term Incentive Plan ( 2008 LTIP ), which is shareholder approved. The 2008 LTIP replaced the Company's 1996 Long-Term Incentive Plan ( 1996 LTIP ) and 1996 Stock Option Plan ( Stock Option Plan ), which have expired and are no longer effective except as to outstanding awards. The 2008 LTIP permits the grant of non-qualified and incentive stock options, stock appreciation rights, full value awards and cash incentive awards to the Company's non-employee directors and certain officers and employees for up to 351,718 shares of common stock. Option awards are generally granted with an exercise price equal to the market price of the Company's common stock at the date of grant; those option awards have vesting periods ranging from immediate vesting to 5 years and have 10-year contractual terms. The Company has a policy of using shares held as treasury stock to satisfy share option exercises. Currently, the Company has a sufficient number of treasury shares to satisfy expected share option exercises.

There were no options granted during the three months ended March 31, 2012 and 2011. The Company recorded \$20 thousand of stock-based compensation expense, net of tax, during the first quarter of 2012 compared to \$23 thousand for the first quarter of 2011.

**NOTE (10) Regulatory Matters**

The Bank is subject to regulatory capital requirements now administered by the Office of the Comptroller of the Currency, or OCC, which is the statutory successor under the Dodd-Frank Act to the former Office of Thrift Supervision, or OTS. The capital requirements, which remain the same as when administered by the OTS, involve quantitative measures of assets, liabilities, and certain off balance sheet items calculated under regulatory accounting practices. Capital amounts and classifications are also subject to qualitative judgments by the OCC. Failure to meet capital requirements can result in regulatory action.

Prompt corrective action regulations also administered by the OCC provide five classifications: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized, although these terms are not used to represent overall financial condition. If only adequately capitalized, regulatory approval is required to accept brokered deposits. If undercapitalized, capital distributions are limited, as is asset growth and expansion, and capital restoration plans are required.

The Company and the Bank consented to the issuance to them of cease and desist orders by the OTS effective September 9, 2010 requiring, among other things, that the Company and the Bank take remedial actions to improve the Bank's loan underwriting and internal asset review procedures, to reduce the amount of its non-performing assets and to



**Table of Contents****BROADWAY FINANCIAL CORPORATION AND SUBSIDIARIES****Notes to Unaudited Consolidated Financial Statements (continued)****March 31, 2012**

improve other aspects of the Bank's business, as well as the Company's management of its business and the oversight of the Company's business by the Board. The cease and desist orders, which are now administered by the OCC with respect to the Bank and the FRB with respect to the Company, require the Bank to attain, and thereafter maintain, a Tier 1 (Core) Capital to Adjusted Total Assets ratio of at least 8% and a Total Risk-Based Capital to Risk-Weighted Assets ratio of at least 12%, both of which ratios are greater than the respective 5% and 10% levels for such ratios that are generally required under OTS (now OCC) regulations. The cease and desist orders also prohibit the Bank from paying dividends to the Company, and prohibit the Company from paying dividends to its shareholders, without the prior written approval of the OCC and the FRB, respectively. In addition, the Company is not permitted to incur, issue, renew, repurchase, make payments on or increase any debt or redeem any capital stock without prior notice to and receipt of written notice of non-objection from the FRB.

The Bank did not meet the minimum capital requirements under the cease and desist order at March 31, 2012 or December 31, 2011.

Actual and normally required capital amounts and ratios at March 31, 2012 and December 31, 2011, together with the higher capital requirements that the Bank is required to meet under the cease and desist order applicable to it, are presented below.

|   | Actual    |        | Required for<br>Capital Adequacy<br>Purposes |       | To Be Well<br>Capitalized Under<br>Prompt Corrective<br>Action Regulations |        | Capital<br>Requirements<br>under Cease and<br>Desist Order |        |
|---|-----------|--------|--|-------|--|--------|--|--------|
|   | Amount    | Ratio  | Amount                                       | Ratio | Amount   | Ratios | Amount   | Ratios |
| <b>March 31, 2012:</b>                        |           |        |  |       |  |        |  |        |
| Tangible Capital to adjusted total assets     | \$ 31,442 | 7.70%  | \$ 6,124                                     | 1.50% | N/A  | N/A    | N/A  | N/A    |
| Tier 1(Core) Capital to adjusted total assets | \$ 31,442 | 7.70%  | \$ 16,331                                    | 4.00% | \$ 20,414  | 5.00%  | \$ 32,662  | 8.00%  |
| Tier 1(Core) Capital to risk weighted assets  | \$ 31,442 | 10.92% | N/A  | N/A   | \$ 17,276  | 6.00%  | N/A  | N/A    |
| Total Capital to risk weighted assets         | \$ 35,216 | 12.23% | \$ 23,035                                    | 8.00% | \$ 28,794  | 10.00% | \$ 34,552  | 12.00% |
| <b>December 31, 2011 :</b>                    |           |        |  |       |  |        |  |        |
| Tangible Capital to adjusted total assets     | \$ 30,961 | 7.27%  | \$ 6,396                                     | 1.50% | N/A  | N/A    | N/A  | N/A    |
| Tier 1(Core) Capital to adjusted total assets | \$ 30,961 | 7.27%  | \$ 17,055                                    | 4.00% | \$ 21,319  | 5.00%  | \$ 34,111  | 8.00%  |
| Tier 1(Core) Capital to risk weighted assets  | \$ 30,961 | 10.31% | N/A  | N/A   | \$ 18,019  | 6.00%  | N/A  | N/A    |
| Total Capital to risk weighted assets         | \$ 34,882 | 11.61% | \$ 24,026                                    | 8.00% | \$ 30,032  | 10.00% | \$ 36,039  | 12.00% |

