

FIRST DEFIANCE FINANCIAL CORP
Form 10-K
February 28, 2014

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-K

(Mark One)

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

For the fiscal year Ended December 31, 2013

or

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

Commission File Number 0-26850

FIRST DEFIANCE FINANCIAL CORP.

(Exact name of registrant as specified in its charter)

OHIO

(State or other jurisdiction of incorporation or organization)

601 Clinton Street, Defiance, Ohio

(Address of principal executive offices)

34-1803915

(I.R.S. Employer Identification Number)

43512

(Zip code)

Registrant's telephone number, including area code: **(419) 782-5015**

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

Common Stock, Par Value \$0.01 Per Share

(Title of Class)

The NASDAQ Stock Market

(Name of each exchange on which registered)

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

None

(Title of Class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes " No ☒

Indicate by check mark if registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act.

Yes " No ☒

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 Website, 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 "

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Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. "

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 definitions of "accelerated filer", "large 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 ☒

The aggregate market value of the voting stock held by non-affiliates of the Registrant computed by reference to the average bid and ask price of such stock as of June 30, 2013 was approximately \$210.8 million.

As of February 21, 2014, there were issued and outstanding 9,653,238 shares of the Registrant's common stock.

Documents Incorporated by Reference

Part III of this Form 10-K incorporates by reference certain information from the registrant's definitive Proxy Statement for the 2014 Annual Shareholders' Meeting.

**First Defiance Financial Corp.
Annual Report on Form 10-K**

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PART I

Item 1. Business

First Defiance Financial Corp. (“First Defiance” or “the Company”) is a unitary thrift holding company that, through its subsidiaries, First Federal Bank of the Midwest (“First Federal”), First Insurance Group of the Midwest, Inc. (“First Insurance”), and First Defiance Risk Management Inc. (collectively, “the Subsidiaries”), focuses on traditional banking and property and casualty, life and group health insurance products. First Federal’s banking activities include originating and servicing residential, commercial, and consumer loans and providing a broad range of depository services. First Insurance’s activities consist primarily of selling property and casualty, life and group health insurance products. First Defiance Risk Management is a wholly-owned insurance company subsidiary of the Company to insure the Company and its subsidiaries against certain risks unique to the operations of the Company and for which insurance may not be currently available or economically feasible in today’s insurance marketplace.

The Company’s philosophy is to grow and prosper, building long-term relationships based on top quality service, high ethical standards and safe and sound assets. The Company operates as a locally oriented, community-based financial services organization, augmented by experienced, centralized support in select critical areas. The Company’s local market orientation is reflected in its market area management and local advisory boards, which are comprised of local business persons, professionals and other community representatives that assist area management in responding to local banking needs.

The Company’s operating objectives include expansion, diversification within its markets, growth of its fee-based income and growth organically and through acquisitions of financial institutions, branches and financial services businesses. The Company seeks merger or acquisition partners that are culturally similar, have experienced management and possess either significant market area presence or have the potential for improved profitability through financial management, economies of scale and expanded services. The Company regularly evaluates merger and acquisition opportunities and conducts due diligence activities related to possible transactions with other financial institutions. As a result, merger or acquisition discussions and, in some cases, negotiations may take place and future mergers or acquisitions involving cash, debt or equity securities may occur. Acquisitions typically involve the payment of a premium over book and market values and, therefore, some dilution of the Company’s tangible book value and net income per common share may occur in any future transaction.

At December 31, 2013, the Company had consolidated assets of \$2.14 billion, consolidated deposits of \$1.74 billion, and consolidated stockholders’ equity of \$272.1 million. The Company was incorporated in Ohio in June of 1995. Its principal executive offices are located at 601 N. Clinton Street, Defiance, Ohio 43512, and its telephone number is (419) 782-5015.

On February 18, 2014, the Company announced the signing of a definitive agreement to acquire First Community Bank (FCB”). Under the merger agreement First Federal will acquire FCB in a cash transaction in which FCB will merge with and into First Federal. FCB operates four branches in the Columbus, Ohio market and at December 31, 2013, had assets of \$101.4 million, loans of \$65.4 million, deposits of \$90.5 million and common equity of \$10.6 million. Under the terms of the merger agreement, First Federal will pay \$12.9 million in cash for all outstanding shares of FCB, subject to certain adjustment factors. The transaction is expected to close by the end of the third quarter of 2014.

First Defiance’s website, www.fdef.com contains a hyperlink under the Investor Relations section to EDGAR where the annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934 are available free of charge as soon as reasonably practicable after First Defiance has filed the report with the United State Securities and Exchange Commission (“SEC”).

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The Subsidiaries

The Company's core business operations are conducted through the Subsidiaries:

First Federal Bank of the Midwest: First Federal is a federally chartered stock savings bank headquartered in Defiance, Ohio. It conducts operations through 26 full service banking center offices in Allen, Defiance, Fulton, Hancock, Henry, Lucas, Ottawa, Paulding, Putnam, Seneca, Williams and Wood counties in northwest Ohio, 1 full service banking center office in Allen County in northeast Indiana and 5 full service banking center offices in Lenawee County in southeast Michigan.

First Federal is primarily engaged in community banking. It attracts deposits from the general public through its offices and uses those and other available sources of funds to originate residential real estate loans, non-residential real estate loans, commercial loans, home improvement and home equity loans and consumer loans. In addition, First Federal invests in U.S. Treasury and federal government agency obligations, obligations of the State of Ohio and its political subdivisions, mortgage-backed securities that are issued by federal agencies, including real estate mortgage investment conduits ("REMICs") and collateralized mortgage obligations ("CMOs"), and corporate bonds. First Federal's deposits are insured by the Federal Deposit Insurance Corporation ("FDIC"). First Federal is a member of the Federal Home Loan Bank ("FHLB") System.

First Insurance Group of the Midwest: First Insurance is a wholly owned subsidiary of First Defiance. First Insurance is an insurance agency that conducts business in the Defiance, Maumee, Oregon, Bryan and Bowling Green, Ohio areas. First Insurance offers property and casualty insurance, life insurance and group health insurance. On July 1, 2011, First Insurance acquired Payak-Dubbs Insurance Agency, Inc. ("PDI") headquartered in Maumee and Oregon, Ohio. In May 2010, First Insurance acquired a group medical benefits business line from Andres O'Neil & Lowe Insurance Agency. See Note 3 Acquisitions in the Notes to the financial statements for additional information.

First Defiance Risk Management: First Defiance Risk Management was incorporated on December 20, 2012, as a wholly-owned insurance company subsidiary of the Company to insure the Company and its subsidiaries against certain risks unique to the operations of the Company and for which insurance may not be currently available or economically feasible in today's insurance marketplace. First Defiance Risk Management pools resources with several other similar insurance company subsidiaries of financial institutions to spread a limited amount of risk among themselves.

Business Strategy

First Defiance's primary objective is to be a high performing community banking organization, well regarded in its market areas. First Defiance accomplishes this through emphasis on local decision making and empowering its employees with tools and knowledge to serve its customers' needs. First Defiance believes in a "Customer First" philosophy that is strengthened by its Trusted Advisor initiative. First Defiance also has a tagline of "Better Together" as an indication of its commitment to local, responsive, personalized service. First Defiance believes this strategy results in greater customer loyalty and profitability through core relationships. First Defiance is focused on diversification of revenue sources and increased market penetration in areas where the growth potential exists for a balance between acquisition and organic growth. The primary elements of First Defiance's business strategy are commercial banking, consumer banking, including the origination and sale of single family residential loans, enhancement of fee income, wealth management and insurance sales, each united by a strong customer service culture throughout the organization.

Commercial and Commercial Real Estate Lending - Commercial and commercial real estate lending have been an ongoing focus and a major component of First Federal's success. First Federal provides primarily commercial real estate and commercial business loans with an emphasis on owner occupied commercial real estate and commercial business lending with a focus on the deposit balances that accompany these relationships. First Federal's client base tends to be small to middle market customers with annual gross revenues generally between \$1 million and \$50 million. First Federal's focus is also on securing multiple guarantors in addition to collateral where possible. These customers require First Federal to have a high degree of knowledge and understanding of their business in order to provide them with solutions to their financial needs. First Federal's Customer First philosophy and culture complements this need of its clients. First Federal believes this personal service model differentiates First Federal from its competitors, particularly the larger regional institutions. First Federal offers a wide variety of products to support commercial clients including remote deposit capture and other cash management services. First Federal also believes that the small business customer is a strong market for First Federal. First Federal participates in many of the Small Business Administration lending programs and has implemented a new program in 2014 targeting the small business customer. Maintaining a diversified portfolio with an emphasis on monitoring industry concentrations and reacting to changes in the credit characteristics of industries is an ongoing focus.

Consumer Banking - First Federal offers customers a full range of deposit and investment products including demand, checking, money market, certificates of deposits, Certificate of Deposit Account Registry Service ("CDARS") and savings accounts. First Federal offers a full range of investment products through the wealth management department and a wide variety of consumer loan products, including residential mortgage loans, home equity loans, and installment loans. First Federal also offers online banking services, which include mobile banking, online bill pay along with debit cards.

Fee Income Development - Generation of fee income and the diversification of revenue sources are accomplished through the mortgage banking operation, insurance subsidiary and the wealth management department as First Defiance seeks to reduce reliance on retail transaction fee income.

Deposit Growth - First Federal's focus has been to grow core deposits with an emphasis on total relationship banking with both our retail and commercial customers. First Federal has initiated a pricing strategy that considers the whole relationship of the customer. First Federal will continue to focus on increasing its market share in the communities it serves by providing quality products with extraordinary customer service, business development strategies and branch expansion. First Federal will look to grow its footprint in areas believed to further complement its overall market share and complement its strategy of being a high performing community bank.

Asset Quality - Maintaining a strong credit culture is of the utmost importance to First Federal. First Federal has maintained a strong credit approval and review process that has allowed the Company to maintain a credit quality standard that balances the return with the risks of industry concentrations and loan types. First Federal is primarily a collateral lender with an emphasis on cash flow performance, while obtaining additional support from personal guarantees and secondary sources of repayment. First Federal has directed its attention on loan types and markets that it knows well and in which it has historically been successful. First Federal strives to have loan relationships that are well diversified in both size and industry, and monitor the overall trends in the portfolio to maintain its industry and loan type concentration targets. First Federal maintains a problem loan remediation process that focuses on detection and resolution. First Federal maintains a strong process of internal control that subjects the loan portfolio to periodic internal reviews as well as independent third party loan review.

Expansion Opportunities - First Defiance believes it is well positioned to take advantage of acquisitions or other business opportunities in its market areas, including FDIC-assisted transactions. First Defiance believes it has a track record of successfully accomplishing both acquisitions and de novo branching in its market area. This track record puts the Company in a solid position to enter or expand its business. First Defiance has successfully integrated acquired institutions in the past with the most recent bank acquisition completed in 2008. First Defiance will continue

to be disciplined as well as opportunistic in its approach to future acquisitions and de novo branching with a focus on its primary geographic market area, which it knows well and has been competing in for a long period of time as well as surrounding market areas. First Defiance completed its acquisition of PDI on July 1, 2011, which was merged into First Insurance with offices located in Maumee and Oregon, Ohio.

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Securities

First Defiance's securities portfolio is managed in accordance with a written policy adopted by the Board of Directors and administered by the Investment Committee. The Chief Financial Officer of First Federal, Chief Executive Officer of First Federal, and the Chief Executive Officer of First Defiance can each approve transactions up to \$3 million. Two of the three officers are required to approve transactions between \$3 million and \$5 million. All transactions in excess of \$5 million must be approved by the Board of Directors.

First Defiance's investment portfolio includes 48 collateralized mortgage obligation ("CMO") issues totaling \$59.8 million, all of which are fully amortizing securities. Management does not believe the risks associated with any of its CMO investments are significantly different from risks associated with other pass-through mortgage-backed securities. First Defiance did not have any off-balance sheet derivative securities at December 31, 2013.

Management determines the appropriate classification of debt securities at the time of purchase. Debt securities are classified as held-to-maturity when First Defiance has the positive intent and ability to hold the securities to maturity. Held-to-maturity securities are stated at amortized cost. Debt securities not classified as held-to-maturity and equity securities are classified as available-for-sale. Available-for-sale securities are stated at fair value.

The carrying value of securities at December 31, 2013 by contractual maturity is shown below. Expected maturities will differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties. For purposes of the maturity table, mortgage-backed securities, which are not due at a single maturity date, have been allocated over maturity groupings based on the weighted-average contractual maturities of underlying collateral. The mortgage-backed securities may mature earlier than their weighted-average contractual maturities because of principal prepayments.

