

CENTRAL FEDERAL CORP
Form 10-Q
May 10, 2016
UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark one)

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

For the quarterly period ended March 31, 2016

Or

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

For the transition period from _____ to _____

Commission File Number 0-25045

CENTRAL FEDERAL CORPORATION

(Exact name of registrant as specified in its charter)

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Delaware 34-1877137
(State or other jurisdiction of (IRS Employer
incorporation or organization) Identification No.)

7000 North High St., Worthington, Ohio 43085

(Address of principal executive offices) (Zip Code)

(614) 334-7979

(Registrant's telephone number, including area code)

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

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

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

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

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

Yes [] No[X]

As of May 6, 2016, there were 16,024,210 shares of the registrant's Common Stock outstanding.

CENTRAL FEDERAL CORPORATION

PART I. Financial Information	Page
Item 1. Financial Statements	3
Consolidated Balance Sheets as of March 31, 2016 (unaudited) and December 31, 2015	3
Consolidated Statements of Income for the three months ended March 31, 2016 and 2015 (unaudited)	4
Consolidated Statements of Comprehensive Income for the three months ended March 31, 2016 and 2015 (unaudited)	5
Consolidated Statements of Changes in Stockholders' Equity for the three months ended March 31, 2016 and 2015 (unaudited)	6
Consolidated Statements of Cash Flows for the three months ended March 31, 2016 and 2015 (unaudited)	7
Notes to Consolidated Financial Statements (three months ended March 31, 2016 and 2015 unaudited)	8
Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations	43
Item 3. Quantitative and Qualitative Disclosures About Market Risk	61
Item 4. Controls and Procedures	62
PART II. Other Information	63
Item 1. Legal Proceedings	63
Item 1A. Risk Factors	63
Item 2. Unregistered Sales of Equity Securities and Use of Proceeds	63
Item 3. Defaults Upon Senior Securities	63
Item 4. Mine Safety Disclosures	63
Item 5. Other Information	63
Item 6. Exhibits	63

Signatures



CENTRAL FEDERAL CORPORATION

CONSOLIDATED BALANCE SHEETS

(Dollars in thousands except per share data)

	March 31, 2016 (unaudited)	December 31, 2015
ASSETS		
Cash and cash equivalents	\$ 24,779	\$ 25,895
Interest-bearing deposits in other financial institutions	-	-
Securities available for sale	9,372	9,368
Loans held for sale, at fair value	1,598	889
Loans, net of allowance of \$6,716 and \$6,620	300,479	297,064
FHLB stock	1,942	1,942
Foreclosed assets, net	1,636	1,636
Premises and equipment, net	3,561	3,609
Bank owned life insurance	4,830	4,797
Accrued interest receivable and other assets	5,154	6,093
Total assets	\$ 353,351	\$ 351,293
LIABILITIES AND STOCKHOLDERS' EQUITY		
Deposits		
Noninterest bearing	\$ 37,266	\$ 42,926
Interest bearing	255,168	247,541
Total deposits	292,434	290,467
FHLB advances	14,500	14,500
Advances by borrowers for taxes and insurance	353	656
Accrued interest payable and other liabilities	2,369	2,203
Subordinated debentures	5,155	5,155
Total liabilities	314,811	312,981
Commitments and contingent liabilities	-	-
Stockholders' equity		
Common stock, \$.01 par value; shares authorized: 50,000,000; shares issued: 16,135,917 in 2016 and 16,135,917 in 2015	161	161
Series B Preferred stock, \$.01 par value; 480,000 shares authorized; 480,000 issued at March 31, 2016 and December 31, 2015	5	5
Additional paid-in capital	59,994	59,937
Accumulated deficit	(18,435)	(18,537)
Accumulated other comprehensive income	60	(9)

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Treasury stock, at cost; 111,707 shares of common stock	(3,245)	(3,245)
Total stockholders' equity	38,540	38,312
Total liabilities and stockholders' equity	\$ 353,351	\$ 351,293

See accompanying notes to consolidated financial statements.

3

CENTRAL FEDERAL CORPORATION

CONSOLIDATED STATEMENTS OF INCOME

(Dollars in thousands except per share data)

(Unaudited)

	Three months ended March 31,	
	2016	2015
Interest and dividend income		
Loans, including fees	\$ 3,279	\$ 2,946
Securities	30	35
FHLB stock dividends	20	20
Federal funds sold and other	29	17
	3,358	3,018
Interest expense		
Deposits	589	485
FHLB advances and other debt	58	57
Subordinated debentures	45	40
	692	582
Net interest income	2,666	2,436
Provision for loan losses	50	75
Net interest income after provision for loan losses	2,616	2,361
Noninterest income		
Service charges on deposit accounts	173	116
Net gains on sales of loans	28	84
Net gain (loss) on sales of securities	-	(12)
Earnings on bank owned life insurance	33	32
Other	70	135
	304	355
Noninterest expense		
Salaries and employee benefits	1,152	1,220
Occupancy and equipment	134	139
Data processing	275	249
Franchise and other taxes	88	80
Professional fees	324	244
Director fees	47	33
Postage, printing and supplies	54	72
Advertising and promotion	17	45
Telephone	31	25
Loan expenses	31	37
Foreclosed assets, net	33	46
Depreciation	53	52
FDIC premiums	114	104