**NOTE (11) Income Taxes**

The Company and its subsidiaries are subject to U.S. federal and state income taxes. Income tax expense is the total of the current year income tax due or refundable and the change in deferred tax assets and liabilities. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carry-forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is not more likely than not that some portion, or all, of the deferred tax asset will be realized. In assessing the realization of deferred tax assets, management evaluates both positive and negative evidence, including the existence of any cumulative losses in the current year and the prior two years, the amount of taxes paid in available carry-back years, the forecasts of future



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**BROADWAY FINANCIAL CORPORATION AND SUBSIDIARIES**

**Notes to Unaudited Consolidated Financial Statements (continued)**

**March 31, 2012**

income and tax planning strategies. This analysis is updated quarterly. Based on this analysis, the Company determined that a valuation allowance of \$8.3 million was required as of March 31, 2012. The Company had recorded a valuation allowance of \$8.2 million as of December 31, 2011. The remaining net deferred tax asset of \$772 thousand at March 31, 2012 is supported by a near term tax planning strategy of selling the Bank's headquarters building at a gain. The sale closed in the second quarter of 2012.

**NOTE (12) Going Concern**

The Company's financial statements have been prepared assuming that the Company will continue as a going-concern, which contemplates continuity of operations, realization of assets and liquidation of liabilities in the ordinary course of business. However, the Company has a tax sharing liability to the Bank which exceeds operating cash at the Company level. The Company used its cash available at the holding company level to pay a substantial portion of this liability pursuant to the terms of the Tax Allocation Agreement between the Bank and the Company on March 30, 2012 and does not have cash available to pay its operating expenses. Additionally, the Company is in default under the terms of a \$5.0 million line of credit with another financial institution lender (see Note 7).

Due to the current regulatory order that is in effect, the Bank is not allowed to make distributions to the Company without regulatory approval, and such approval is not likely to be given. In that event, the Company would not be able to meet its payment obligations within the foreseeable future unless the Company is able to secure new capital and/or obtain requisite forbearances from its lender. These conditions raise substantial doubt about the Company's ability to continue as a going concern.

Management's plan to address the conditions described above is to raise additional equity capital for the Company and exchange senior securities for common equity (see Note 7). The Company's ability to continue as a going concern is dependent on the timely implementation and success of this plan. There can be no assurance that management's plan will be achieved.

**Table of Contents****ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

Management's Discussion and Analysis of Financial Condition and Results of Operations ( MD&A ) is intended to provide a reader of our financial statements with a narrative from the perspective of our management on our financial condition, results of operations, liquidity and certain other factors that may affect our future results. Our MD&A should be read in conjunction with the Consolidated Financial Statements and related Notes included in Part I Item 1, Financial Statements, of this Quarterly Report on Form 10-Q and our amended Annual Report on Form 10-K/A for the year ended December 31, 2011.

**Overview**

Total assets decreased during the first quarter of 2012 primarily due to a decrease in our loan portfolio, as loan repayments, foreclosures and charge-offs exceeded loan originations during the period. The decrease in our loan portfolio primarily consisted of a \$4.5 million decrease in our five or more units residential real estate loan portfolio, a \$4.8 million decrease in our commercial real estate loan portfolio, a \$1.7 million decrease in our church loan portfolio, a \$514 thousand decrease in our one-to-four family residential real estate loan portfolio, and a \$809 thousand decrease in our consumer loan portfolio.

Total deposits decreased during the first quarter of 2012, while FHLB borrowings, subordinated debentures and other borrowings remained unchanged.

Our net earnings for the first quarter 2012 were \$154 thousand, compared to a net loss of \$129 thousand for the same period a year ago. The increase from a net loss to net earnings was primarily due to lower provision for loan losses, higher net gains on sales of real estate owned ( REO ), lower compensation and benefits expense, and lower provision for losses on loans held for sale and REO, which were partially offset by lower net interest income.