	Contractually Maturing								Total
		Weighted		Weighted		Weighted		Weighted	
	Under 1 Year (Dollars in Thousands)	Average Rate	1 - 5 Years	Average Rate	6-10 Years	Average Rate	Over 10 Years	Average Rate	Amount
Mortgage-backed securities	\$ 6,088	3.54	% \$ 17,057	3.36	% \$ 11,061	3.21	% \$ 5,362	3.03	% \$ 39,56
CMOs	9,646	3.33	27,274	3.05	16,840	2.71	5,293	2.53	59,05
U.S. government and federal agency obligations	-	-	-	-	5,000	1.80	-	-	5,000
Obligations of states and political subdivisions (1)	135	4.79	4,343	3.42	30,876	3.44	42,516	3.84	77,87
Trust preferred stock and preferred stock	-	-	-	-	17	-	3,247	2.38	3,264
Corporate bonds	2,000	1.04	3,854	0.64	3,000	1.16	-	-	8,854
Total	\$ 17,869		\$ 52,528		\$ 66,794		\$ 56,418		\$ 193,6
Unamortized premiums/ (discounts)									3,550
									1,399

Unrealized gain
on
securities
available
for sale
Total

\$ 198,5

(1) Tax exempt yield based on effective tax rate of 35%. Actual coupon rate is approximately equal to the weighted average rate disclosed in the table times 65%.

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The carrying value of investment securities is as follows:

	December 31 2013 (In Thousands)	2012	2011
Available-for-sale securities:			
Obligations of U.S. government corporations and agencies	\$ 4,921	\$ 11,069	\$ 17,085
U.S. treasury bonds	-	1,002	2,010
Obligations of state and political subdivisions	80,220	82,611	71,503
CMOs, REMICS and mortgage-backed securities	101,133	88,927	132,619
Trust preferred stock and preferred stock	2,954	1,608	1,450
Corporate bonds	8,942	8,884	8,252
Total	\$ 198,170	\$ 194,101	\$ 232,919
Held-to-maturity securities:			
Mortgage-backed securities	\$ 201	\$ 291	\$ 353
Obligations of state and political subdivisions	186	217	308
Total	\$ 387	\$ 508	\$ 661

For additional information regarding First Defiance's investment portfolio, refer to Note 5 Investment Securities to the consolidated financial statements.

Interest-Bearing Deposits

The Company had \$143.0 million and \$91.0 million in overnight investments at the Federal Reserve at December 31, 2013 and 2012, respectively, which amount is included in interest-bearing deposits. First Defiance had interest-earning deposits in the FHLB of Cincinnati and other financial institutions amounting to \$2.3 million and \$1.7 million at December 31, 2013 and 2012, respectively.

Residential Loan Servicing Activities

Servicing mortgage loans for investors involves a contractual right to receive a fee for processing and administering loan payments on mortgage loans that are not owned by the Company and are not included on the Company's balance sheet. This processing involves collecting monthly mortgage payments on behalf of investors, reporting information to those investors on a monthly basis and maintaining custodial escrow accounts for the payment of principal and interest to investors and property taxes and insurance premiums on behalf of borrowers. At December 31, 2013, First Federal serviced 14,319 loans totaling \$1.37 billion. The vast majority of the loans serviced for others are fixed rate conventional mortgage loans. The Company primarily sells its loans to Freddie Mac, Fannie Mae and FHLB. At December 31, 2013, 60.50%, 38.48% and 0.88% of the Company's sold loans were to Freddie Mac, Fannie Mae and FHLB, respectively.

As compensation for its mortgage servicing activities, the Company receives servicing fees, usually 0.25% per annum of the loan balances serviced, plus any late charges collected from delinquent borrowers and other fees incidental to the services provided. In the event of a default by the borrower, the Company receives no servicing fees until the default is cured.

The following table sets forth certain information regarding the number and aggregate principal balance of the mortgage loans serviced by the Company, including both fixed and adjustable rate loans, at various interest rates:

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Rate	December 31 2013			2012			2011		
	Number of Loans (Dollars in Thousands)	Aggregate Principal Balance	Percentage of Aggregate Principal Balance	Number of Loans	Aggregate Principal Balance	Percentage of Aggregate Principal Balance	Number of Loans	Aggregate Principal Balance	Percentage of Aggregate Principal Balance
Less than 3.00%	1,901	\$ 220,376	16.07	% 1,182	\$ 148,144	11.15	% 109	\$ 12,501	0.98
3.00% - 3.99%	4,771	544,512	39.71	3,822	454,634	34.22	1,693	208,158	16.39
4.00% - 4.99%	3,508	333,469	24.32	3,597	346,528	26.08	4,485	476,007	37.47
5.00% - 5.99%	2,537	177,999	12.98	3,218	243,077	18.29	4,457	370,355	29.15
6.00% - 6.99%	1,316	80,457	5.87	1,746	116,855	8.79	2,383	177,353	13.96
7.00% and over	286	14,428	1.05	362	19,479	1.47	449	26,013	2.05
Total	14,319	\$ 1,371,241	100.00	% 13,927	\$ 1,328,717	100.00	% 13,576	\$ 1,270,387	100.00

Loan servicing fees decrease as the principal balance on the outstanding loan decreases and as the remaining time to maturity of the loan shortens. The following table sets forth certain information regarding the remaining maturity of the mortgage loans serviced by the Company as of the dates shown.

Maturity	December 31 2013				2012				2011		
	Number of Loans (Dollars in Thousands)	% of Number of Loans	Unpaid Principal Amount	% of Unpaid Principal Amount	Number of Loans	% of Number of Loans	Unpaid Principal Amount	% of Unpaid Principal Amount	Number of Loans	% of Number of Loans	Unpaid Principal Amount
1 - 5 years	846	5.91	% \$ 19,593	1.43	% 507	3.64	% \$ 10,537	0.79	% 375	2.7	% 1,000
6 - 10 years	1,009	7.05	52,404	3.82	4,030	28.94	395,066	29.73	1,677	12.3	1,000
11 - 15 years	4,340	30.31	420,362	30.66	1,391	9.99	134,916	10.16	3,326	24.4	1,000
16 - 20 years	1,704	11.90	158,467	11.56	1,846	13.25	163,929	12.34	1,026	7.5	1,000
21 - 25 years	1,218	8.51	102,844	7.50	1,370	9.84	60,618	4.56	2,347	17.3	1,000
More than 25 years	5,202	36.32	617,571	45.03	4,783	34.34	563,651	42.42	4,825	35.5	1,000
Total	14,319	100.00	% \$ 1,371,241	100.00	% 13,927	100.00	% \$ 1,328,717	100.00	% 13,576	100.00	% 1,328,717

Lending Activities

General A savings bank generally may not make loans to one borrower and related entities in an amount which exceeds 15% of its unimpaired capital and surplus, although loans in an amount equal to an additional 10% of unimpaired capital and surplus may be made to a borrower if the loans are fully secured by readily marketable collateral. Real estate is not considered “readily marketable collateral.” Certain types of loans are not subject to these limits. In applying these limits, loans to certain borrowers may be aggregated. Notwithstanding the specified limits, a savings bank may lend to one borrower up to \$500,000 “for any purpose.” At December 31, 2013, First Federal’s limit on loans-to-one borrower was \$39.1 million and its five largest loans (including available lines of credit) or groups of loans to one borrower, including related entities, were \$33.4 million, \$30.4 million, \$29.2 million, \$27.0 million and \$23.3 million. All of these loans or groups of loans were performing in accordance with their terms at December 31, 2013.

Loan Portfolio Composition The net increase or (decrease) in net loans receivable over the prior year was \$57.0 million, \$44.7 million and (\$24.6 million) at December 31, 2013, 2012, and 2011, respectively. The loan portfolio contains no foreign loans. The Company’s loan portfolio is concentrated geographically in its northwest Ohio, northeast Indiana and southeast Michigan market areas. Management has identified lending for income generating rental properties as an industry concentration. Total loans for income generating property totaled \$408.4 million at December 31, 2013, which represents 25.3% of the Company’s loan portfolio.

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The following table sets forth the composition of the Company's loan portfolio by type of loan at the dates indicated.

	December 31 2013		2012		2011		2010		2009	
	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%
	(Dollars in Thousands)									
Real estate:										
Single family residential	\$ 195,752	12.2	% \$ 200,826	13.0	% \$ 203,401	13.6	% \$ 205,938	13.5	% \$ 227,592	
Five or more family residential	148,952	9.2	122,275	7.9	126,246	8.4	120,534	7.9	103,169	
Nonresidential real estate	670,666	41.6	675,110	43.7	649,746	43.3	646,478	42.2	703,721	
Construction	86,058	5.3	37,788	2.5	31,552	2.1	30,340	2.0	48,625	
Total real estate loans	1,101,428	68.3	1,035,999	67.1	1,010,945	67.4	1,003,290	65.6	1,083,107	
Other:										
Consumer finance	16,902	1.0	15,936	1.0	18,887	1.3	22,848	1.5	34,105	
Commercial	388,236	24.1	383,817	24.9	349,053	23.2	369,959	24.2	379,408	
Home equity and improvement	106,930	6.6	108,718	7.0	122,143	8.1	133,593	8.7	147,977	
Total non-real estate loans	512,068	31.7	508,471	32.9	490,083	32.6	526,400	34.4	561,490	
Total loans	1,613,496	100.0	% 1,544,470	100.0	% 1,501,028	100.0	% 1,529,690	100.0	% 1,644,597	
Less:										
Loans in process	32,290		18,478		13,243		9,267		26,494	
Deferred loan origination fees	758		735		709		920		981	
Allowance for loan losses	24,950		26,711		33,254		41,080		36,547	
Net loans	\$ 1,555,498		\$ 1,498,546		\$ 1,453,822		\$ 1,478,423		\$ 1,580,575	

In addition to the loans reported above, First Defiance had \$9.1 million, \$22.1 million, \$13.8 million, \$18.1 million, and \$10.3 million in loans classified as held for sale at December 31, 2013, 2012, 2011, 2010 and 2009, respectively. The fair value of such loans, which are all single-family residential mortgage loans, approximated their carrying value for all years presented.

Contractual Principal, Repayments and Interest Rates The following table sets forth certain information at December 31, 2013 regarding the dollar amount of gross loans maturing in First Defiance's portfolio, based on the contractual terms to maturity. Demand loans, loans having no stated schedule of repayments and no stated maturity, and overdrafts are reported as due in one year or less.

Years After December 31, 2013
Due Less

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	than 1 (In Thousands)	Due 1-2	Due 3-5	Due 5-10	Due 10-15	Due 15+	Total
Real estate	\$ 274,718	\$ 124,116	\$ 525,816	\$ 95,005	\$ 27,520	\$ 54,253	\$ 1,101,428
Non-real estate:							
Commercial	253,764	48,475	81,270	4,727	-	-	388,236
Home equity and improvement	70,633	8,930	22,389	3,887	382	709	106,930
Consumer finance	7,201	4,274	5,237	167	23	-	16,902
Total	\$ 606,316	\$ 185,795	\$ 634,712	\$ 103,786	\$ 27,925	\$ 54,962	\$ 1,613,496

The schedule above does not reflect the actual life of the Company's loan portfolio. The average life of loans is substantially less than their contractual terms because of prepayments and due-on-sale clauses, which give First Defiance the right to declare a conventional loan immediately due and payable in the event, among other things, that the borrower sells the real property subject to the mortgage and the loan is not repaid.

The following table sets forth the dollar amount of gross loans due after one year from December 31, 2013 which have fixed interest rates or which have floating or adjustable interest rates.

	Fixed Rates (In Thousands)	Floating or Adjustable Rates	Total
Real estate	\$ 302,710	\$ 524,000	\$ 826,710
Commercial	120,499	13,973	134,472
Other	45,137	861	45,998
	\$ 468,346	\$ 538,834	\$ 1,007,180

Originations, Purchases and Sales of Loans The lending activities of First Federal are subject to the written, non-discriminatory, underwriting standards and loan origination procedures established by the Board of Directors and management. Loan originations are obtained from a variety of sources, including referrals from existing customers, real estate brokers, developers and builders, newspaper and radio advertising and walk-in customers.

First Federal's loan approval process for all types of loans is intended to assess the borrower's ability to repay the loan, the viability of the loan and the adequacy of the value of the collateral that will secure the loan.

A commercial loan application is first reviewed and underwritten by one of the commercial loan officers, who may approve credits within their lending limit. Another loan officer with limits sufficient to cover the exposure must approve credits exceeding an individual's lending limit. All credits which exceed \$100,000 in aggregate exposure must be presented for review or approval to the Senior Loan Committee comprised of senior lending personnel. Credits which exceed \$2,000,000 in aggregate exposure must be presented for approval to the Executive Loan Committee.