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Regulatory assessment	28	51
Other insurance	31	30
Other	42	38
	2,454	2,465
Income before incomes taxes	466	251
Income tax expense	150	-
Net income	316	251
Dividends on Series B preferred stock and accretion of discount	(214)	(214)
Net income attributable to common stockholders	\$ 102	\$ 37
Earnings per common share:		
Basic	\$ 0.01	\$ 0.00
Diluted	\$ 0.01	\$ 0.00

See accompanying notes to consolidated financial statements.

CENTRAL FEDERAL CORPORATION

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Dollars in thousands except per share data)

(Unaudited)

	Three months ended March 31, 2016 2015	
Net income	\$ 316	\$ 251
Other comprehensive income:		
Unrealized holding gain arising during the period related to securities available for sale, net of tax of \$37 and \$0	69	34
Less: reclassification adjustment for net losses realized during the period on investment securities available for sale, net of tax of \$0 and \$0	-	12
Other comprehensive income (loss), net of tax	69	46
Comprehensive income	\$ 385	\$ 297

See accompanying notes to consolidated financial statements.

5

CENTRAL FEDERAL CORPORATION

CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY

(Dollars in thousands except per share data)

(Unaudited)

	Common Stock	Series	Additional Paid-In Capital	Accumulated Deficit	Accumulated		Total Stockholders' Equity
		B Preferred Stock			Other Comprehensive Income	Treasury Stock	
Balance at January 1, 2016	\$ 161	\$ 5	\$ 59,937	\$ (18,537)	\$ (9)	\$ (3,245)	\$ 38,312
Net income				316			316
Other comprehensive income (loss)					69		69
Restricted option expense, net of forfeitures			22				22
Stock option expense, net of forfeitures			8				8
Cash dividends declared on Series B preferred stock and accretion of discount			27	(214)			(187)
Balance at March 31, 2016	\$ 161	\$ 5	\$ 59,994	\$ (18,435)	\$ 60	\$ (3,245)	\$ 38,540

	Common Stock	Series	Additional Paid-In Capital	Accumulated Deficit	Accumulated		Total Stockholders' Equity
		B Preferred Stock			Other Comprehensive Income	Treasury Stock	
Balance at January 1, 2015	\$ 159	\$ 5	\$ 59,696	\$ (22,157)	\$ 51	\$ (3,245)	\$ 34,509
Net income (loss)				251			251
Other comprehensive income (loss)					46		46
			35				35

Stock option expense, net of forfeitures							
Cash dividends declared on Series B preferred stock and accretion of discount			27	(214)			(187)
Balance at March 31, 2015	\$ 159	\$ 5	\$ 59,758	\$ (22,120)	\$ 97	\$ (3,245)	\$ 34,654

See accompanying notes to consolidated financial statements.

6

CENTRAL FEDERAL CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Dollars in thousands)

(Unaudited)

	Three months ended March 31,	
	2016	2015
Net Income	\$ 316	\$ 251
Adjustments to reconcile net loss to net cash from operating activities:		
Provision for loan losses	50	75
Depreciation	53	52
Amortization, net	(8)	(6)
Net loss on sales of securities	-	12
Originations of loans held for sale	(2,936)	(12,123)
Proceeds from sale of loans held for sale	2,255	14,134
Net gains on sales of loans	(28)	(84)
Earnings on bank owned life insurance	(33)	(32)
Stock-based compensation expense	30	35
Change in deferred income taxes	(31)	-
Net change in:		
Accrued interest receivable and other assets	939	362
Accrued interest payable and other liabilities	166	(135)
Net cash from operating activities	773	2,541
Cash flows from investing activities		
Available-for-sale securities:		
Maturities, prepayments and calls	86	1,073
Loan originations and payments, net	(4,567)	(10,049)
Proceeds from the sale of loans	1,124	-
Additions to premises and equipment	(6)	(6)
Net cash used by investing activities	(3,363)	(8,982)
Cash flows from financing activities		
Net change in deposits	1,964	2,415
Proceeds from FHLB advances	-	2,500
Repayments on FHLB advances	-	(2,500)
Net change in advances by borrowers for taxes and insurance	(303)	(100)
Cash dividends paid on Series B preferred stock	(187)	(187)
Net cash from financing activities	1,474	2,128

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Net change in cash and cash equivalents	(1,116)	(4,313)
Beginning cash and cash equivalents	25,895	28,207
Ending cash and cash equivalents	\$ 24,779	\$ 23,894
Supplemental cash flow information:		
Interest paid	\$ 687	\$ 578
Supplemental noncash disclosures:		
Loans transferred from held for sale to portfolio	\$ -	834
Dividends payable on Series B preferred stock	187	187

See accompanying notes to consolidated financial statements.