**Results of Operations***Net Interest Income*

For the first quarter of 2012, our net interest income before provision for loan losses was \$3.7 million, which represented a decrease of \$660 thousand, or 15%, from the first quarter of 2011. The \$660 thousand decrease in net interest income primarily resulted from a \$78.1 million decrease in average interest-earning assets.

Average interest-earning assets for the first quarter of 2012 decreased \$78.1 million to \$401.7 million from \$479.8 million for the first quarter of 2011, which resulted in a \$1.3 million reduction in interest income. The decline in average interest-earning assets, primarily loans receivable, reflects our strategy throughout 2011 to maintain our capital ratios above the required regulatory thresholds, in part by shrinking total assets. The annualized yield on our average interest-earning assets decreased 1 basis point to 5.47% for the first quarter of 2012, from 5.48% for the same period a year ago.

Average interest-bearing liabilities for the first quarter of 2012 decreased \$58.0 million to \$386.1 million from \$444.1 million for the first quarter of 2011. The decrease in average interest-bearing liabilities resulted in a \$226 thousand reduction in interest expense. The annualized cost of our average interest-bearing liabilities decreased 14 basis points to 1.87% for the first quarter of 2012 from 2.01% for the same period a year ago, and resulted in a decrease of \$194 thousand in interest expense.

*Provision and Allowance for Loan Losses*

We record a provision for loan losses as a charge to earnings when necessary in order to maintain the allowance for loan losses at a level sufficient, in management's judgment, to absorb losses inherent in the loan portfolio. At least quarterly, we conduct an assessment of the overall quality of the loan portfolio and general economic trends in the local market. The determination of the appropriate level for the allowance is based on that review, considering such factors as historical loss experience for each type of loan, the size and composition of our loan portfolio, the levels and composition of our loan delinquencies, non-performing loans and net loan charge-offs, the value of underlying collateral on problem loans, regulatory policies, general economic conditions, and other factors related to the collectability of loans in the portfolio.

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The provision for loan losses for the first quarter of 2012 totaled \$959 thousand compared to \$1.2 million for the same period a year ago. The decrease in the provision for loan losses for the first quarter of 2012 was due primarily to the decrease in the size of our loan portfolio from \$393.9 million a year ago to \$327.1 million at March 31, 2012. The first quarter provision was also impacted by specific loss allocations on loans that became impaired during the quarter, charge-offs that were not reserved for at year-end 2011 and higher reserves on our church loan portfolio.

At March 31, 2012 our allowance for loan losses was \$17.8 million, or 5.42% of our gross loans receivable, compared to \$17.3 million, or 5.09% of our gross loans, at year-end 2011. The ratio of the allowance for loan losses to NPLs, excluding loans held for sale, decreased to 42.39% at March 31, 2012, compared to 44.20% at year-end 2011. Despite the decrease in the allowance ratio, management believes that the remaining loss potential has been reduced as certain losses inherent in our NPLs have been recognized as charge-offs which resulted in a lower ratio of the allowance for loan losses to NPLs. As of March 31, 2012, 65% of our NPLs had been written down to their adjusted fair value less estimated selling costs, by establishing specific reserves or charged-off as necessary.

Loan charge-offs during the first quarter of 2012 were \$644 thousand, or 0.74% of average loans, compared to \$709 thousand, or 0.66% of average loans, during the first quarter of 2011. The \$644 thousand of charge-offs were not reserved for at year-end 2011 and were primarily related to loans that became impaired during the first quarter of 2012 and with respect to which recent valuations of the underlying collateral reflected impairment losses. Charge-offs in one-to-four family residential real estate loans totaled \$355 thousand and represented 55% of charge-offs during 2012. Charge-offs in church loans totaled \$231 thousand and represented 36% of charge-offs during 2012. Charge-offs in commercial real estate loans totaled \$58 thousand and represented 9% of charge-offs during 2012.

Impaired loans at March 31, 2012 were \$59.0 million compared to \$56.3 million at December 31, 2011. Specific reserves for impaired loans were \$3.9 million, or 6.64% of the aggregate impaired loan amount at March 31, 2012, compared to \$3.9 million, or 7.00%, at December 31, 2011. Excluding specific reserves for impaired loans, our coverage ratio (general allowance as a percentage of total non-impaired loans) was 5.16% at March 31, 2012, compared to 4.71% at December 31, 2011.

We performed an impairment analysis for all non-performing and restructured loans, and established specific loss allocations for impaired loans of \$3.9 million at March 31, 2012. Of the \$3.9 million specific loss allocations at March 31, 2012, \$1.2 million were related to \$3.8 million of loans that are non-performing and with respect to which the recent valuation of the underlying collateral reflected a decrease in values. Additionally, we recorded \$2.7 million of specific loss allocations for impairment related to \$16.6 million of accruing loans that were modified in troubled debt restructurings. On \$18.6 million of impaired loans, the fair value of collateral less estimated selling costs exceeded the recorded investment in the loan and did not require a specific loss allocation. The remaining \$20.0 million of impaired loans had been written down to fair value after charge-offs of \$13.0 million.