Residential mortgage applications are accepted by retail lenders or branch managers, who utilize an automated underwriting system to review the loan request. First Federal also receives mortgage applications via an online residential mortgage origination system. A final approval of all residential mortgage applications is made by a member of a centralized underwriting staff within their designated lending limits. Loan requests in excess or outside an individual underwriter's limit are approved by the Senior Loan Committee and, if necessary, by the Executive Loan Committee.

Retail lenders and branch managers are authorized to originate and approve direct consumer loan requests that are within policy guidelines and within the lender's approved lending limit. Loans in excess of the lender's approved lending limit may be approved by retail lending managers up to their approved lending limit. Loans in excess of the retail lending manager's authorized lending limit or outside of policy must be approved by Senior Loan Committee and, if necessary, by the Executive Loan Committee. Indirect consumer loans originated by auto dealers are underwritten and approved by a designated underwriter in accordance with company policy and lending limits.

First Defiance offers adjustable-rate loans in order to decrease the vulnerability of its operations to changes in interest rates. The demand for adjustable-rate loans in First Defiance's primary market area has been a function of several factors, including customer preference, the level of interest rates, the expectations of changes in the level of interest rates and the difference between the interest rates offered for fixed-rate loans and adjustable-rate loans. The relative amount of fixed-rate and adjustable-rate residential loans that can be originated at any time is largely determined by the demand for each in a competitive environment.

Adjustable-rate loans represented 9.2% of First Defiance's total originations of one-to-four family residential mortgage loans in 2013 compared to 7.1% and 5.4% during 2012 and 2011, respectively.

Adjustable-rate loans decrease the risks associated with changes in interest rates, but involve other risks, primarily because as interest rates rise, the payment by the borrower rises to the extent permitted by the terms of the loan, thereby increasing the potential for default. At the same time, the marketability of the underlying property may be adversely affected by higher interest rates.

The following table shows total loans originated, loan reductions, and the net increase in First Defiance's total loans and loans held for sale during the periods indicated:

	Years Ended December 31		
	2013	2012	2011
	(In Thousands)		
Loan originations:			
Single family residential	\$ 326,700	\$ 546,773	\$ 282,321
Multi-family residential	50,874	28,521	11,401
Non-residential real estate	113,999	191,742	125,884
Construction	67,530	33,557	29,189
Commercial	435,248	603,415	186,338
Home equity and improvement	41,552	32,684	19,063
Consumer finance	10,043	9,722	10,216
Total loans originated	1,045,946	1,446,414	664,412
Loans purchased:	4,545	-	25,842
Loan reductions:			
Loan pay-offs	205,254	299,479	227,812
Loans sold	315,812	514,351	266,580
Periodic principal repayments	473,343	580,919	228,810
	994,409	1,394,749	723,202
Net (decrease) increase in total loans and loans held for sale	\$ 56,082	\$ 51,665	\$ (32,948)

Asset Quality

First Defiance's credit policy establishes guidelines to manage credit risk and asset quality. These guidelines include loan review and early identification of problem loans to ensure sound credit decisions. First Defiance's credit policies and review procedures are meant to minimize the risk and uncertainties inherent in lending. In following the policies and procedures, management must rely on estimates, appraisals and evaluations of loans and the possibility that changes in these could occur because of changing economic conditions.

Delinquent Loans The following table sets forth information concerning delinquent loans at December 31, 2013, in dollar amount and as a percentage of First Defiance's total loan portfolio. The amounts presented represent the total outstanding principal balances of the related loans, rather than the actual payment amounts that are past due.

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	30 to 59 Days		60 to 89 Days		90 Days and Over		Total	
	Amount	Percentage	Amount	Percentage	Amount	Percentage	Amount	Percentage
(Dollars in Thousands)								
One to four family residential real estate Nonresidential and Multi-family residential Commercial Construction Home Equity and Improvement Consumer Finance Total	\$ 2,045	0.12	% \$ 594	0.04	% \$ 1,394	0.09	% \$ 4,033	0.25 %
	1,420	0.09	1,410	0.09	5,936	0.36	8,766	0.54
	37	0.00	26	0.00	3,984	0.25	4,047	0.25
	-	0.00	-	0.00	-	0.00	-	0.00
	1,153	0.07	153	0.01	413	0.03	1,719	0.11
	131	0.01	-	0.00	-	0.00	131	0.01
	\$ 4,786	0.29	% \$ 2,183	0.14	% \$ 11,727	0.73	% \$ 18,696	1.16 %

Overall, the level of delinquencies at December 31, 2013 has decreased from the levels at December 31, 2012, when First Defiance reported that 1.56% of its outstanding loans were at least 30 days delinquent. The level of total loans 90 or more days delinquent has decreased to 0.73% at December 31, 2013 from 0.84% at December 31, 2012. The level of total loans 60-89 days delinquent decreased to 0.14% at December 31, 2013 from 0.32% at December 31, 2012. Overall, the level of loans that were 30 to 59 days past due decreased from 0.40% at December 31, 2012 to 0.29% at December 31, 2013. Management has assessed the collectability of all loans that are 90 days or more delinquent as part of its procedures in establishing the allowance for loan losses.

Nonperforming Assets All loans are reviewed on a regular basis and are placed on non-accrual status when, in the opinion of management, the collectability of additional interest is not expected. Generally, First Defiance places all loans more than 90 days past due on non-accrual status. First Defiance also places loans on non-accrual when the loan is paying as agreed but the Company believes the financial condition of the borrower is such that this classification is warranted. When a loan is placed on non-accrual status, total unpaid interest accrued to date is reversed. Subsequent payments are generally applied to the outstanding principal balance but may be recorded as interest income, depending on the assessment of the ultimate collectability of the loan. First Defiance considers that a loan is impaired when, based on current information and events, it is probable that it will be unable to collect all amounts due (both principal and interest) according to the contractual terms of the loan agreement. First Defiance measures impairment based on the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's observable market price, or the fair value of the collateral, if collateral dependent. If the estimated recoverability of the impaired loan is less than the recorded investment, First Defiance will recognize impairment by allocating a portion of the allowance for loan losses on cash flow dependent loans and by charging off the deficiency on collateral dependent loans.

Loans originated by First Federal having principal balances of \$57.3 million, \$71.1 million and \$47.9 million were considered impaired as of December 31, 2013, 2012 and 2011, respectively. The decrease in impaired loans from 2012 to 2013 is mainly due to a concerted effort by management and the lending staff to work specific credits out of the bank or back to performing status. These amounts of impaired loans exclude large groups of small-balance homogeneous loans that are collectively evaluated for impairment such as residential mortgage, consumer installment and credit card loans. There was \$2.1 million of interest received and recorded in income during 2013 related to

impaired loans. There was \$1.3 million and \$1.6 million recorded in 2012 and 2011, respectively. Unrecorded interest income based on the loan's contractual terms on these impaired loans and all non-performing loans in 2013, 2012 and 2011 was \$1.1 million, \$2.5 million, and \$2.3 million, respectively. The average recorded investment in impaired loans during 2013, 2012 and 2011 (excluding loans accounted for under FASB ASC Topic 310 Subtopic 30) was \$64.7 million, \$53.3 million and \$61.0 million, respectively. The total allowance for loan losses related to these loans was \$1.4 million, \$1.5 million, and \$7.2 million at December 31, 2013, 2012 and 2011, respectively.

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Real estate acquired by foreclosure is classified as real estate owned until such time as it is sold. First Defiance also repossesses other assets securing loans, consisting primarily of automobiles. When such property is acquired it is recorded at fair value less cost to sell. Costs relating to development and improvement of property are capitalized, whereas costs relating to holding the property are expensed. Valuations are periodically performed by management and a write-down of the value is recorded with a corresponding charge to operations if it is determined that the carrying value of property exceeds its estimated net realizable value. During 2013, First Defiance recognized \$740,000 of expense related to write-downs in value of real estate acquired by foreclosure. The balance of real estate owned at December 31, 2013 was \$5.9 million.

As of December 31, 2013, First Defiance's total non-performing loans amounted to \$27.8 million or 1.76% of total loans (net of undisbursed loan funds and deferred fees and costs), compared to \$32.6 million or 2.14% of total loans, at December 31, 2012. Non-performing loans are loans which are more than 90 days past due or on nonaccrual. The nonperforming loan balance includes \$23.8 million of loans originated by First Federal also considered impaired or acquired loans accounted for under Topic 310 Subtopic 30.

The following table sets forth the amounts and categories of First Defiance's non-performing assets (excluding impaired loans not considered non-performing) and troubled debt restructurings at the dates indicated.

	December 31									
	2013	2012	2011	2010	2009					
	(Dollars in Thousands)									
Nonperforming loans:										
One to four family residential real estate	\$ 3,273	\$ 3,602	\$ 3,890	\$ 7,232	\$ 5,349					
Nonresidential and multi-family residential real estate	15,834	23,090	28,150	21,737	24,042					
Commercial	8,327	5,661	6,884	11,547	10,615					
Construction	-	-	-	64	675					
Home Equity and Improvement	413	217	394	446	451					
Consumer finance	-	-	10	14	59					
Total nonperforming loans	27,847	32,570	39,328	41,040	41,191					
Real estate owned	5,859	3,805	3,608	9,591	13,413					
Other repossessed assets	-	-	20	-	114					
Total repossessed assets	5,859	3,805	3,628	9,591	13,527					
Total nonperforming assets	\$ 33,706	\$ 36,375	\$ 42,956	\$ 50,631	\$ 54,718					
Restructured loans, accruing	\$ 27,630	\$ 28,203	\$ 3,380	\$ 6,001	\$ 6,715					
Total nonperforming assets as a percentage of total assets	1.58	%	1.78	%	2.08	%	2.49	%	2.66	%

Total nonperforming loans as a percentage of total loans*	1.76	%	2.14	%	2.64	%	2.70	%	2.55	%
Total nonperforming assets as a percentage of total loans plus REO*	2.12	%	2.38	%	2.88	%	3.70	%	3.77	%
Allowance for loan losses as a percent of total nonperforming assets	74.02	%	73.43	%	77.41	%	81.14	%	66.79	%

* Total loans are net of undisbursed loan funds and deferred fees and costs.

Allowance for Loan Losses First Defiance maintains an allowance for loan losses to absorb probable incurred credit losses in the loan portfolio. The allowance for loan loss is made up of two components. The first is a general reserve, which is used to record loan loss reserves for groups of homogenous loans in which the Company estimates the losses incurred in the portfolio based on quantitative and qualitative factors. Quantitative factors are primarily the historical loss experience of the portfolio for the most recent three years. Qualitative factors that may lead the Company to add additional general reserves on the non-impaired loan portfolio include such things as: changes in international, national and local economic business conditions, changes in the value of underlying collateral for collateral dependent loans, changes in the political and regulatory environment and changes in the trends of the loan portfolio.

The second component of the allowance for loan loss is the specific reserve in which the Company sets aside reserves based on the analysis of individual credits. In evaluating the adequacy of its allowance each quarter, management grades all loans in the commercial portfolio. In establishing specific reserves, the Company analyzes all substandard, doubtful and loss graded loans quarterly and makes judgments about the risk of loss based on the cash flow of the borrower, the value of any collateral and the financial strength of any guarantors. If the loan is cash flow dependent, then a specific reserve is established for the discount on the net present value of expected future cash flows. If the loan is collateral dependent, then any shortfall is usually charged off. The Company also considers the impacts of any Small Business Association or Farm Service Agency guarantees. An internal loan review of all loan relationships between \$250,000 and \$1,000,000 is performed annually. Management also engages a third-party to do an annual review of all loan relationships in excess of \$1,000,000. Both of these loan reviews, among other things, independently assess management's loan grades.

Loans charged-off are charged against the allowance when such loans meet the Company's established policy on loan charge-offs and the allowance itself is adjusted quarterly by recording a provision for loan losses. As such, actual losses and losses provided for should be approximately the same if the overall quality, composition and size of the portfolio remained static. To the extent that the portfolio grows at a rapid rate or overall quality deteriorates, the provision generally will exceed charge-offs, as in 2009 and 2010. However, in certain circumstances, as in 2011 through 2013, net charge-offs may exceed the provision for loan losses when management determines that loans previously provided for in the allowance for loan losses are uncollectible and should be charged off or as overall credit improves. Although management believes that it uses the best information available to make such determinations, future adjustments to the allowances may be necessary, and net earnings could be significantly affected, if circumstances differ substantially from the assumptions used in making the initial determinations.