7

CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands)

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation:

The consolidated financial statements include Central Federal Corporation (the “Holding Company”) and its wholly-owned subsidiary, CFBank. The Holding Company and CFBank are sometimes collectively referred to herein as the “Company”. Intercompany transactions and balances are eliminated in consolidation. The accompanying unaudited interim consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (the “SEC”) and in compliance with U.S. generally accepted accounting principles (GAAP). Because this report is based on an interim period, certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted.

In the opinion of the management of the Company, the accompanying unaudited interim consolidated financial statements include all adjustments necessary for a fair presentation of the Company’s financial condition and the results of operations for the periods presented. These adjustments are of a normal recurring nature, unless otherwise disclosed in this Form 10-Q. The financial performance reported for the Company for the three months ended March 31, 2016 is not necessarily indicative of the results that may be expected for the full year. This information should be read in conjunction with the Company’s latest Annual Report to Stockholders and Annual Report on Form 10-K on file with the SEC. Reference is made to the accounting policies of the Company described in Note 1 to the Audited Consolidated Financial Statements contained in the Company’s 2015 Annual Report to Stockholders that was filed as Exhibit 13.1 to the Company’s Form 10-K for the year ended December 31, 2015 (referred to herein as the “2015 Audited Financial Statements”). The Company has consistently followed those policies in preparing this Form 10-Q.

Loans: Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are reported at the principal balance outstanding, adjusted for purchase premiums and discounts, deferred loan fees and costs and an allowance for loan losses (ALLL). Interest income is accrued on the unpaid principal balance. Loan origination fees, net of certain direct origination costs, are deferred and recognized in interest income using the level yield method without anticipating prepayments.

The accrual of interest income on all classes of loans, except other consumer loans, is discontinued and the loan is placed on nonaccrual status at the time the loan is 90 days delinquent unless the loan is well-secured and in process of collection. Other consumer loans are typically charged off no later than 90 days past due. Past due status is based on the contractual terms of the loan for all classes of loans. In all cases, loans are placed on nonaccrual or charged-off at an earlier date if collection of principal or interest is considered doubtful. Nonaccrual loans and loans past due 90 days still on accrual include both smaller balance homogeneous loans that are collectively evaluated for impairment and individually classified impaired loans. Commercial loans, multi-family residential real estate loans and commercial real estate loans placed on nonaccrual status are individually classified as impaired loans.

All interest accrued but not received for loans placed on nonaccrual is reversed against interest income in the period in which the loan is placed in a nonaccrual status. Interest received on such loans is accounted for on the cash-basis or cost recovery method, until qualifying for return to accrual status. Loans are considered for return to accrual status if and when all the principal and interest amounts that are contractually due are brought current, there is a current and well documented credit analysis, there is reasonable assurance of repayment of principal and interest, and the

customer has demonstrated sustained, amortizing payment performance of at least six months.

Allowance for Loan Losses (ALLL): The ALLL is a valuation allowance for probable incurred credit losses. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance. Management estimates the allowance balance required using past loan loss experience, the nature and volume of the portfolio, information about specific borrower situations and estimated collateral values, economic conditions, and other factors. Allocations of the allowance may be made for specific loans, but the entire allowance is available for any loan that, in management's judgment, should be charged off.

The allowance consists of specific and general components. The specific component relates to loans that are individually classified as impaired. A loan is impaired when, based on current information and events, it is probable that CFBank will be unable to collect all amounts due according to the contractual terms of the loan agreement. Loans within any loan class for which the terms have been modified resulting in a concession, and for which the borrower is experiencing financial difficulties, are considered troubled debt restructurings (TDRs) and classified as impaired.

CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands)

Factors considered by management in determining impairment for all loan classes include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record and the amount of the shortfall in relation to the principal and interest owed.

All loans within the commercial, multi-family residential and commercial real estate segments, regardless of size, and loans of all other classes with balances over \$250 are individually evaluated for impairment when they are 90 days past due, or earlier than 90 days past due if information regarding the payment capacity of the borrower indicates that payment in full according to the loan terms is doubtful. If a loan is impaired, a portion of the allowance is allocated so that the loan is reported, net, at the present value of estimated future cash flows using the loan's existing rate, or at the fair value of collateral, less costs to sell, if repayment is expected solely from the collateral. Large groups of smaller balance homogeneous loans, such as consumer and single-family residential real estate loans, are collectively evaluated for impairment, and accordingly, they are not separately identified for impairment disclosures.

TDRs of all classes of loans are separately identified for impairment disclosures and are measured at the present value of estimated future cash flows using the loan's effective rate at inception. If a TDR is considered to be a collateral dependent loan, the loan is reported, net, at the fair value of the collateral. If the payment of the loan is dependent on the sale of the collateral, then costs to liquidate the collateral are included when determining the impairment. For TDRs that subsequently default, the amount of reserve is determined in accordance with the accounting policy for the ALLL.