Management believes that the allowance for loan losses is adequate to cover probable incurred losses in the loan portfolio as of March 31, 2012, but there can be no assurance that actual losses will not exceed the estimated amounts. In addition, the OCC and the FDIC periodically review the allowance for loan losses as an integral part of their examination process. These agencies may require an increase in the allowance for loan losses based on their judgments of the information available to them at the time of their examinations. The provisions for loan losses and corresponding allowance for loan losses in these financial statements contained in Part 1, Item 1 of this Form 10-Q reflect judgments by the OCC made during its supervisory examination of our Bank completed in July 2012.

**Table of Contents***Non-interest Income*

Non-interest income for the first quarter of 2012 totaled \$423 thousand compared to \$181 thousand for the first quarter of 2011. The \$242 thousand increase from the first quarter of 2011 was primarily due to higher net gains on sales of REOs, which was partially offset by higher net losses on mortgage banking activities and lower service charges for loan-related fees and retail banking fees.

*Non-interest Expense*

Non-interest expense for the first quarter of 2012 totaled \$2.9 million, compared to \$3.5 million for the first quarter of 2011. Lower non-interest expense in the first quarter of 2012 was primarily due to lower provisions for losses on loans held for sale and REO, and lower compensation and benefits expense, occupancy expense and office services and supplies expense, primarily resulting from two branch closures at the end of 2011.

*Income Taxes*

The Company's effective income tax rate was 32.75% for the three months ended March 31, 2012 compared to 40.00% for the three months ended March 31, 2011. Income taxes for interim periods are computed by applying the projected annual effective income tax rate for the year to the year-to-date earnings plus discrete items (items incurred in the quarter). The projected annual effective tax rate incorporates certain non-taxable federal and state income items, federal and state tax credits, and expected increases to the valuation allowance for projected deferred tax assets.

**Financial Condition***Total Assets*

Total assets were \$408.9 million at March 31, 2012, which represented a decrease of \$4.9 million, or 1%, from December 31, 2011. During the first quarter of 2012, net loans decreased by \$13.2 million, loans held for sale decreased by \$75 thousand, securities decreased by \$952 thousand, REO decreased by \$2.7 million, deferred tax assets decreased by \$78 thousand and other assets (primarily income tax receivable) decreased by \$1.0 million, while cash and cash equivalents increased by \$13.6 million.

*Loan Portfolio*

Our gross loan portfolio decreased by \$12.7 million to \$327.1 million at March 31, 2012 from \$339.8 million at December 31, 2011, as loan repayments, foreclosures and charge-offs exceeded loan originations during the first quarter of 2012. The decrease in our loan portfolio primarily consisted of a \$4.5 million decrease in our five or more units residential real estate loan portfolio, a \$4.8 million decrease in our commercial real estate loan portfolio, a \$1.7 million decrease in our church loan portfolio, a \$514 thousand decrease in our one-to-four family residential real estate loan portfolio and a \$809 thousand decrease in our consumer loan portfolio.

Loan originations for the three months ended March 31, 2012 totaled \$3.4 million compared to \$1.6 million for the three months ended March 31, 2011. Loan repayments for the three months ended March 31, 2012 totaled \$14.6 million compared to \$6.5 million for the comparable period in 2011. Loans transferred to REO during the first quarter of 2012 totaled \$790 thousand, compared to \$1.9 million during the first quarter of 2011.

*Deposits*

Deposits totaled \$290.4 million at March 31, 2012, down \$4.3 million, or 1%, from year-end 2011. During the first quarter of 2012, core deposits (NOW, demand, money market and passbook accounts) decreased by \$2.2 million and represented 33% of total deposits at March 31, 2012 and December 31, 2011. Our certificates of deposit (CDs) decreased by \$2.1 million during the first quarter of 2012 and represented 67% of total deposits at March 31, 2012 and December 31, 2011. Brokered deposits represented 3% of total deposits at March 31, 2012 and December 31, 2011.



**Table of Contents***Borrowings*

Since year-end 2011, FHLB borrowings, subordinated debentures and other borrowings remained unchanged at \$83.0 million, \$6.0 million, and \$5.0 million, respectively. At March 31, 2012 and December 31, 2011, FHLB advances were 20% of total assets and the weighted average cost of advances at those dates was 3.09%. See Liquidity for further information on subordinated debentures and other borrowings.

*Non-Performing Assets*

Non-performing assets ( NPAs ) include non-accrual loans and real estate owned through foreclosure or deed in lieu of foreclosure ( REO ). NPAs at March 31, 2012 were \$51.4 million, or 12.57% of total assets, compared to \$51.4 million, or 12.43% of total assets, at December 31, 2011. At March 31, 2012, non-accrual loans were \$47.4 million compared to \$44.7 million at December 31, 2011. These loans consist of delinquent loans that are 90 days or more past due and troubled debt restructurings ( TDRs ) that do not qualify for accrual status.