At December 31, 2013, First Defiance's allowance for loan losses amounted to \$25.0 million compared to \$26.7 million at December 31, 2012. The following table sets forth the activity in First Defiance's allowance for loan losses during the periods indicated.

	Years Ended December 31				
	2013	2012	2011	2010	2009
	(Dollars in Thousands)				
Allowance at beginning of year	\$ 26,711	\$ 33,254	\$ 41,080	\$ 36,547	\$ 24,592
Provision for credit losses	1,824	10,924	12,434	23,177	23,232
Allowance acquired in acquisitions	-	-	-	-	-
Charge-offs:					
Single family residential real estate	(643)	(2,515)	(2,753)	(3,092)	(2,281)
Commercial real estate and multi-family	(2,475)	(11,319)	(13,150)	(9,928)	(5,799)
Commercial	(1,230)	(4,047)	(4,398)	(5,118)	(2,664)
Consumer finance	(94)	(133)	(95)	(124)	(320)
Home equity and improvement	(757)	(1,165)	(1,052)	(1,066)	(762)
Total charge-offs	(5,199)	(19,179)	(21,448)	(19,328)	(11,826)
Recoveries	1,614	1,712	1,188	684	549
Net charge-offs	(3,585)	(17,467)	(20,260)	(18,644)	(11,277)
Ending allowance	\$ 24,950	\$ 26,711	\$ 33,254	\$ 41,080	\$ 36,547
Allowance for loan losses to total non-performing loans at end of year	89.60 %	82.01 %	84.56 %	100.10 %	88.73 %
Allowance for loan losses to total loans at end of year*	1.58 %	1.75 %	2.24 %	2.70 %	2.26 %
Allowance for loan losses to net charge-offs for the year	695.96 %	152.92 %	164.14 %	220.34 %	324.08 %
Net charge-offs for the year to average loans	0.23 %	1.18 %	1.41 %	1.21 %	0.70 %

* Total loans are net of undisbursed loan funds and deferred fees and costs.

The provision for credit losses has decreased in 2013 and 2012 from previous years due to improved credit quality of the loan portfolio. Charge-offs trended downward in 2013. Management anticipates a stable to lower level of net charge-offs in 2014 compared to 2013 and feels that the level of the allowance for loan losses at December 31, 2013 is sufficient to cover the estimated losses incurred but not yet recognized in the loan portfolio.

The following table sets forth information concerning the allocation of First Defiance's allowance for loan losses by loan categories at the dates indicated. For information about the percent of total loans in each category to total loans, see "Lending Activities-Loan Portfolio Composition."

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	December 31 2013		2012		2011		2010		2009	
	Amount	Percent of total loans by category	Amount	Percent of total loans by category	Amount	Percent of total loans by category	Amount	Percent of total loans by category	Amount	Percent of total loans by category
	(Dollars in Thousands)									
Single family residential and construction	\$ 2,981	17.5	% \$ 3,581	15.5	% \$ 4,158	15.7	% \$ 6,029	15.5	% \$ 6,029	15.5
Nonresidential and Multi-family residential	14,508	50.8	14,899	51.6	20,490	51.7	22,355	50.1	22,355	50.1
real estate Other:										
Commercial loans	5,678	24.1	6,325	24.9	6,576	23.2	10,871	24.2	10,871	24.2
Consumer and home equity and improvement loans	1,783	7.6	1,906	8.0	2,030	9.4	1,825	10.2	1,825	10.2
	\$ 24,950	100.0	% \$ 26,711	100.0	% \$ 33,254	100.0	% \$ 41,080	100.0	% \$ 41,080	100.0

Sources of Funds

General Deposits are the primary source of First Defiance's funds for lending and other investment purposes. In addition to deposits, First Defiance derives funds from loan principal repayments. Loan repayments are a relatively stable source of funds, while deposit inflows and outflows are significantly influenced by general interest rates and money market conditions. Borrowings from the FHLB may be used on a short-term basis to compensate for reductions in the availability of funds from other sources. They may also be used on a longer-term basis for general business purposes. During 2007, First Defiance issued \$15.0 million of trust preferred securities through an unconsolidated affiliated trust. Proceeds from the offering were used for general corporate purposes including funding of dividends and stock buybacks as well as bolstering regulatory capital at the First Federal level. First Defiance also issued \$20.0 million of similar trust preferred securities in 2005.

Deposits First Defiance's deposits are attracted principally from within First Defiance's primary market area through the offering of a broad selection of deposit instruments, including checking accounts, money market accounts, savings accounts, and term certificate accounts. Deposit account terms vary, with the principal differences being the minimum balance required, the time periods the funds must remain on deposit, and the interest rate.

To supplement its funding needs, First Defiance also utilizes the national market for Certificates of Deposit. Such deposits have maturities ranging from one to thirty-five months. These deposits are issued at the current rates available to customers in our market areas. The total balance of national certificates of deposit was \$0 and \$2.0 million at December 31, 2013 and 2012, respectively.

Average balances and average rates paid on deposits are as follows:

	Years Ended December 31								
	2013			2012			2011		
	Amount	Rate		Amount	Rate		Amount	Rate	
	(Dollars in Thousands)								
Non-interest-bearing demand deposits	\$ 308,591	-		\$ 266,913	-		\$ 231,343	-	
Interest bearing demand deposits	677,903	0.17	%	629,568	0.20	%	592,093	0.36	%
Savings deposits	179,041	0.05		164,508	0.07		153,318	0.16	
Time deposits	496,360	0.95		558,648	1.21		613,374	1.60	
Totals	\$ 1,661,895	0.36	%	\$ 1,619,637	0.50	%	\$ 1,590,128	0.77	%

The following table sets forth the maturities of First Defiance's retail certificates of deposit having principal amounts greater than \$100,000 at December 31, 2013 (in thousands):

Retail certificates of deposit maturing in quarter ending:

March 31, 2014	\$ 28,608
June 30, 2014	28,862
September 30, 2014	30,192
December 31, 2014	15,194
After December 31, 2014	69,598
Total retail certificates of deposit with balances greater than \$100,000	\$ 172,454

At December 31, 2013, the Company had total deposits having principal amounts greater than \$250,000 of \$393.0 million.

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The following table details the deposit accrued interest payable as of December 31:

	2013 (In Thousands)	2012
Interest bearing demand deposits and money market accounts	\$ 14	\$ 13
Certificates of deposit	34	58
	\$ 48	\$ 71

For additional information regarding First Defiance's deposits see Note 11 to the financial statements.

Borrowings First Defiance may obtain advances from the FHLB of Cincinnati by pledging certain of its residential mortgage loans, non-residential loans, multi-family loans, home equity loans and investment securities provided certain standards related to creditworthiness have been met. Such advances are made pursuant to several credit programs, each of which has its own interest rate and range of maturities.

The following table sets forth certain information as to First Defiance's FHLB advances and other borrowings at the dates indicated.

	December 31		2012		2011	
	2013					
	(Dollars in Thousands)					
Long-term:						
FHLB advances	\$ 22,520		\$ 12,796		\$ 81,841	
Weighted average interest rate	2.36	%	2.80	%	3.66	%
Short-term:						
Securities sold under agreement to repurchase	\$ 51,919		\$ 51,702		\$ 60,386	
Weighted average interest rate	0.31	%	0.63	%	0.92	%

The following table sets forth the maximum month-end balance and average balance of First Defiance's long-term FHLB advances and other borrowings during the periods indicated.

	Years Ended December 31		2012		2011	
	2013					
	(Dollars in Thousands)					
Long-term:						
FHLB advances:						
Maximum balance	\$ 22,765		\$ 81,838		\$ 116,882	
Average balance	16,569		66,121		93,652	
Weighted average interest rate	2.62	%	3.67	%	3.43	%

The following table sets forth the maximum month-end balance and average balance of First Defiance's short-term FHLB advances and other borrowings during the periods indicated.

	Years Ended December 31						
	2013		2012		2011		
	(Dollars in Thousands)						
Short-term:							
FHLB advances:							
Maximum balance	\$	50,000	\$	-	\$	-	
Average balance		1,164		-		16	
Weighted average interest rate		0.09	%	-		0.17	%
Securities sold under agreement to repurchase:							
Maximum balance	\$	57,182	\$	57,050	\$	61,240	
Average balance		50,877		53,171		56,495	
Weighted average interest rate		0.44	%	0.70	%	0.94	%

First Defiance borrows funds under a variety of programs at the FHLB. As of December 31, 2013, there was \$22.5 million outstanding under various long-term FHLB advance programs. First Defiance utilizes short-term advances from the FHLB to meet cash flow needs and for short-term investment purposes. At December 31, 2013 and December 31, 2012, no outstanding balances existed under First Defiance's Cash Management Advance Line of Credit. The total available under this line is \$15.0 million. Additionally, First Defiance has \$100.0 million available under a REPO line of credit. Amounts are generally borrowed under these lines on an overnight basis. First Federal's total borrowing capacity at the FHLB is limited by various collateral requirements. Eligible collateral includes mortgage loans, home equity loans, non-mortgage loans, cash, and investment securities. At December 31, 2013, other than amounts available on the REPO and Cash Management line, First Federal had additional borrowing capacity with the FHLB of \$428.7 million as a result of these collateral requirements.

As a member of the FHLB of Cincinnati, First Federal must maintain a minimum investment in the capital stock of that FHLB in an amount defined in the FHLB's regulations. First Federal is permitted to own stock in excess of the minimum requirement and is in compliance with the minimum requirement with an investment in stock of the FHLB of Cincinnati of \$19.3 million at December 31, 2013. First Federal also acquired \$2.0 million in stock of the FHLB of Indianapolis from the Pavilion acquisition, which had a balance of \$1.3 million at December 31, 2012. The balance of this stock was \$10,000 at December 31, 2013.

Each FHLB is required to establish standards of community investment or service that its members must maintain for continued access to long-term advances from the FHLB. The standards take into account a member's performance under the Community Reinvestment Act and its record of lending to first-time homebuyers.

For additional information regarding First Defiance's FHLB advances and other debt see Notes 12 and 14 to the financial statements.

Subordinated Debentures - In March 2007, the Company sponsored an affiliated trust, First Defiance Statutory Trust II ("Trust Affiliate II") that issued \$15 million of Guaranteed Capital Trust Securities (Trust Preferred Securities). In connection with the transaction, the Company issued \$15.5 million of Junior Subordinated Deferrable Interest Debentures (Subordinated Debentures) to Trust Affiliate II. Trust Affiliate II was formed for the purpose of issuing Trust Preferred Securities to third-party investors and investing the proceeds from the sale of these capital securities solely in Subordinated Debentures of the Company. The Subordinated Debentures held by Trust Affiliate II are the sole assets of the trust. Distributions on the Trust Preferred Securities issued by Trust Affiliate II are payable quarterly at a variable rate equal to the three-month LIBOR rate plus 1.5%. The Coupon rate payable on the Trust

Preferred Securities issued by Trust Affiliate II was 1.75% and 1.89% as of December 31, 2013 and 2012 respectively.

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The Trust Preferred Securities are subject to mandatory redemption, in whole or in part, upon repayment of the Subordinated Debentures. The Company has entered into an agreement that fully and unconditionally guarantees the Trust Preferred Securities subject to the terms of the guarantee. The Trust Preferred Securities and Subordinated Debentures mature on June 15, 2037, but could have been redeemed at the Company's option at any time on or after June 15, 2012, or at any time upon certain events.

In October 2005, the Company formed an affiliated trust, First Defiance Statutory Trust I ("Trust Affiliate I") that issued \$20 million of Trust Preferred Securities. In connection with the transaction, the Company issued \$20.6 million of Subordinated Debentures to Trust Affiliate I. Trust Affiliate I was formed for the purpose of issuing Trust Preferred Securities to third-party investors and investing the proceeds from the sale of these capital securities solely in Subordinated Debentures of the Company. The Subordinated Debentures held by Trust Affiliate I are the sole assets of the trust. Distributions on the Trust Preferred Securities issued by Trust Affiliate I are payable quarterly at a variable rate equal to the three-month LIBOR rate plus 1.38%, or 1.63% and 1.77% as of December 31, 2013 and 2012 respectively.

The Trust Preferred Securities issued by Trust Affiliate I are subject to mandatory redemption, in whole or in part, upon repayment of the Subordinated Debentures. The Company has entered into an agreement that fully and unconditionally guarantees the Trust Preferred Securities subject to the terms of the guarantee. The Trust Preferred Securities and Subordinated Debentures could have been redeemed by the issuer at par after October 28, 2010. The Subordinated Debentures mature on December 15, 2035.