Interest income on all classes of impaired loans that are on nonaccrual status is recognized in accordance with the accounting policy on nonaccrual loans. Cash receipts on all classes of impaired loans that are on nonaccrual status are generally applied to the principal balance outstanding. Interest income on all classes of impaired loans that are not on nonaccrual status is recognized on the accrual method. TDRs may be classified as accruing if the borrower has been current for a period of at least six months with respect to loan payments and management expects that the borrower will be able to continue to make payments in accordance with the terms of the restructured loan.

The general reserve component covers non-impaired loans of all classes and is based on historical loss experience adjusted for current factors. The historical loss experience is determined by loan class and is based on the actual loss history experienced by CFBank over a three-year period. The general component is calculated based on CFBank's loan balances and actual three-year historical loss rates. For loans with little or no actual loss experience, industry estimates are used based on loan segment. This actual loss experience is supplemented with other economic and judgmental factors based on the risks present for each loan class. These economic and judgmental factors include consideration of the following: levels of and trends in delinquencies and impaired loans; levels of and trends in charge-offs and recoveries; trends in volume and terms of loans; effects of any changes in risk selection and underwriting standards; other changes in lending policies, procedures, and practices; experience, ability, and depth of lending management and other relevant staff; national and local economic trends and conditions; industry conditions; and effects of changes in credit concentrations.

CFBank's charge-off policy for commercial loans, single-family residential real estate loans, multi-family residential real estate loans, commercial real estate loans, construction loans and home equity lines of credit requires management to record a specific reserve or charge-off as soon as it is apparent that the borrower is troubled and there is, or likely will be, a collateral shortfall related to the estimated value of the collateral securing the loan. Other consumer loans are typically charged off no later than 90 days past due.

Joint Ventures: The Holding Company has contributed funds into a series of joint ventures (equity stake) for the purpose of allocating excess liquidity into higher earning assets while diversifying its revenue sources. The funding for the joint ventures is related to shorter term operating activities and is related to the development of single family real estate in the form of condominiums. Income is recognized based on a rate of return on the outstanding investment balance. As units are sold, the Holding Company receives an additional incentive payment, which is recognized as income.

9

CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands)

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

	Three months ended March 31,	
	2016 (unaudited)	2015 (unaudited)
Basic		
Net income	\$ 316	\$ 251
Dividends on Series B preferred stock and accretion of discount	(214)	(214)
Net income allocated to common stockholders	\$ 102	\$ 37
Weighted average common shares outstanding including unvested share-based payment awards	16,024,210	15,823,710
Less: Unvested share-based payment awards	-	-
Average shares	16,024,210	15,823,710
Basic earnings per common share	\$ 0.01	\$ 0.00
Diluted		
Net earnings allocated to common stockholders	\$ 102	\$ 37
Weighted average common shares outstanding for basic earnings per common share	16,024,210	15,823,710
Add: Dilutive effects of assumed exercises of stock options	9,778	7,444
Add: Dilutive effects of assumed exercises of Series B preferred stock	-	-
Average shares and dilutive potential common shares	16,033,988	15,831,154
Diluted earnings per common share	\$ 0.01	\$ 0.00

The following securities exercisable for or convertible into common shares were anti-dilutive and not considered in computing diluted earnings (loss) per common share.

Three months ended
March 31,

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	2016	2015
	(unaudited)	(unaudited)
Stock options	394,196	456,396
Series B preferred stock	6,857,143	6,857,143
Stock warrants	1,152,125	1,152,125

10

CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands)

Adoption of New Accounting Standards:

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (Topic 606) (May 2014). The topic of Revenue Recognition had become broad with several other regulatory agencies issuing standards, which lacked cohesion. The new guidance establishes a “comprehensive framework” and “reduces the number of requirements to which an entity must consider in recognizing revenue” and yet provides improved disclosures to assist stakeholders reviewing financial statements. The amendments in this Update are effective for annual reporting periods beginning after December 15, 2017. Early adoption is not permitted. The Company will adopt the methodologies prescribed by this ASU by the date required. Adoption of the ASU is not expected to have a significant effect on the Company's consolidated financial statements.

In June 2014, the FASB issued ASU 2014-12, Compensation - Stock Compensation (Topic 718): Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period (June 2014). This Update defines the accounting treatment for share-based payments and “resolves the diverse accounting treatment of those awards in practice.” The new requirement mandates that “a performance target that affects vesting and that could be achieved after the requisite service period be treated as a performance condition.” Compensation cost will now be recognized in the period in which it becomes likely that the performance target will be met. The amendments in this Update are effective for annual reporting periods beginning after December 15, 2015. Early adoption is permitted. The Company will adopt the methodologies prescribed by this ASU by the date required. Adoption of the ASU is not expected to have a significant effect on the Company's consolidated financial statements.

In January 2016, the FASB issued ASU 2016-01, Financial Instruments—Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities. ASU 2016-01 amends the guidance in U.S. GAAP on the accounting for equity investments, financial liabilities under the fair value option and the presentations and disclosure requirements of financial instruments. ASU 2016-01 is effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. Early adoption is permitted for the accounting guidance on financial liabilities under the fair value option. The Company will adopt the methodologies prescribed by the ASU by the date required. Adoption of the ASU is not expected to have a significant effect on the Company's consolidated financial statements.