The non-accrual loans at March 31, 2012 included 35 church loans totaling \$26.1 million, 22 one-to-four family residential real estate loans totaling \$8.8 million, 14 commercial real estate loans totaling \$6.2 million, 10 five or more units residential real estate loans totaling \$5.9 million, a land loan for \$296 thousand, and a consumer loan for \$70 thousand.

During the first quarter of 2012, REO decreased by \$2.7 million to \$4.0 million at March 31, 2012, from \$6.7 million at the end of 2011. At March 31, 2012 the Bank's REO consisted of three one-to-four family residential properties and eight commercial real estate properties, six of which are church buildings. As part of our efforts to reduce non-performing assets, we sold five REO properties for total proceeds of \$4.0 million, and recorded a corresponding net gain of \$412 thousand, during the first quarter of 2012.

*Performance Ratios*

The annualized return on average equity for the three months ended March 31, 2012 was 3.34%, compared to an annualized loss on average equity of (1.55%) for the three months ended March 31, 2011. The annualized return on average assets for the three months ended March 31, 2012 was 0.15%, compared to an annualized loss on average assets of (0.11%) for the three months ended March 31, 2011. The efficiency ratios for the three months ended March 31, 2012 was 71.60%, compared to 75.15% for the three months ended March 31, 2011. The improvement in these ratios was primarily due to the profit for the three months ended March 31, 2012 as a result of lower provision for loan losses, higher net gains on sales of REO, lower compensation and benefits expense and lower provision for losses on loans held sale and REO, which were partially offset by lower net interest income.

**Liquidity**

The objective of liquidity management is to ensure that we have the continuing ability to fund operations and meet other obligations on a timely and cost-effective basis. The Bank's sources of funds include deposits, advances from the FHLB and other borrowings, proceeds from the sale of loans, mortgage-backed and investment securities, and principal and interest payments from loans and mortgage-backed and other investment securities. Primary uses of funds include withdrawal of and interest payments on deposits, originations of loans, purchases of mortgage-backed and other investment securities, and payment of operating expenses.

Net cash inflows from operating activities totaled \$1.8 million and \$345 thousand during the first quarter of 2012 and 2011, respectively. Net cash inflows from operating activities for the first quarter of 2012 were primarily attributable to interest payments received on loans and securities.

Net cash inflows from investing activities totaled \$16.6 million and \$12.8 million during the first quarter of 2012 and 2011, respectively. Net cash inflows from investing activities for the first quarter of 2012 were attributable primarily to principal repayments on loans and securities and proceeds from sales of REOs.

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Net cash outflows from financing activities totaled \$4.8 million and \$7.5 million during the first quarter of 2012 and 2011, respectively. Net cash outflows from financing activities for the first quarter of 2012 were attributable primarily to the net decrease in deposits.

When the Bank has more funds than required for reserve requirements or short-term liquidity needs, the Bank sells federal funds to other financial institutions. Conversely, when the Bank has fewer funds than required, the Bank may borrow funds from the FHLB. The Bank is currently approved by the FHLB to borrow up to \$100.0 million to the extent the Bank provides qualifying collateral and hold sufficient FHLB stock. That approved limit and collateral requirement would have permitted the Bank, as of March 31, 2012, to borrow an additional \$7.9 million.

At times we maintain a portion of our liquid assets in interest-bearing cash deposits with other banks, in overnight federal funds sold to other banks, and in securities available-for-sale that are not pledged. The Bank's liquid assets at March 31, 2012 consisted of \$45.2 million in cash and cash equivalents and \$15.5 million in securities available-for-sale that are not pledged, compared to \$31.6 million in cash and cash equivalents and \$17.4 million in securities available-for-sale that are not pledged at December 31, 2011.

The Company has a tax sharing liability to the Bank which exceeds operating cash at the Company level. The liability was partially settled pursuant to the terms of the Tax Allocation Agreement between the Bank and the Company on March 30, 2012, which settlement consumed the Company's operating cash. Our ability to service our debt obligations and pay dividends and holding company expenses is dependent primarily on the recapitalization plan discussed in Capital Resources. Holding company debt obligations, which are included in other borrowings, are described below.

On March 17, 2004, the Company issued \$6.0 million of Floating Rate Junior Subordinated Debentures in a private placement. The debentures mature in 10 years and interest is payable quarterly at a rate per annum equal to the 3-month LIBOR plus 2.54%. The interest rate is determined as of each March 17, June 17, September 17, and December 17, and was 3.10% at December 31, 2011. The Company stopped paying interest on the debentures and the senior line of credit discussed below in September 2010. As disclosed previously, the Company is not permitted to make payments on any debts without prior notice to and receipt of written notice of non-objection from the FRB. In addition, under the terms of the subordinated debentures, the Company is not allowed to make payments on the subordinated debentures if the Company is in default on any of its senior indebtedness, which term includes the senior line of credit described below.