Repurchase of Preferred Shares related to the Capital Purchase Program

In June 2012, the U.S. Treasury sold its preferred shares of the Company through a public offering structured as a modified Dutch auction. The Company bid on its preferred shares in the auction after receiving approval from its regulators. The clearing price per preferred share was \$962.66 (compared to a par value of \$1,000.00 per share) and the Company was successful in repurchasing 16,560 of the 37,000 preferred shares outstanding through the auction process. The Company also acquired an additional 19,440 preferred shares in the secondary market prior to the end of the second quarter of 2012. The remaining 1,000 outstanding preferred shares were purchased at par value on July 18, 2012. The clearing prices per preferred share purchased in the secondary market were as follows: 1,100 shares at \$997.50, 2,500 shares at \$1,000.00 and 16,840 shares at \$998.75.

The net balance sheet impact of the repurchase was a reduction to stockholders' equity of \$36.4 million which is comprised of a decrease in preferred shares of \$37.0 million and a \$642,000 increase to retained earnings related to the discount on the shares repurchased, which is also included in net income applicable to common shares for purposes of calculating earnings per share.

Included in the 2012 operating results is \$181,000 of costs incurred by the Company related to the U.S. Treasury's offering. These costs were not tax-deductible.

Balance Sheet Restructure

In the fourth quarter of 2012, the Company executed a balance sheet restructuring strategy to enhance the Company's current and future profitability while increasing its capital ratios and protecting the balance sheet against rising rates. The strategy required taking an after tax loss of approximately \$260,000 by selling \$60 million in securities for a gain of \$1.6 million and paying off \$62.0 million in FHLB advances with a prepayment penalty of \$2.0 million.

Employees

First Defiance had 549 employees at December 31, 2013. None of these employees are represented by a collective bargaining agent, and First Defiance believes that it maintains good relationships with its personnel.

Competition

Competition in originating non-residential mortgage and commercial loans comes mainly from commercial banks with banking center offices in the Company's market area. Competition for the origination of mortgage loans arises mainly from savings associations, commercial banks, and mortgage companies. The distinction among market participants is based on a combination of price, the quality of customer service and name recognition. The Company competes for loans by offering competitive interest rates and product types and by seeking to provide a higher level of personal service to borrowers than is furnished by competitors. First Federal has a significant market share of the lending markets in which it conducts operations.

Management believes that First Federal's most direct competition for deposits comes from local financial institutions. The distinction among market participants is based on price and the quality of customer service and name recognition. First Federal's cost of funds fluctuates with general market interest rates. During certain interest rate environments, additional significant competition for deposits may be expected from corporate and governmental debt securities, as well as from money market mutual funds. First Federal competes for conventional deposits by emphasizing quality of service, extensive product lines and competitive pricing.

Regulation

General First Defiance and First Federal are subject to regulation, examination and oversight by the Office of the Comptroller of the Currency ("OCC") and the Federal Reserve Board ("Federal Reserve"). Because the FDIC insures First Federal's deposits, First Federal is also subject to examination and regulation by the FDIC. First Defiance and First Federal must file periodic reports with the Federal Reserve and the OCC and examinations are conducted periodically by the Federal Reserve, OCC and the FDIC to determine whether First Defiance and First Federal are in compliance with various regulatory requirements and are operating in a safe and sound manner. First Federal is subject to various consumer protection and fair lending laws. These laws govern, among other things, truth-in-lending disclosure, equal credit opportunity, and, in the case of First Federal, fair credit reporting and community reinvestment. Failure to abide by federal laws and regulations governing community reinvestment could limit the ability of First Federal to open a new branch or engage in a merger transaction. Community reinvestment regulations evaluate how well and to what extent First Federal lends and invests in its designated service area, with particular emphasis on low-to-moderate income communities and borrowers in such areas.

First Defiance is also subject to various Ohio laws which restrict takeover bids, tender offers and control-share acquisitions involving public companies which have significant ties to Ohio.

Regulatory Capital Requirements First Federal is required by regulations to meet certain minimum capital requirements. Current capital requirements call for core capital of 4.0% of adjusted total assets, except for associations with the highest examination rating and acceptable levels of risk, and risk-based capital of 8.0% of risk-weighted assets.

The following table sets forth the amount and percentage level of regulatory capital of First Federal at December 31, 2013, and the amount by which it exceeds the minimum capital requirements. Tier 1 capital is reflected as a percentage of adjusted total assets. Tier 1 capital to risk-weighted assets and total (or risk-based) capital, which consists of core and supplementary capital, is reflected as a percentage of risk-weighted assets. Assets, excluding the collateralized debt obligation securities, are weighted at percentage levels ranging from 0% to 100% depending on their relative risk. The collateralized debt obligations securities are subject to the dollar-for-dollar capital requirement.

	Actual Amount	Ratio		Minimum Required for Adequately Capitalized Amount	Ratio		Minimum Required for Well Capitalized Amount	Ratio	
Tier 1 Capital (1)									
Consolidated	\$ 246,258	11.86	%	\$ 83,045	4.0	%	N/A	N/A	
First Federal	\$ 235,699	11.36	%	\$ 82,978	4.0	%	\$ 103,722	5.0	%
Tier 1 Capital (to Risk Weighted Assets) (1)									
Consolidated	\$ 246,258	13.98	%	\$ 70,473	4.0	%	N/A	N/A	
First Federal	\$ 235,699	13.39	%	\$ 70,418	4.0	%	\$ 105,627	6.0	%
Total Capital (to Risk Weighted Assets) (1)									
Consolidated	\$ 268,317	15.23	%	\$ 140,947	8.0	%	N/A	N/A	
First Federal	\$ 257,741	14.64	%	\$ 140,836	8.0	%	\$ 176,046	10.0	%

Core capital is computed as a percentage of adjusted total assets of \$2.08 billion and \$2.07 billion for consolidated (1) and First Federal, respectively. Risk-based capital is computed as a percentage of total risk-weighted assets of \$1.76 billion and \$1.76 billion for consolidated and First Federal, respectively.

To be categorized as a well-capitalized institution, institutions need to maintain a tier 1 (core) capital ratio of 5%, a tier 1 capital to risk-weighted assets ratio of 6%, and a risk-based capital ratio of 10%. First Federal's capital at December 31, 2013 meets the standards for a well-capitalized institution. There are no conditions or events since the most recent notification from any of the regulatory agencies regarding those capital standards that management believes have changed any of the well-capitalized categorizations of First Federal. First Defiance does not have capital requirements at this time.

Dividends - First Defiance's payment of dividends to its shareholders is generally funded by the payment of dividends by the Subsidiaries. Dividends paid by First Federal to First Defiance are subject to various regulatory restrictions. First Federal can initiate dividend payments equal to its net profits (as defined by statute) for the current year plus the preceding two calendar years. First Federal paid \$3.0 million and \$37.0 million in dividends in 2013 and 2012, respectively. First Insurance paid \$1.5 million and \$300,000 in dividends to First Defiance during 2013 and 2012, respectively.

First Defiance's ability to pay dividends to its shareholders is primarily dependent on the ability of the Subsidiaries to pay dividends to First Defiance. Capital distributions include, without limitation, payments of cash dividends, repurchases and certain other acquisitions by an association of its shares and payments to shareholders of another association in an acquisition of such other association.

Transactions with Insiders and Affiliates - Loans to executive officers, directors and principal shareholders and their related interests must conform to the lending limits. Most loans to directors, executive officers and principal shareholders must be approved in advance by a majority of the "disinterested" members of board of directors of the association with any "interested" director not participating. All loans to directors, executive officers and principal

shareholders must be made on terms substantially the same as offered in comparable transactions with the general public or as offered to all employees in a company-wide benefit program. Loans to executive officers are subject to additional restrictions. In addition, all related party transactions must be approved by the Company's audit committee pursuant to NASDAQ Rule 5630, including loans made by financial institutions in the ordinary course of business. All transactions between savings associations and their affiliates must comport with Sections 23A and 23B of the Federal Reserve Act (FRA) and the Federal Reserve's (FRB) Regulation W. An affiliate of a savings association is any company or entity that controls, is controlled by, or is under common control with the savings association. First Defiance and First Insurance are affiliates of First Federal.

Holding Company Regulation - First Defiance is a unitary thrift holding company and is subject to the Federal Reserve regulations, examination, supervision and reporting requirements. Federal law generally prohibits a thrift holding company from controlling any other savings association or thrift holding company, without prior approval of the Federal Reserve, or from acquiring or retaining more than 5% of the voting shares of a savings association or holding company thereof, which is not a subsidiary.

Deposit Insurance - First Federal is a member of the Deposit Insurance Fund (“DIF”), which is administered by the FDIC. Deposit accounts at First Federal are insured by the FDIC, generally up to a maximum of \$250,000. Further, from December 31, 2010 through December 31, 2012, deposits held in noninterest-bearing transaction accounts were fully insured by the FDIC regardless of the amount in the account. The Bank opted to participate in the FDIC’s Transaction Account Guarantee Program, which expired on December 31, 2012.

In October 2010, the FDIC adopted a new DIF restoration plan to ensure that the fund reserve ratio reaches 1.35% by September 30, 2020, as required by the Dodd-Frank Act. Under the new restoration plan, the FDIC will maintain the current schedule of assessment rates for all depository institutions. At least semi-annually, the FDIC will update its loss and income projections for the fund and, if needed, will increase or decrease assessment rates, following notice-and-comment rulemaking if required.

Insurance of deposits may be terminated by the FDIC upon finding that an institution has engaged in unsafe or unsound practices, is in an unsafe or unsound condition to continue operations or has violated any applicable law, regulation, rule, order or condition imposed by the FDIC. Management does not currently know of any practice, condition or violation that might lead to termination of the deposit insurance.

Recent Developments

Impact of Legislation - Over the last several years, Congress and the U.S. Department of the Treasury have enacted legislation and taken actions to address the disruptions in the financial system, declines in the housing market, and the overall regulation of financial institutions and the financial system. In this regard, the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act”), includes provisions affecting large and small financial institutions alike, including several provisions that profoundly affect the regulation of community banks, thrifts, and bank and thrift holding companies, such as First Defiance. Also, the Dodd-Frank Act abolished the Office of Thrift Supervision effective July 21, 2011 and transferred its functions to the Office of the Comptroller of the Currency (“OCC”), FDIC, and Federal Reserve. The Dodd-Frank Act relaxed rules regarding interstate branching, allows financial institutions to pay interest on business checking accounts, changed the scope of federal deposit insurance coverage, imposed new capital requirements on bank and thrift holding companies, and imposed limits on debit card interchange fees charged by issuer banks (commonly known as the Durbin Amendment).

The Dodd-Frank Act also established the Consumer Financial Protection Bureau (“CFPB”) as an independent bureau within the Federal Reserve, which has broad authority to regulate consumer financial products and services and entities offering such products and services, including banks. Many of the consumer financial protection functions formerly assigned to the federal banking and other designated agencies are now performed by the CFPB. The CFPB has broad rulemaking authority over providers of credit, savings, and payment services and products. In this regard, the CFPB has the authority to implement regulations under federal consumer protection laws and enforce those laws against, and examine, financial institutions. State officials also will be authorized to enforce consumer protection rules issued by the CFPB. This bureau also is authorized to collect fines and provide consumer restitution in the event of violations, engage in consumer financial education, track consumer complaints, request data, and promote the availability of financial services to underserved consumers and communities. The CFPB also is directed to prevent “unfair, deceptive or abusive practices” and ensure that all consumers have access to markets for consumer financial products and services and that such markets are fair, transparent, and competitive. Although the CFPB has begun to implement its regulatory, supervisory, examination, and enforcement authority, there continues to be significant

uncertainty as to how the agency's strategies and priorities will impact First Defiance.

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The CFPB has indicated that mortgage lending is an area of supervisory focus and that it will concentrate its examination and rulemaking efforts on the variety of mortgage-related topics required under the Dodd-Frank Act, including steering consumers to less-favorable products, discrimination, abusive or unfair lending practices, predatory lending, origination disclosures, minimum mortgage underwriting standards, mortgage loan originator compensation, and servicing practices. The CFPB recently published several final regulations impacting the mortgage industry, including rules related to ability-to-pay, mortgage servicing, and mortgage loan originator compensation. The ability-to-repay rule makes lenders liable if they fail to assess ability to repay under a prescribed test, but also creates a safe harbor for so called “qualified mortgages.” The “qualified mortgages” standards include a tiered cap structure that places limits on the total amount of certain fees that can be charged on a loan, a 43% cap on debt-to-income (i.e., total monthly payments on debt to monthly gross income), exclusion of interest-only products, and other requirements. The 43% debt-to-income cap does not apply for the first seven years the rule is in effect for loans that are eligible for sale to Fannie Mae or Freddie Mac or eligible for government guarantee through the FHA or the Veterans Administration. Failure to comply with the ability-to-repay rule may result in possible CFPB enforcement action and special statutory damages plus actual, class action, and attorney fees damages, all of which a borrower may claim in defense of a foreclosure action at any time. First Defiance’s management team is currently assessing the impact of these requirements on our mortgage lending business.