On February 25, 2016, the FASB issued Accounting Standards Update (ASU) 2016-02, Leases (Topic 842), the long-awaited new standard on lease accounting. Under the new ASU, lessees will recognize lease assets and liabilities on their balance sheet for all leases with terms of more than 12 months. The new lessee accounting model retains two types of leases, and is consistent with the lessee accounting model under existing GAAP. One type of lease (finance leases) will be accounted for in substantially the same manner as capital leases are accounted for today. The other type of lease (operating leases) will be accounted for (both in the income statement and statement of cash flows) in a manner consistent with today's operating leases. Lessor accounting under the new standard is fundamentally consistent with existing GAAP. Lessees and lessors would be required to provide additional qualitative and quantitative disclosures to help financial statement users assess the amount, timing, and uncertainty of cash flows arising from leases. These disclosures are intended to supplement the amounts recorded in the financial statements so that users can understand more about the nature of an organization's leasing activities. For public business entities, the final leases standard will be effective for fiscal years beginning after December 15, 2018 including interim periods

within those fiscal years. Early application is permitted. The Company will adopt the methodologies prescribed by this ASU by the date required. Adoption of the ASU is not expected to have a significant effect on the Company's consolidated financial statements.

11

CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands)

The FASB has issued ASU No. 2015-03, Interest – Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs. The amendments in this ASU require that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The recognition and measurement guidance for debt issuance costs are not affected by the amendments in this ASU. For public business entities, the amendments are effective for financial statements issued for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years. The amendments should be applied on a retrospective basis, wherein the balance sheet of each individual period presented should be adjusted to reflect the period-specific effects of applying the new guidance. Upon transition, an entity is required to comply with the applicable disclosures for a change in an accounting principle. These disclosures include the nature of and reason for the change in accounting principle, the transition method, a description of the prior-period information that has been retrospectively adjusted and the effect of the change on the financial statement line items, i.e., debt issuance cost asset and the debt liability. The Company has adopted the methodologies prescribed by this ASU. Adoption of the ASU did not have a significant effect on the Company's consolidated financial statements.

General Litigation

The Company is subject to claims and lawsuits that arise primarily in the ordinary course of business. It is the opinion of management that the disposition or ultimate resolution of such claims and lawsuits will not have a material adverse effect on the consolidated financial position, results of operations and cash flows of the Company.

Reclassifications

Reclassification of certain amounts in the 2015 consolidated financial statements have been made to conform to the 2016 presentation.

NOTE 2- REGULATORY ORDER CONSIDERATIONS

Regulatory Order Considerations:

On May 25, 2011, the Holding Company and CFBank each consented to the issuance of an Order to Cease and Desist (the “Holding Company Order” and the “CFBank Order”, respectively, and collectively, the “Orders”) by the Office of Thrift Supervision (the “OTS”), the primary regulator of the Holding Company and CFBank at the time the Orders were issued. In July 2011, in accordance with the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”), the Federal Reserve Board (the “FRB”) replaced the OTS as the primary regulator of the Holding Company and the Office of the Comptroller of the Currency (the “OCC”) replaced the OTS as the primary regulator of CFBank. The Orders imposed significant directives applicable to the Holding Company and CFBank, including requirements that we maintain heightened capital levels, reduce the level of our classified and criticized assets, achieve growth and operating metrics in line with an approved business plan, and comply with restrictions on brokered deposits and on certain types of lending and prohibitions on dividends and repurchases of our capital stock.

Effective as of January 23, 2014, the OCC released and terminated the CFBank Order based upon the improved capital position of CFBank, among other factors. Notwithstanding the release of the CFBank Order, CFBank was required to continue to maintain a minimum Tier 1 Leverage Capital Ratio of 8% and a Total Risk-based Capital to Risk-Weighted Assets ratio of 12% until December 23, 2015. In addition, in connection with the release and termination of the CFBank Order, CFBank made certain commitments to the OCC to continue to adhere to certain prudent practices, including, without limitation, maintaining a written program to continue to improve CFBank's credit underwriting and administrative process; take actions to protect its interest in criticized assets as identified by CFBank, the OCC examiners or its external loan review process; implement its written program to effectively identify, monitor, control and continue to reduce the level of credit risk to CFBank; review and monitor progress against such plan with the Board of Directors; and continue CFBank's aggressive workout efforts and individualized workout plans on all criticized assets greater than \$250,000. The foregoing commitments remained in place until December 23, 2015.

12

CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands)

On May 15, 2014, the FRB announced the termination of the Holding Company Order, effective as of May 9, 2014. Notwithstanding the termination of the Holding Company Order, the Holding Company was required to continue to adhere to certain requirements and restrictions based on commitments made to the FRB in connection with the termination of the Holding Company Order. These commitments required the Holding Company, among other things, to continue to implement certain actions in accordance with the capital plan previously submitted to the FRB; not declare or pay dividends on its stock, purchase or redeem its stock, or accept dividends or other capital distributions from CFBank without the prior written approval of the FRB; not incur, increase or guarantee any debt without the prior written consent of the FRB; and provide prior written notice to the FRB with respect to certain changes in directors and senior executive officers. The foregoing commitments remained in place until January 8, 2016.