On February 28, 2010, the Company borrowed an aggregate of \$5.0 million under its \$5.0 million line of credit with another financial institution, and invested all of the proceeds in the equity capital of the Bank. Borrowings under this line of credit are secured by the Company's assets. The interest rate on the line of credit adjusts annually, subject to a minimum of 6.00%, and increases by an additional 5% in the event of default. The full amount of this borrowing became due and payable on July 31, 2010. The Company does not have sufficient cash available to repay the borrowing at this time and would require approval of the FRB to make any payment on this senior line of credit or to obtain a dividend from the Bank for such purpose. This senior line of credit has not been repaid and the Company is now in default under the line of credit agreement. On April 7, 2011, the lender agreed to forbear from exercising its rights (other than increasing the interest rate by the default rate margin) pursuant to the line of credit agreement until January 1, 2012 subject to certain conditions. The lender has informed the Company that it does not intend to extend the forbearance agreement.

Due to the current regulatory order that is in effect, the Bank is not allowed to make distributions to the Company without regulatory approval, and such approval is not likely to be given. Accordingly, the Company will not be able to meet its payment obligations within the foreseeable future unless the Company is able to secure new capital.

These conditions and the Company's operating losses raise substantial doubt about the Company's ability to continue as a going concern. These and related matters are discussed in Note 12 "Going Concern" of the Notes to Consolidated Financial Statements.

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### **Capital Resources**

On November 14, 2008, the Company issued 9,000 shares of the Company's Fixed Rate Cumulative Perpetual Preferred Stock, Series D, having a liquidation preference of \$1,000 per share, together with a ten-year warrant to purchase 183,175 shares of Company common stock at \$7.37 per share, to the U.S. Treasury Department for gross proceeds of \$9.0 million. The sale of the Series D Preferred Stock was made pursuant to the U.S. Treasury Department's TARP Capital Purchase Program.

On December 8, 2009, the Company issued 6,000 shares of the Company's Fixed Rate Cumulative Perpetual Preferred Stock, Series E, having a liquidation preference of \$1,000 per share, to the U.S. Treasury Department for gross proceeds of \$6.0 million. The sale of the Series E Preferred Stock was made pursuant to the U.S. Treasury Department's TARP Capital Purchase Program.

We are pursuing our comprehensive recapitalization plan to improve the Company's capital structure. To date, we have entered into written agreements with:

The U.S. Treasury Department pursuant to which the U.S. Treasury will exchange the shares of our Series D and E Fixed Rate Cumulative Perpetual Preferred Stock held by it for our common stock at a discount of 50% of the liquidation amount, plus an undiscounted exchange of the accumulated but unpaid dividends on such preferred stock for common stock, subject to various conditions, including the exchange of the Company's other outstanding series of preferred stock at discounts of 50% of the aggregate liquidation values, the placement of at least \$5 million of new common equity capital, and other conditions; and

The holder of our Series A Perpetual Preferred Stock to exchange its holdings for common stock at a discount of 50% of the liquidation amount, subject to various conditions, including the exchange of the Company's other outstanding series of preferred stock, the placement of new common equity capital, and other conditions.

We are also in negotiations with the holders of our Series B Perpetual Preferred Stock and Series C Noncumulative Perpetual Convertible Preferred Stock regarding exchange of their holdings for common stock on a similar basis as the exchange of the Series A Perpetual Preferred Stock, and we are in discussions with our senior bank lender regarding the exchange of a portion of the \$5 million outstanding amount borrowed under our line of credit, which is currently in default, for common stock at 100% of the face amount to be exchanged; the forgiveness of the accrued interest on the entire amount of the line of credit to the date of the exchange; and the execution of a modified credit agreement for the remainder of the facility that would be outstanding after the exchange.

The conditions to each of the above proposed exchanges include, or are expected to include, requirements that the holders of each series of our outstanding preferred stock concurrently exchange their preferred stock for our common stock on similar terms and that we concurrently complete private placements or other sales of new shares of common stock, as discussed above. Based on the agreements that we have executed, we anticipate that these exchanges and placements and sales of common stock would, if completed, result in the issuance of approximately 17.1 million new shares of the Company's common stock, which would constitute approximately 91% of the pro forma outstanding shares of the Company's common stock. The 17.1 million new shares of common stock exceed the Company's current unissued and authorized shares. We plan to seek shareholder approval to increase the Company's authorized shares, and issue a portion of such shares in the recapitalization.

In addition, we are negotiating to sell our Bank's headquarters building and work to decrease NPAs through proactive management and loan sales as part of our efforts to raise capital and increase earnings.