In addition, the Federal Reserve and other federal bank regulatory agencies have issued a proposed rule under the Dodd-Frank Act that would exempt “qualified residential mortgages” from the securitization risk retention requirements of the Dodd-Frank Act. The final definition of what constitutes a “qualified residential mortgage” may impact the pricing and depth of the secondary market into which the Company may sell mortgages it originates. At this time, First Defiance cannot predict the content of the final CFPB and other federal agency regulations or the impact they might have on First Defiance’s financial results. The CFPB’s authority over mortgage lending, and its authority to change regulations adopted in the past by other regulators, or to rescind or ignore past regulatory guidance, could increase First Defiance’s compliance costs and litigation exposure.

In addition to the CFPB’s authority over mortgage lending, the Dodd-Frank Act includes a series of provisions covering mortgage loan origination standards affecting, among other things, originator compensation, minimum repayment standards, and pre-payments. Moreover, the Dodd-Frank Act requires public companies like First Defiance to hold shareholder advisory “say-on-pay” votes on executive compensation at least once every three years and submit related proposals to a vote of shareholders. First Defiance held its first such “say-on-pay” vote at its 2013 annual meeting of shareholders.

New Volcker Rules - On December 10, 2013, the Board of Governors of the Federal Reserve System, the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Securities and Exchange Commission, and the Commodity Futures Trading Commission (“Regulators”) adopted the final version of the Volcker Rule (“Final Volcker Rule”). The Final Volcker Rule restricts United States banks from making certain kinds of speculative investments that do not benefit their customers. The Final Volcker Rule’s purpose is to put in place, as mandated under Section 619 of the Dodd-Frank Act, regulations to help avoid the financial crisis that occurred during the recent past. The Final Volcker Rule is intended to effectively reduce risks posed to banking entities by proprietary trading activities and investments in or relationships with covered funds while permitting banking entities to continue to provide client-oriented financial services that are critical to capital generation and liquid markets.

On January 14, 2014, the Regulators issued an interim final rule (“Interim Final Volcker Rule”) regarding the treatment of certain collateralized debt obligations backed by trust preferred securities (“TruPS-backed CDOs”) under the Final Volcker Rule implementing Section 619 of the Dodd-Frank Act. The Interim Final Volcker Rule, which does not technically amend the Final Volcker Rule but will operate as a “companion rule” to the Final Volcker Rule, specifies that the Final Volcker Rule’s covered fund restrictions do not apply to the ownership by a banking entity of an interest in, or sponsorship of, any issuer of TruPS-backed CDOs if certain conditions are met. Contemporaneously with the Regulators release of the Interim Final Volcker Rule, the Regulators issued a non-exclusive list of issuers of TruPS-backed CDOs that meet the requirements of the Interim Final Volcker Rule. The Interim Final Volcker Rule provides that a banking entity “may rely” on this list.

First Defiance owns eight collateralized debt obligations (“CDOs”). Six of those CDOs were on the Regulators non-exclusive list or have no book value while the other two CDOs were deemed to be disallowed under the Interim Final Volcker Rule. These two CDOs were subsequently sold on January 15, 2014.

First Defiance’s management team continues to actively monitor the implementation of the Dodd-Frank Act and the regulations promulgated thereunder and assess its probable impact on the business, financial condition, and results of operations of First Defiance. However, the ultimate effect of the Dodd-Frank Act on the financial services industry in general, and First Defiance in particular, continues to be uncertain.

New Proposed Capital Rules - On July 2, 2013, the Federal Reserve approved final rules that substantially amend the regulatory risk-based capital rules applicable to First Defiance and First Federal. The FDIC and the OCC have subsequently approved these rules. The final rules were adopted following the issuance of proposed rules by the Federal Reserve in June 2012, and implement the “Basel III” regulatory capital reforms and changes required by the Dodd-Frank Act.

The rules include new risk-based capital and leverage ratios, which will be phased in from 2015 to 2019, and will refine the definition of what constitutes “capital” for purposes of calculating those ratios. The new minimum capital level requirements applicable to First Defiance and First Federal under the final rules are: (i) a new common equity Tier 1 capital ratio of 4.5%; (ii) a Tier 1 capital ratio of 6% (increased from 4%); (iii) a total capital ratio of 8% (unchanged from current rules); and (iv) a Tier 1 leverage ratio of 4% for all institutions. The final rules also establish a “capital conservation buffer” above the new regulatory minimum capital requirements, which must consist entirely of common equity Tier 1 capital. The capital conservation buffer will be phased-in over four years beginning on January 1, 2016, as follows: the maximum buffer will be 0.625% of risk-weighted assets for 2016, 1.25% for 2017, 1.875% for 2018, and 2.5% for 2019 and thereafter. This will result in the following minimum ratios beginning in 2019: (i) a common equity Tier 1 capital ratio of 7.0%, (ii) a Tier 1 capital ratio of 8.5%, and (iii) a total capital ratio of 10.5%. Under the final rules, institutions are subject to limitations on paying dividends, engaging in share repurchases, and paying discretionary bonuses if its capital level falls below the buffer amount. These limitations establish a maximum percentage of eligible retained income that could be utilized for such actions.

The final rules implement revisions and clarifications consistent with Basel III regarding the various components of Tier 1 capital, including common equity, unrealized gains and losses, as well as certain instruments that will no longer qualify as Tier 1 capital, some of which will be phased out over time. However, the final rules provide that small depository institution holding companies with less than \$15 billion in total assets as of December 31, 2009 (which includes First Defiance) will be able to permanently include non-qualifying instruments that were issued and included in Tier 1 or Tier 2 capital prior to May 19, 2010 in additional Tier 1 or Tier 2 capital until they redeem such instruments or until the instruments mature.

The final rules also contain revisions to the prompt corrective action framework, which is designed to place restrictions on insured depository institutions, including First Federal, if their capital levels begin to show signs of weakness. These revisions take effect January 1, 2015. Under the prompt corrective action requirements, which are designed to complement the capital conservation buffer, insured depository institutions will be required to meet the following increased capital level requirements in order to qualify as “well capitalized”: (i) a new common equity Tier 1 capital ratio of 6.5%; (ii) a Tier 1 capital ratio of 8% (increased from 6%); (iii) a total capital ratio of 10% (unchanged from current rules); and (iv) a Tier 1 leverage ratio of 5% (increased from 4%).

The final rules set forth certain changes for the calculation of risk-weighted assets, which First Federal will be required to utilize beginning January 1, 2015. The standardized approach final rule utilizes an increased number of credit risk exposure categories and risk weights, and also addresses: (i) an alternative standard of creditworthiness consistent with Section 939A of the Dodd-Frank Act; (ii) revisions to recognition of credit risk mitigation; (iii) rules for risk weighting of equity exposures and past due loans; (iv) revised capital treatment for derivatives and repo-style transactions; and (v) disclosure requirements for top-tier banking organizations with \$50 billion or more in total assets that are not subject to the “advanced approaches rules” that apply to banks with greater than \$250 billion in consolidated assets.

Based on our current capital composition and levels, management believes it will be in compliance with the requirements as set forth in the final rules.

Item 1A. Risk Factors

The risks listed below present risks that could have a material impact on the Company's financial condition, results of operations, or business. The risks and uncertainties described below are the not the only ones facing the Company. Additional risks and uncertainties that management is not aware of or focused on or that management currently deems immaterial may also impair the Company's business operations.

Economic conditions may adversely affect First Defiance's operations and financial condition.

Local Economic Conditions - First Defiance conducts its banking and insurance business primarily in northwest Ohio, northeast Indiana and southeast Michigan. Unemployment rates for most of the counties within our geographic market area are above the median rate for the United States and above the median rates for the states of Ohio, Indiana, and Michigan. As reported for December 2013, the 14 counties in which our offices are located had unemployment rates between 5.2% and 11.5%, and 10 either stayed the same or experienced an improvement in their unemployment rate in 2013 compared to 2012. However, real estate values in certain First Defiance's markets are still unstable and may continue to be so in 2014. While the Company has seen improvement in the unemployment rates in its market areas and housing values starting to recover, high unemployment and unstable real estate values could have a negative impact on the Company's earnings and financial condition because:

- more borrowers are unable to make payments on their loans;
- the value of collateral securing loans has declined; and
- the overall quality of the loan portfolio has declined.

General Economic Conditions - Dramatic declines in real estate values, along with high unemployment, disrupted the national credit and capital markets over the last several years.

While economic conditions are beginning to improve slightly, First Defiance continues to face the following risks:

- inability of borrowers to make timely repayments of their loans, or decreases in value of real estate collateral securing the payment of such loans resulting in significant credit losses, which could result in increased delinquencies, foreclosures and customer bankruptcies, any of which could have a material adverse effect on our operating results;
- increased regulation of the financial services industry, including heightened legal standards and regulatory requirements or expectations; compliance with such regulation will likely increase costs and may limit the Company's ability to pursue business opportunities;
- further disruptions in the capital markets or other events, including actions by rating agencies and deteriorating investor expectations, may result in an inability to borrow on favorable terms or at all from other financial institutions;
- increased competition among financial services companies due to the consolidation of financial institutions, which may adversely affect our ability to market the Company's products and services; and
- further increases in FDIC insurance premiums due to the market developments which have significantly depleted the insurance fund of the FDIC and reduced the ratio of reserves to insured deposits.

Declining Real Estate Values - Approximately 74.9% of the loans in First Defiance's portfolio are secured in whole or in part by real estate. Because residential real estate prices have declined, some of our borrowers have mortgages that exceed the value of their homes. The decline in home values, coupled with the weakened economy, has increased defaults and foreclosures. Commercial real estate values have also declined, and the owners of many income-producing properties are experiencing declines in their revenue, which may adversely affect their ability to repay their loans. Foreclosures and resolutions of nonperforming loans require significant personnel resources and involve other costs that may increase our operating expenses. Properties acquired through foreclosure or by deed in lieu of foreclosure are taking longer to sell in the current economy, which increases the Company's expenses for managing, maintaining and insuring real estate owned. If First Defiance is unable to sell properties at a price that will cover its expenses as well as the unpaid principal and interest on the loan, the resulting write-downs and losses will adversely affect First Defiance's net income. The reduced levels of home sales have had a materially adverse effect on the prices achieved on the sale of foreclosed properties. Further decline in home values may escalate these problems, resulting in higher delinquencies, greater charge-offs, and increased losses on the sale of foreclosed real estate in future periods.

Volatile Capital Markets - The capital and credit markets have experienced volatility and disruption. In some cases, the markets have produced downward pressure on credit availability for certain issuers. Continuing market disruption and volatility could have an adverse effect on the Company's ability to access capital and on its business, financial condition and results of operations.

First Defiance's stock price may fluctuate significantly in the future and these fluctuations may be unrelated to the underlying performance of First Defiance. General market price declines and overall market volatility in the future could adversely affect the price of its common stock, and the current market price of the stock may not be indicative of future market prices.

First Defiance's stock price has been volatile in the past and several factors could cause the price to fluctuate substantially in the future. These factors include:

- Actions by government regulators;
- First Defiance's announcements of developments related to its business;
- Fluctuation in First Defiance's results of operation;
- Sales of substantial amounts of First Defiance's securities into the marketplace; and
- New reports of trends, concerns and other issues related to the financial services industry.

First Defiance's loan portfolio includes a concentration of commercial real estate loans and commercial loans, which involve risks specific to real estate value and the successful operations of these businesses.

At December 31, 2013, First Federal's portfolio of commercial real estate loans totaled \$819.6 million, or approximately 50.8% of total loans. First Federal's commercial real estate loans typically have higher principal amounts than residential real estate loans, and many of our commercial real estate borrowers have more than one loan outstanding. As a result, an adverse development on one loan can expose First Defiance to greater risk of loss on other loans. Additionally, repayment of the loans is generally dependent, in large part, on sufficient income from the properties securing the loans to cover operating expenses and debt service. Economic conditions and events outside of the control of the borrower or lender could negatively impact the future cash flow and market values of the affected properties.