The significant directives contained in the Orders and the commitments made by CFBank and the Holding Company in connection with the release and termination of the Orders provided challenges for the operation of our business and our ability to effectively compete in our markets over the past several years. In addition, the Orders and our subsequent commitments to the regulators required that we obtain approval from our regulators for any deviations from our business plan, which limited our flexibility to make changes to the scope of our business activities.

Under the terms of the Holding Company Order, the Holding Company was prohibited from declaring or paying any dividends on its stock, repurchasing any of its stock, or making any capital contributions to CFBank except with the prior approval of the FRB. In accordance with the commitments made by the Holding Company in connection with the release and termination of the Holding Company Order, the Holding Company remained subject to such restrictions until January 8, 2016.

The ability of the Holding Company to pay dividends on its common stock and Series B Preferred Stock is generally dependent upon the receipt of dividends and other distributions from CFBank. The Holding Company is a legal entity that is separate and distinct from CFBank, which has no obligation to make any dividends or other funds available for the payment of dividends by the Holding Company. The Holding Company also is subject to various legal and regulatory policies and guidelines impacting the Holding Company's ability to pay dividends on its stock. In addition, the Holding Company's ability to pay dividends on its stock is conditioned upon the payment, on a current basis, of quarterly interest payments on the subordinated debentures underlying the Company's trust preferred securities. Finally, so long as the Company's Series B Preferred Stock remains outstanding, the Holding Company will be prohibited from paying dividends on (other than dividends payable solely in shares) the Company's common stock, for the then-current dividend period, unless full dividends on the Series B Preferred Stock have been paid or set aside for payment. Dividends on the Series B Preferred Stock are non-cumulative, which means that if for any reason we do not declare cash dividends on the Series B Preferred Stock for a quarterly dividend period we will have no obligation to pay any dividends for that period (i.e., the dividends will not accrue or cumulate), whether or not we declare dividends on the Series B Preferred Stock for any subsequent dividend period.

CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands)

NOTE 3 – SECURITIES

The following table summarizes the amortized cost and fair value of the available-for-sale securities portfolio at March 31, 2016 and December 31, 2015 and the corresponding amounts of unrealized gains and losses recognized in accumulated other comprehensive income (loss):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
March 31, 2016 (unaudited)				
Issued by U.S. government-sponsored entities and agencies:				
U.S. Treasury	\$ 8,566	\$ 63	\$ 1	\$ 8,628
Mortgage-backed securities - residential	432	17	-	449
Collateralized mortgage obligations	283	12	-	295
Total	\$ 9,281	\$ 92	\$ 1	\$ 9,372

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
December 31, 2015				
Issued by U.S. government-sponsored entities and agencies:				
U.S. Treasury	\$ 8,575	\$ 4	\$ 43	\$ 8,536
Mortgage-backed securities - residential	463	18	-	481
Collateralized mortgage obligations	339	12	-	351
Total	\$ 9,377	\$ 34	\$ 43	\$ 9,368

There was no other-than-temporary impairment recognized in accumulated other comprehensive income (loss) for securities available for sale at March 31, 2016 or March 31, 2015.

There were no sales of securities for the three months ended March 31, 2016 or March 31, 2015; however, there was an early redemption of a municipal security during the first quarter of 2015 which is reflected in net gain (loss) on sales of securities.

CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands)

The amortized cost and fair value of debt securities at March 31, 2016 and December 31, 2015 are shown in the table below by contractual maturity. 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 are shown separately.

	March 31, 2016 (unaudited)		December 31, 2015	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due in one year or less	\$ 1,002	\$ 1,002	\$ 1,002	\$ 1,000
Due from one to five years	7,564	7,626	7,573	7,536
Mortgage-backed securities	432	449	463	481
Collateralized mortgage obligations	283	295	339	351
Total	\$ 9,281	\$ 9,372	\$ 9,377	\$ 9,368

Fair value of securities pledged was as follows:

	March 31, 2016 (unaudited)	December 31, 2015
Pledged as collateral for:		
FHLB advances	\$ 3,491	\$ 3,530
Public deposits	2,064	2,055
Interest-rate swaps	243	261
Total	\$ 5,798	\$ 5,846

At March 31, 2016 and December 31, 2015, there were no holdings of securities of any one issuer, other than U.S. government-sponsored entities and agencies, in an amount greater than 10% of stockholders' equity.

CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands)

The following table summarizes securities with unrealized losses at March 31, 2016 and December 31, 2015 aggregated by major security type and length of time in a continuous unrealized loss position.