There can be no assurance our recapitalization plan will be achieved on the currently contemplated terms, or at all. If we are unable to raise capital, we plan to continue to shrink assets and implement other strategies to increase earnings. Failure to maintain capital sufficient to meet the higher capital requirements could result in further regulatory action, which could include the appointment of a conservator or receiver for the Bank. The Company or its creditors could also initiate bankruptcy proceedings.

**Table of Contents****Regulatory Capital**

The capital regulations applicable to the Bank, which are now administered by the OCC, include three separate minimum capital requirements. First, the tangible capital requirement mandates that the Bank's shareholder's equity, less intangible assets, be at least 1.50% of adjusted total assets as defined in the capital regulations. Second, the core capital requirement currently mandates that core capital (tangible capital plus certain qualifying intangible assets) be at least 4.00% of adjusted total assets as defined in the capital regulations. Third, the risk-based capital requirement presently mandates that core capital plus supplemental capital (as defined by the OCC) be at least 8.00% of risk-weighted assets as prescribed in the capital regulations. The capital regulations assign specific risk weightings to all assets and off-balance-sheet items for this purpose.

The Bank was in compliance with all capital requirements in effect at March 31, 2012, and met the generally applicable capital ratio standards necessary to be considered well-capitalized under the prompt corrective action regulations adopted pursuant to the Federal Deposit Insurance Corporation Improvement Act of 1991. However, in March 2010, the Company and the Bank were determined to be in troubled condition by the OTS and they consented to them of cease and desist orders by the OTS effective September 9, 2010, which orders remain in effect and are now administered by the OCC. The cease and desist orders require the Bank to achieve and maintain higher levels of regulatory capital than normally required. Under the applicable regulations, the Bank is therefore precluded from being considered to be more than adequately capitalized until such special capital requirements are terminated and the Company and the Bank are no longer considered to be in troubled condition.

The Bank did not meet the minimum capital requirements under the cease and desist order at March 31, 2012 and December 31, 2011. Actual and normally required capital amounts and ratios at March 31, 2012 and December 31, 2011, together with the higher capital requirements that the Bank is required to meet under the cease and desist order applicable to it, are presented below.

|   | Actual    |        | Required for<br>Capital Adequacy<br>Purposes |       | To Be Well<br>Capitalized Under<br>Prompt Corrective<br>Action Regulations |        | Capital<br>Requirements<br>under Cease and<br>Desist Order |        |
|---|-----------|--------|--|-------|--|--------|--|--------|
|   | Amount    | Ratio  | Amount                                       | Ratio | Amount   | Ratios | Amount   | Ratios |
| <b>March 31, 2012:</b>                        |           |        |  |       |  |        |  |        |
| Tangible Capital to adjusted total assets     | \$ 31,442 | 7.70%  | \$ 6,124                                     | 1.50% | N/A  | N/A    | N/A  | N/A    |
| Tier 1(Core) Capital to adjusted total assets | \$ 31,442 | 7.70%  | \$ 16,331                                    | 4.00% | \$ 20,414  | 5.00%  | \$ 32,662  | 8.00%  |
| Tier 1(Core) Capital to risk weighted assets  | \$ 31,442 | 10.92% | N/A  | N/A   | \$ 17,276  | 6.00%  | N/A  | N/A    |
| Total Capital to risk weighted assets         | \$ 35,216 | 12.23% | \$ 23,035                                    | 8.00% | \$ 28,794  | 10.00% | \$ 34,552  | 12.00% |
| <b>December 31, 2011 :</b>                    |           |        |  |       |  |        |  |        |
| Tangible Capital to adjusted total assets     | \$ 30,961 | 7.27%  | \$ 6,396                                     | 1.50% | N/A  | N/A    | N/A  | N/A    |
| Tier 1(Core) Capital to adjusted total assets | \$ 30,961 | 7.27%  | \$ 17,055                                    | 4.00% | \$ 21,319  | 5.00%  | \$ 34,111  | 8.00%  |
| Tier 1(Core) Capital to risk weighted assets  | \$ 30,961 | 10.31% | N/A  | N/A   | \$ 18,019  | 6.00%  | N/A  | N/A    |
| Total Capital to risk weighted assets         | \$ 34,882 | 11.61% | \$ 24,026                                    | 8.00% | \$ 30,032  | 10.00% | \$ 36,039  | 12.00% |

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**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

Not Applicable

**ITEM 4. CONTROLS AND PROCEDURES**

**Evaluation of Disclosure Controls and Procedures**

An evaluation of the effectiveness of the design and operation of the Company's disclosure controls and procedures was performed under the supervision of the Company's Chief Executive Officer ( CEO ) and Chief Financial Officer ( CFO ) as of March 31, 2012. Based on that evaluation and due to the material weaknesses identified below, the Company's CEO and CFO concluded that the Company's disclosure controls and procedures were not effective as of March 31, 2012.