At December 31, 2013, First Federal's portfolio of commercial loans totaled \$388.2 million, or approximately 24.1% of total loans. Commercial loans generally expose First Defiance to a greater risk of nonpayment and loss than commercial real estate or residential real estate loans since repayment of such loans often depends on the successful operations and income stream of the borrowers. First Federal's commercial loans are primarily made based on the identified cash flow of the borrower and secondarily on the underlying collateral provided by the borrower such as

accounts receivable, inventory, machinery or real estate. In the case of loans secured by accounts receivable, the availability of funds for the repayment of these loans may be substantially dependent on the ability of the borrower to collect amounts due from its customers. The collateral securing other loans may depreciate over time, may be difficult to appraise and may fluctuate in value based on the success of the business. Credit support provided by the borrower for most of these loans and the probability of repayment is based on the liquidation of the pledged collateral and enforcement of a personal guarantee, if any exists.

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First Defiance targets its business lending towards small and medium-sized businesses, many of which have fewer financial resources than larger companies and may be more susceptible to economic downturns. If general economic conditions negatively impact these businesses, First Defiance's results of operations and financial condition may be adversely affected.

Increases to the allowance for loan losses may cause First Defiance's earnings to decrease.

First Federal makes a number of assumptions and judgments about the collectability of its loan portfolio, including the creditworthiness of our borrowers and the value of the real estate and other assets serving as collateral for the repayment of loans. In determining the amount of the allowance for loan losses, First Federal relies on loan quality reviews, past loss experience, and an evaluation of economic conditions, among other factors. If its assumptions prove to be incorrect, First Federal's allowance for loan losses may not be sufficient to cover actual losses, resulting in additions to the allowance. In addition, bank regulators periodically review First Federal's allowance and may require First Federal to increase its allowance. Material additions to the allowance and any loan losses that exceed First Federal's reserves would materially adversely affect First Defiance's results of operations and financial condition.

Changes in interest rates can adversely affect First Defiance's profitability

First Defiance's earnings and financial condition are dependent to a large degree upon net interest income, which is the difference, or spread, between interest earned from loans and investments and interest paid on deposits and borrowings. Interest rates are highly sensitive to many factors, including:

- the rate of inflation;
- economic conditions;
- federal monetary policies; and
- stability of domestic and foreign markets.

Because First Defiance's interest-bearing liabilities may reprice or mature more quickly than its interest-earning assets, an increase in interest rates could result in a decrease in First Defiance's net interest income.

First Federal originates a significant amount of residential mortgage loans that it sells in the secondary market. The origination of residential mortgage loans is highly dependent on the local real estate market and the current interest rates. Increasing interest rates tend to reduce the origination of loans for sale and consequently fee income, which First Defiance reports as mortgage banking income. Conversely, decreasing interest rates have the effect of causing clients to refinance mortgage loans faster than anticipated. This causes the value of mortgage servicing rights on the loans sold to be lower than originally anticipated. If this happens, First Defiance may be required to write down the value of its mortgage servicing rights faster than anticipated, which will increase expense and lower earnings. Accelerated repayments on loans and mortgage backed securities could result in the reinvestment of funds at lower rates than the loans or securities were paying.

Laws and regulations may affect First Defiance's results of operations.

The earnings of financial institutions are affected by the regulations and policies of various regulatory authorities, including the Federal Reserve, which regulates the money supply, and the Federal Reserve which regulates the Company and OCC which regulates First Federal, and the FDIC, which regulates First Federal. The Federal Reserve has extensive supervisory authority over the Company, affecting a comprehensive range of matters relating to ownership and control of First Defiance's shares, First Defiance's acquisition of other companies and businesses, permissible activities for the Company to engage in, maintenance of adequate capital levels and other aspects of

operations. These supervisory and regulatory powers are intended primarily for the protection for First Defiance's depositors and customers and the deposit insurance fund, rather than First Defiance's shareholders.

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Comprehensive revisions to the regulatory capital framework were finalized by the FRB, OCC, and FDIC in 2013. Included within those revisions is Basel III, which incorporates changes made by the Basel Committee on Banking Supervision to the Basel Capital framework in addition to implementing relevant provisions of the Dodd-Frank Act. Basel III specifically revises what qualifies as regulatory capital, raises minimum requirements and introduces the concept of additional capital buffers. The need to maintain more and higher quality capital as well as greater liquidity going forward could limit our business activities, including lending, and our ability to expand, either organically or through acquisitions. In addition, the new liquidity standards could require us to increase our holdings of highly liquid short-term investments, thereby reducing our ability to invest in longer-term assets even if more desirable from a balance sheet management perspective.

The laws and regulations applicable to the banking industry could change at any time. As a result of ongoing challenges facing the U.S. economy in particular, the potential exists for new laws and regulations, and bank regulatory agencies are expected to be active in responding to concerns and trends identified in examinations. Increased regulation could increase First Defiance's cost of compliance and reduce its income to the extent that they limit the manner in which First Defiance may conduct business, including its ability to offer new products, charge fees for specific products and services, obtain financing, attract deposits, make loans and achieve satisfactory interest spreads.

First Defiance's ability to meet cash flow needs on a timely basis at a reasonable cost may adversely affect net income.

First Defiance's principal sources of liquidity are local deposits and wholesale funding sources such as FHLB advances, Federal Funds purchased, securities sold under repurchase agreements, and brokered or other out-of-market certificate of deposit purchases. Also, First Defiance maintains a portfolio of securities that can be used as a secondary source of liquidity. First Defiance's access to funding sources in amounts adequate to finance or capitalize its activities or on terms that are acceptable could be impaired by factors that affect First Defiance directly or the financial services industry or economy in general, such as further disruptions in the financial markets or negative views and expectations about the prospects for the financial services industry.

Other possible sources of liquidity include the sale or securitization of loans, the issuance of additional collateralized borrowings beyond those currently utilized with the FHLB, the issuance of debt securities and the issuance of preferred or common securities in public or private transactions, or borrowings from a commercial bank. First Defiance does not currently have any borrowings from a commercial bank, but it has used them in the past.

Any decline in available funding could adversely impact our ability to originate loans, invest in securities, meet our expenses, pay dividends to First Defiance's shareholders, or fulfill obligations such as repaying First Defiance's borrowings or meeting deposit withdrawal demands, any of which could have a material adverse impact on our liquidity, business, results of operations and financial condition.

Competition affects First Defiance's earnings.

First Defiance's continued profitability depends on its ability to continue to effectively compete to originate loans and attract and retain deposits. Competition for both loans and deposits is intense in the financial services industry. The Company competes in its market area by offering superior service and competitive rates and products. The type of institutions First Defiance competes with include large regional commercial banks, smaller community banks, savings institutions, mortgage banking firms, credit unions, finance companies, brokerage firms, insurance agencies and mutual funds. As a result of their size and ability to achieve economies of scale, certain of First Defiance's competitors can offer a broader range of products and services than the Company can offer. To stay competitive in its market area, First Defiance may need to adjust the interest rates on its products to match rates of its competition, which could have a negative impact on net interest margin.

The increasing complexity of First Defiance's operations presents varied risks that could affect its earnings and financial condition.

First Defiance processes a large volume of transactions on a daily basis and is exposed to numerous types of risks related to internal processes, people and systems. These risks include, but are not limited to, the risk of fraud by persons inside or outside the Company, the execution of unauthorized transactions by employees, errors relating to transaction processing and systems, breaches of data security and our internal control system and compliance with a complex array of consumer and safety and soundness regulations. First Defiance could also experience additional loss as a result of potential legal actions that could arise as a result of operational deficiencies or as a result of noncompliance with applicable laws and regulations.

First Defiance has established and maintains a system of internal controls that provides management with information on a timely basis and allows for the monitoring of compliance with operational standards. These systems have been designed to manage operational risks at an appropriate, cost effective level. Procedures exist that are designed to ensure that policies relating to conduct, ethics, and business practices are followed. Losses from operational risks may still occur, however, including losses from the effects of operational errors.

First Defiance's operations are also dependent on its existing infrastructure, including equipment and facilities. Extended disruption of vital infrastructure as a result of fire, power loss, natural disaster, telecommunications failures, computer hacking or viruses, terrorist activity or the domestic response to such activity, or other events outside of the control of management could have a material adverse impact on its business, results of operations, cash flows and financial condition. First Defiance has a business recovery plan, but there are no assurances that such a plan will work as intended or that it will prevent significant interruptions to operations.

Unauthorized disclosure of sensitive or confidential client or customer information, whether through a breach of the Company's computer systems or otherwise, could severely harm its business.

In the normal course of business, First Defiance collects, processes and retains sensitive and confidential client and customer information on behalf of First Defiance and other third parties. Despite the security measures the Company has in place, First Defiance's facilities and systems, and those of the Company's third party service providers, may be vulnerable to security breaches, acts of vandalism, computer viruses, lost or misplaced data, or other similar events. Any security breach involving the unauthorized disclosure or loss of confidential customer information, whether by First Defiance or by the Company's third party vendors, could severely damage First Defiance's reputation, expose the Company to risks of litigation and liability, disrupt First Defiance's operations and have a material adverse effect on First Defiance's business.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

At December 31, 2013, First Federal conducted its business from its main office at 601 Clinton Street, Defiance, Ohio, and thirty-one other full service banking centers in northwest Ohio, northeast Indiana and southeast Michigan. First Insurance conducted its business from leased office space at 419 5th Street, Suite 1200, Defiance, Ohio; 209 West Poe Road, Bowling Green, Ohio; 926 East High Street, Bryan, Ohio; 1755 Indian Wood Circle, Maumee, Ohio and 4350 Navarre Ave, Oregon, Ohio.

In September 2013, First Federal closed its branch on 926 E. High Street, Bryan, Ohio. This building is owned by First Federal.

In October 2013, First Insurance closed its insurance office on 214 N. Defiance St., Archbold, Ohio. This was a leased facility.

First Defiance maintains its headquarters in the main office of First Federal at 601 Clinton Street, Defiance, Ohio. Back-office operation departments, including information technology, loan processing and underwriting, deposit processing, accounting and risk management are headquartered in an operations center located at 25600 Elliott Road, Defiance, Ohio.

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The following table sets forth certain information with respect to the offices and other properties of the Company at December 31, 2013. See Note 9 to the Consolidated Financial Statements.

Description/address	Leased/ Owned	Net Book Value of Property (In Thousands)	Deposits
Main Office, First Federal			
601 Clinton St., Defiance, OH	Owned	\$ 4,476	\$ 220,886
Operations Center			
25600 Elliott Rd., Defiance, OH	Owned	5,311	N/A
Mobile Banking			
1011 W. Beecher St., Adrian, MI	Owned	190	N/A
Branch Offices, First Federal			
204 E. High St., Bryan, OH*	Owned	649	134,120
211 S. Fulton St., Wauseon, OH	Owned	437	52,457
625 Scott St., Napoleon, OH	Owned	999	68,800
1050 East Main St., Montpelier, OH	Owned	347	39,415
926 East High St., Bryan, OH*	Owned	87	-
1800 Scott St., Napoleon, OH	Owned	1,269	28,394
1177 N. Clinton St., Defiance, OH	Owned, Land Lease Leased	875	38,915
905 N. Williams St., Paulding, OH	Owned	738	61,033
201 E. High St., Hicksville, OH	Owned	346	30,422
3900 N. Main St., Findlay, OH	Owned	937	47,654
11694 N. Countyline St., Fostoria, OH	Owned	638	40,681
1226 W. Wooster, Bowling Green, OH	Owned	979	101,144
301 S. Main St., Findlay, OH	Owned	960	56,849
405 E. Main St., Ottawa, OH	Owned	324	88,830
124 E. Main St., McComb, OH	Owned	186	19,862
7591 Patriot Dr., Findlay, OH	Owned	1,115	35,557
417 W Dussell Dr., Maumee, OH	Owned, Land Lease	830	53,861
230 E. Second St., Delphos, OH	Owned	989	95,362
105 S. Greenlawn Ave., Elida, OH	Owned	319	47,180
2600 Allentown Rd., Lima, OH	Owned	770	45,466
22020 W. State Rt. 51, Genoa, OH	Owned	829	30,908
3426 Navarre Ave., Oregon, OH	Owned	910	29,771
1077 Louisiana Ave., Perrysburg, OH	Owned	1,070	30,963
2565 Shawnee Rd., Lima, OH	Owned	1,406	70,821
1595 Dupont Rd., Fort Wayne, IN	Leased	28	21,388
135 South Main St., Glandorf, OH	Leased	-	16,149
300 N. Main St., Adrian, MI	Owned	704	64,288
1701 W. Maumee St., Adrian, MI	Owned	160	45,320
211 W. Main St., Morenci, MI	Owned	159	28,771
539 S. Meridian, Hudson, MI	Owned	555	39,935
1449 W. Chicago Blvd., Tecumseh, MI	Owned	1,472	45,946
1200 North Main St., Bowling Green OH	Owned	1,644	4,644
First Insurance Group			
419 5th Street, Suite 1200, Defiance, OH	Leased	17	N/A
209 West Poe Road, Bowling Green, OH	Leased	8	N/A

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926 E. High Street, Bryan, OH	Leased	-	N/A
1755 Indian Wood Circle, Maumee, OH	Leased	-	N/A
4350 Navarre Ave, Oregon, OH	Leased	-	N/A
		\$ 32,733	\$ 1,735,792

* The Bryan East (926 East High St.) deposits are now included in the Bryan Main (204 E. High Street) totals.