March 31, 2016 (unaudited)	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
Description of Securities Issued by U.S. government-sponsored entities and agencies:						
U.S. Treasury	\$ 1,518	\$ 1	\$ -	\$ -	\$ 1,518	\$ 1
Mortgage-backed securities - residential	-	-	-	-	-	-
Collateralized mortgage obligations	3	-	-	-	3	-
Total temporarily impaired	\$ 1,521	\$ 1	\$ -	\$ -	\$ 1,521	\$ 1

December 31, 2015	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
Description of Securities Issued by U.S. government-sponsored entities and agencies:						
U.S. Treasury	\$ 6,541	\$ 43	\$ -	\$ -	\$ 6,541	\$ 43
Mortgage-backed securities - residential	-	-	-	-	-	-
Collateralized mortgage obligations	-	-	-	-	-	-
Total temporarily impaired	\$ 6,541	\$ 43	\$ -	\$ -	\$ 6,541	\$ 43

The unrealized losses in U.S Treasuries at March 31, 2016 are related to two securities. The unrealized losses in U.S. Treasuries at December 31, 2015 are related to multiple securities. Because the decline in fair value is attributable to changes in market conditions, and not credit quality, and because the Company does not have the intent to sell these

securities and it is likely that it will not be required to sell these securities before their anticipated recovery, the Company did not consider these securities to be other-than-temporarily impaired at March 31, 2016 and December 31, 2015.

CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands)

NOTE 4 – LOANS

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

	March 31, 2016 (unaudited)	December 31, 2015
Commercial	\$ 47,505	\$ 43,744
Real estate:		
Single-family residential	80,367	81,985
Multi-family residential	30,369	28,950
Commercial	98,116	96,488
Construction	23,064	24,662
Consumer:		
Home equity lines of credit	23,250	21,837
Other	4,524	6,018
Subtotal	307,195	303,684
Less: ALLL	(6,716)	(6,620)
Loans, net	\$ 300,479	\$ 297,064

Mortgage Purchase Program

CFBank has participated in a Mortgage Purchase Program with Northpointe Bank (Northpointe), a Michigan banking corporation, since December 2012. Pursuant to the terms of a participation agreement, CFBank purchases participation interests in loans made by Northpointe related to fully underwritten and pre-sold mortgage loans originated by various prescreened mortgage brokers located throughout the U.S. The underlying loans are individually (MERS) registered loans which are held until funded by the end investor. The mortgage loan investors include Fannie Mae and Freddie Mac, and other major financial institutions such as Wells Fargo Bank. This process on average takes approximately 14 days. Given the short-term holding period of the underlying loans, common credit risks (such as past due, impairment and TDR, nonperforming, and nonaccrual classification) are substantially reduced. Therefore, no allowance is allocated by CFBank to these loans. These loans are 100% risk rated for CFBank capital adequacy purposes. Under the participation agreement, CFBank agrees to purchase a 95% ownership/participation interest in each of the aforementioned loans, and Northpointe maintains a 5% ownership interest in each loan it participates. At March 31, 2016 and December 31, 2015, CFBank held \$38,572 and \$43,517,

respectively, of such loans which have been included in single-family residential loan totals above.

17

CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands)

Allowance for Loan Losses

The ALLL is a valuation allowance for probable incurred credit losses in the loan portfolio based on management's evaluation of various factors including past loan loss experience, the nature and volume of the portfolio, information about specific borrower situations and estimated collateral values, economic conditions and other factors. A provision for loan losses is charged to operations based on management's periodic evaluation of these and other pertinent factors described in Note 1 to the 2015 Audited Financial Statements.

The following table presents the activity in the ALLL by portfolio segment for the three months ended March 31, 2016:

	Three months ended March 31, 2016 (unaudited)					Consumer		Total
	Real Estate			Commercial	Construction	Home	Other	
	Commercial	Single-family	Multi-family					Equity lines of credit
Beginning balance	\$ 1,380	\$ 691	\$ 705	\$ 2,710	\$ 561	\$ 474	\$ 99	\$ 6,620
Addition to (reduction in) provision for loan losses	106	50	17	(101)	(38)	50	(34)	50
Charge-offs	-	-	-	-	-	-	-	-
Recoveries	-	-	-	-	-	46	-	46
Ending balance	\$ 1,486	\$ 741	\$ 722	\$ 2,609	\$ 523	\$ 570	\$ 65	\$ 6,716

The following table presents the activity in the ALLL by portfolio segment for the three months ended March 31, 2015:

	Three months ended March 31, 2015 (unaudited)					Consumer		Total
	Real Estate			Commercial	Construction	Home	Other	
	Commercial	Single-family	Multi-family					Equity lines

						of credit		
Beginning balance	\$ 1,346	\$ 634	\$ 818	\$ 2,541	\$ 442	\$ 441	\$ 94	\$ 6,316
Addition to (reduction in) provision for loan losses	88	65	(125)	(77)	99	23	2	75
Charge-offs	(8)	-	-	-	-	-	(10)	(18)
Recoveries	25	1	-	33	-	4	6	69
Ending balance	\$ 1,451	\$ 700	\$ 693	\$ 2,497	\$ 541	\$ 468	\$ 92	\$ 6,442

CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands)