The Company's external auditors identified certain material misstatements in the course of their audit of our consolidated financial statements for the year ended December 31, 2011 and appropriate adjustments to the consolidated financial statements, resulting in an additional net loss of \$677 thousand, were made prior to their issuance. The adjustments included corrections of errors in the determination of specific allowances for impaired loans, errors in the calculation of the amortization of our investment in low-income housing projects and errors in the calculation of our income tax provision and the determination of the valuation allowance on our deferred tax assets.

Subsequent to the issuance of our 2011 consolidated financial statements and the filing of our Annual Report on Form 10-K on March 30, 2012, management became aware of certain additional errors in the preparation of our 2011 consolidated financial statements. The errors included failure in connection with preparation of our financial statements to obtain and take into account certain appraisals of the values of properties securing impaired loans that had been ordered and received by the Bank prior to the issuance date of our financial statements and failure to follow appropriate methods for calculating expected future payments on loans in connection with our discounted cash flow analysis for measuring impairment of loans deemed to be troubled debt restructurings. In addition, certain appraisals received after year-end 2011 indicated that impairment losses that had been determined using values based on broker provided opinions of value ( BPOs ) understated the losses inherent in those loans. We have determined that these additional errors also constituted material weaknesses in our system of internal controls over financial reporting.

Management, with the oversight of the Audit Committee, has taken and intends to take actions to address the material weaknesses discovered in our internal control over financial reporting. These include implementation of changes in our accounting policies and procedures to assure that appropriate methods are used in determining the values of collateral dependent loans and that all appraisals that have been ordered by the Bank to determine the values of properties securing our loans and REO are obtained and appropriately considered by accounting personnel in connection with preparation of our financial statements. In addition, we have discontinued our former practice of obtaining and relying upon BPOs in connection with valuing properties securing our loans. Management further intends to consult with subject matter experts when appropriate to determine appropriate loan valuation procedures or related accounting and regulatory requirements in situations not previously encountered by Bank accounting personnel and to institute second review procedures over financial reporting. The Audit Committee will also increase its oversight of the financial reporting process.

Except as described above, there has been no change in our internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

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**PART II. OTHER INFORMATION**

Item 1. LEGAL PROCEEDINGS  
*OTS Investigation*

In 2010, the OTS notified us that it had initiated a formal investigation of the activities of a former loan officer of the Bank whose employment was terminated in March 2010. In connection with the investigation, the OTS issued subpoenas to the chief lending officer and chief executive officer requesting documents relating to our former loan officer and loans he originated while employed by the Bank. The subpoenas also contemplate taking oral testimony from the officers. While the OTS did not inform us of the scope of its investigation, we believe the investigation includes, but may not be limited to, inquiry into whether documentation submitted in connection with loan applications for loans originated by the loan officer contained inaccurate or deliberately falsified information and whether the loan officer received unauthorized direct or indirect benefits from payments made by the borrowers on such loans to loan brokers or other persons associated with the lending process. All of the loans originated by the former loan officer have been reviewed by us and by the independent loan review firm we engaged to perform a general review of our loan portfolio pursuant to the C&D issued to us by the OTS. We have taken the results of these loan reviews into account, along with all other relevant information known to us, in determining the amounts of our loan loss provisions and the level of our loan loss reserves that we believe to be appropriate as of March 31, 2012.

Item 1A. RISK FACTORS  
Not Applicable

Item 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS  
None

Item 3. DEFAULTS UPON SENIOR SECURITIES  
None

Item 4. MINE SAFETY DISCLOSURES  
Not Applicable

Item 5. OTHER INFORMATION  
None

Item 6. EXHIBITS

- Exhibit 31.1 - Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- Exhibit 31.2 - Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

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|            |   |
|------------|---|
| Exhibit 32 | - Certifications of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 |
| 101.INS    | XBRL Instance Document (1)  |
| 101.SCH    | XBRL Taxonomy Extension Schema Document (1)   |
| 101.CAL    | XBRL Taxonomy Extension Calculation Linkbase Document (1)   |
| 101.DEF    | XBRL Taxonomy Extension Definitions Linkbase Document (1)   |

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| 101.LAB | XBRL Taxonomy Extension Label Linkbase Document (1)        |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase Document (1) |

- (1) Pursuant to SEC rules, these interactive data file exhibits shall not be deemed filed for purposes of Section 11 or 12 of the Securities Act or Section 18 of the Exchange Act or otherwise subject to the liability of those sections.



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**SIGNATURES**

In accordance with the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Date: September 21, 2012

By: /s/ Wayne-Kent A. Bradshaw  
Wayne-Kent A. Bradshaw  
Chief Executive Officer

Date: September 21, 2012

By: /s/ Samuel Sarpong  
Samuel Sarpong  
Chief Financial Officer