The following table presents the balance in the ALLL and the recorded investment in loans by portfolio segment and based on the impairment method as of March 31, 2016 (unaudited):

	Real Estate			Commercial	Construction	Consumer		Total
	Commercial	Single-family	Multi-family			Home Equity lines of credit	Other	
ALLL:								
Ending allowance balance attributable to loans:								
Individually evaluated for impairment	\$ 54	\$ 1	\$ -	\$ 27	\$ -	\$ -	\$ -	\$ 82
Collectively evaluated for impairment	1,432	740	722	2,582	523	570	65	6,634
Total ending allowance balance	\$ 1,486	\$ 741	\$ 722	\$ 2,609	\$ 523	\$ 570	\$ 65	\$ 6,716
Loans:								
Individually evaluated for impairment	\$ 721	\$ 287	\$ 1,577	\$ 3,627	\$ -	\$ -	\$ -	\$ 6,212
Collectively evaluated for impairment	46,784	80,080	28,792	94,489	23,064	23,250	4,524	300,983
Total ending loan balance	\$ 47,505	\$ 80,367	\$ 30,369	\$ 98,116	\$ 23,064	\$ 23,250	\$ 4,524	\$ 307,195

The following table presents the balance in the ALLL and the recorded investment in loans by portfolio segment and based on the impairment method as of December 31, 2015:

	Real Estate			Consumer Home Equity lines of credit			Other	Total
	Commercial	Single-family	Multi-family	Commercial	Construction			
ALLL:								
Ending allowance balance attributable to loans:								
Individually evaluated for impairment	\$ 5	\$ 1	\$ -	\$ 14	\$ -	\$ -	\$ -	\$ 20
Collectively evaluated for impairment	1,375	690	705	2,696	561	474	99	6,600
Total ending allowance balance	\$ 1,380	\$ 691	\$ 705	\$ 2,710	\$ 561	\$ 474	\$ 99	\$ 6,620
Loans:								
Individually evaluated for impairment	422	\$ 289	\$ 1,590	\$ 3,449	\$ -	\$ -	\$ -	\$ 5,750
Collectively evaluated for impairment	43,322	81,696	27,360	93,039	24,662	21,837	6,018	297,934
Total ending loan balance	\$ 43,744	\$ 81,985	\$ 28,950	\$ 96,488	\$ 24,662	\$ 21,837	\$ 6,018	\$ 303,684

CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands)

The following table presents loans individually evaluated for impairment by class of loans at March 31, 2016. The unpaid principal balance is the contractual principal balance outstanding. The recorded investment is the unpaid principal balance adjusted for partial charge-offs, purchase premiums and discounts, deferred loan fees and costs. The table presents accrual basis interest income recognized during the three months ended March 31, 2016. Cash payments of interest on these loans during the three months ended March 31, 2016 totaled \$79.

	As of March 31, 2016 (unaudited)			Three months ended March 31, 2016 (unaudited)	
	Unpaid Principal Balance	Recorded Investment	ALLL Allocated	Average Recorded Investment	Interest Recognized
With no related allowance recorded:					
Commercial	\$ 36	\$ 28	\$ -	\$ 28	\$ -
Real estate:					
Single-family residential	322	161	-	161	-
Multi-family residential	1,534	1,534	-	1,539	23
Commercial:					
Non-owner occupied	546	446	-	446	-
Owner occupied	890	368	-	370	9
Land	-	-	-	-	-
Total with no allowance recorded	3,328	2,537	-	2,544	32
With an allowance recorded:					
Commercial	694	693	54	701	2
Real estate:					
Single-family residential	127	126	1	127	2
Multi-family residential	43	43	-	44	1
Commercial:					
Non-owner occupied	2,213	2,214	21	2,217	33
Owner occupied	359	360	3	361	5
Land	284	239	3	242	4
Total with an allowance recorded	3,720	3,675	82	3,692	47
Total	\$ 7,048	\$ 6,212	\$ 82	\$ 6,236	\$ 79

CENTRAL FEDERAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands)

The following table presents loans individually evaluated for impairment by class of loans at December 31, 2015. The unpaid principal balance is the contractual principal balance outstanding. The recorded investment is the unpaid principal balance adjusted for partial charge-offs, purchase premiums and discounts, deferred loan fees and costs. The table presents accrual basis interest income recognized during the three months ended March 31, 2015. Cash payments of interest during the three months ended March 31, 2015 totaled \$83.

	As of December 31, 2015			Three months ended March 31, 2015 (unaudited)	
	Unpaid Principal Balance	Recorded Investment	ALLL Allocated	Average Recorded Investment	Interest Recognized
With no related allowance recorded:					
Commercial	\$ 36	\$ 28	\$ -	\$ 69	\$ 1
Real estate:					
Single-family residential	322	161	-	171	-
Multi-family residential	1,545	1,545	-	1,574	23
Commercial:					
Non-owner occupied	546	446	-	468	-
Owner occupied	688	167	-	180	10
Land	-	-	-	-	-
Total with no allowance recorded					