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Item 3. Legal Proceedings

First Defiance is involved in routine legal proceedings occurring in the ordinary course of business which, in the aggregate, are believed by management to be immaterial to the financial condition of First Defiance.

Item 4. Mine Safety Disclosures

Not applicable.

PART II

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

The Company's common shares trade on The NASDAQ Global Select Market under the symbol "FDEF." As of February 21, 2014, the Company had 2,020 shareholders of record.

The table below shows the reported high and low sales prices of the common shares and cash dividends declared per common share during the periods indicated in 2013 and 2012.

	Years Ending December 31, 2013			December 31, 2012		
	High	Low	Dividend	High	Low	Dividend
Quarter ended:						
March 31	\$ 23.75	\$ 18.42	\$ 0.10	\$ 17.76	\$ 14.41	\$ 0.05
June 30	23.75	20.80	0.10	17.46	15.23	0.05
September 30	28.46	22.49	0.10	18.06	15.80	0.05
December 31	27.25	23.31	0.10	19.38	15.75	0.05

The line graph below compares the yearly percentage change in cumulative total shareholder return on First Defiance common shares and the cumulative total return of the NASDAQ Composite Index, the SNL NASDAQ Bank Index and the SNL Midwest Thrift Index. An investment of \$100 on December 31, 2008, and the reinvestment of all dividends are assumed. The performance graph represents past performance and should not be considered to be an indication of future performance.

Index	Period Ending					
	12/31/08	12/31/09	12/31/10	12/31/11	12/31/12	12/31/13
First Defiance Financial Corp.	100.00	153.53	161.82	199.10	265.02	364.68
NASDAQ Composite	100.00	145.36	171.74	170.38	200.63	281.22
SNL Bank NASDAQ	100.00	81.12	95.71	84.92	101.22	145.48
SNL Midwest Thrift	100.00	84.23	68.28	60.23	77.87	96.03

The following table provides information regarding First Defiance's purchases of its common stock during the three-month period ended December 31, 2013:

Period		Total Number of Shares Purchased	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (1)	Maximum Number of Shares (or Approximate Dollar Value) that May Yet Be Purchased Under the Plans or Programs (2)
October 1	October 31, 2013	-	\$ -	-	-
November 1	November 30, 2013	23,127	25.16	23,127	465,873
December 1	December 31, 2013	47,839	25.89	47,839	418,034
Total		70,966	\$ 25.65	70,966	418,034

The reported shares were repurchased pursuant to First Defiance's publicly announced stock repurchase program, (1) which became effective September 30, 2013. Up to 489,000 shares were authorized to be purchased under the program. There is no expiration date for the program.

The number of shares shown represents, as of the end of each period, the maximum number of shares of common (2) stock that may yet be purchased under publicly announced stock repurchase programs. The shares may be purchased, from time to time, depending on market conditions.

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Item 6. Selected Financial Data

The following table is derived from the Company's audited financial statements as of and for the five years ended December 31, 2013. The following consolidated selected financial data should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations and the Consolidated Financial Statements and related notes included elsewhere in this Form 10-K. The operating results of the acquired companies are included with the Company's results of operations since their respective dates of acquisition.

	As of and For the Year Ended December 31				
	2013	2012	2011	2010	2009
	(Dollars in Thousands, Except Per Share Data)				
Financial Condition:					
Total assets	\$ 2,137,148	\$ 2,046,948	\$ 2,068,190	\$ 2,035,517	\$ 2,057,523
Investment securities	198,557	194,609	233,580	166,091	139,378
Loans receivable, net	1,555,498	1,498,546	1,453,822	1,478,423	1,580,575
Allowance for loan losses	24,950	26,711	33,254	41,080	36,547
Nonperforming assets (1)	33,706	36,375	42,956	50,631	54,718
Deposits and borrowers' escrow balances	1,737,311	1,668,945	1,597,643	1,576,356	1,580,891
FHLB advances	22,520	12,796	81,841	116,885	146,927
Stockholders' equity	272,147	258,128	278,127	240,331	234,086
Share Information:					
Basic earnings per share	2.28	1.86	1.44	0.75	0.64
Diluted earnings per share	2.19	1.81	1.42	0.75	0.63
Book value per common share	27.91	26.44	24.74	25.00	24.26
Tangible book value per common share	21.22	19.63	17.78	17.16	16.44
Cash dividends per common share	0.40	0.20	0.05	-	0.295
Dividend payout ratio	17.45 %	10.75 %	3.47 %	NM	46.09 %
Weighted average diluted shares outstanding	10,171	9,998	9,540	8,153	8,196
Shares outstanding end of period	9,720	9,729	9,726	8,118	8,118
Operations:					
Interest income	\$ 74,781	\$ 80,943	\$ 87,067	\$ 95,865	\$ 100,579
Interest expense	7,170	11,937	17,186	25,702	33,257
Net interest income	67,611	69,006	69,881	70,163	67,322
Provision for loan losses	1,824	10,924	12,434	23,177	23,232
Non-interest income	30,570	34,374	27,516	27,590	26,295
Non-interest expense	64,844	65,780	62,764	63,463	60,524
Income before tax	31,513	26,676	22,199	11,113	9,861
Federal income tax	9,278	8,012	6,665	3,005	2,667
Net Income	22,235	18,664	15,534	8,108	7,194
Performance Ratios:					

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Return on average assets	1.08	%	0.90	%	0.75	%	0.39	%	0.36	%
Return on average equity	8.39	%	6.99	%	5.89	%	3.40	%	3.09	%
Interest rate spread (2)	3.65	%	3.64	%	3.69	%	3.68	%	3.50	%
Net interest margin (2)	3.76	%	3.81	%	3.88	%	3.89	%	3.76	%
Ratio of operating expense to average total assets	3.16	%	3.19	%	3.05	%	3.09	%	2.99	%
Efficiency ratio (3)	64.81	%	63.93	%	63.62	%	63.89	%	61.50	%
Capital Ratios:										
Equity to total assets at end of period	12.73	%	12.61	%	13.45	%	11.81	%	11.38	%
Tangible common equity to tangible assets at end of period	9.94	%	9.64	%	8.65	%	7.06	%	6.69	%
Average equity to average assets	12.92	%	12.95	%	12.82	%	11.62	%	11.49	%
Asset Quality Ratios:										
Nonperforming assets to total assets at end of period (1)	1.58	%	1.78	%	2.08	%	2.49	%	2.66	%
Allowance for loan losses to total loans*	1.58	%	1.75	%	2.24	%	2.70	%	2.26	%
Net charge-offs to average loans	0.23	%	1.18	%	1.41	%	1.21	%	0.70	%

(1) *Nonperforming assets consist of non-accrual loans that are contractually past due 90 days or more and real estate, mobile homes and other assets acquired by foreclosure or deed-in-lieu thereof.*

(2) *Interest rate spread represents the difference between the weighted average yield on interest-earning assets and the weighted average rate on interest-bearing liabilities. Net interest margin represents net interest income as a percentage of average interest-earning assets. Interest income on tax-exempt securities and loans has been adjusted to a tax-equivalent basis using the statutory federal income tax rate of 35%.*

(3) *Efficiency ratio represents non-interest expense divided by the sum of tax-equivalent net interest income plus non-interest income, excluding securities gain or losses, net.*

* *Total loans are net of undisbursed loan funds and deferred fees and costs.*

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

Forward-Looking Statements and Factors that Could Affect Future Results

Certain statements contained in this Annual Report on Form 10-K that are not statements of historical fact constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 ("Act"), notwithstanding that such statements are not specifically identified as such. In addition, certain statements may be contained in the Company's future filings with the SEC, in press releases, and in oral and written statements made by or with the approval of the Corporation that are not statements of historical fact and constitute forward-looking statements within the meaning of the Act. Examples of forward-looking statements include, but are not limited to: (i) projections of revenues, expenses, income or loss, earnings or loss per common share, the payment or nonpayment of dividends, capital structure and other financial items; (ii) statements of plans, objectives and expectations of First Defiance or its management or Board of Directors, including those relating to products or services; (iii) statements of future economic performance; and (iv) statements of assumptions underlying such statements. Words such as "believes", "anticipates", "expects", "intends", "targeted", "continue", "remain", "will", "should", "may" and other similar expressions are used to identify forward-looking statements but are not the exclusive means of identifying such statements.

Forward-looking statements involve risks and uncertainties that may cause actual results to differ materially from those in such statements. Factors that could cause actual results to differ from those discussed in the forward-looking statements include, but are not limited to:

- Local, regional, national and international economic conditions and the impact they may have on the Company and its customers and the Company's assessment of that impact.

- Volatility and disruption in national and international financial markets.

- Government intervention in the U.S. financial system.

- Changes in the level of non-performing assets and charge-offs.

- Changes in estimates of future reserve requirements based upon the periodic review thereof under relevant regulatory and accounting requirements.

- The effects of and changes in trade and monetary and fiscal policies and laws, including the interest rate policies of the Federal Reserve Board.

- Inflation, interest rate, securities market and monetary fluctuations.

- Political instability.

- Acts of God or of war or terrorism.

- The timely development and acceptance of new products and services and perceived overall value of these products and services by users.

- Changes in consumer spending, borrowing and saving habits.

- Changes in the financial performance and/or condition of the Company's borrowers.

- Technological changes including core system conversions.

· Acquisitions and integration of acquired businesses.

· The ability to increase market share and control expenses.

· Changes in the competitive environment among financial holding companies and other financial service providers.

· The effect of changes in laws and regulations (including laws and regulations concerning taxes, banking, securities and insurance) with which the Company and the subsidiaries must comply.

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The effect of changes in accounting policies and practices, as may be adopted by the regulatory agencies, as well as the Public Company Accounting Oversight Board, the Financial Accounting Standards Board and other accounting standard setters.

The costs and effects of legal and regulatory developments including the resolution of legal proceedings or regulatory or other governmental inquiries and the results of regulatory examinations or reviews.

Greater than expected costs or difficulties related to the integration of new products and lines of business.

The Company's success at managing the risks involved in the foregoing items.

Forward-looking statements speak only as of the date on which such statements are made. The Company undertakes no obligation to update any forward-looking statement to reflect events or circumstances after the date on which such statement is made or to reflect the occurrence of unanticipated events.

The following section presents information to assess the financial condition and results of operations of First Defiance. This section should be read in conjunction with the consolidated financial statements and the supplemental financial data contained elsewhere in this Annual Report on Form 10-K.

Overview

First Defiance is a unitary thrift holding company that conducts business through its subsidiaries, First Federal, First Insurance and First Defiance Risk Management.

First Federal is a federally chartered stock savings bank that provides financial services to communities based in northwest Ohio, northeast Indiana, and southeastern Michigan where it operates 32 full service banking centers in 12 northwest Ohio counties, 1 northeast Indiana county, and 1 southeastern Michigan county.

First Federal provides a broad range of financial services including checking accounts, savings accounts, certificates of deposit, real estate mortgage loans, commercial loans, consumer loans, home equity loans and trust and wealth management services through its extensive branch network.

First Insurance sells a variety of property and casualty, group health and life and individual health and life insurance products. First Insurance is an insurance agency that does business in the Defiance, Bryan, Bowling Green, Maumee and Oregon, Ohio areas. On July 1, 2011, the Company completed its acquisition of Payak-Dubbs Insurance Agency, Inc. ("PDI"), an independent property and casualty insurance agency with two office locations based in Maumee, Ohio and Oregon, Ohio for a cash price of \$4.8 million. PDI was merged into First Insurance. See Note 3 Acquisitions in the Notes to the Financial Statements.

First Defiance Risk Management is a wholly-owned insurance company subsidiary of the Company to insure the Company and its subsidiaries against certain risks unique to the operations of the Company and for which insurance may not be currently available or economically feasible in today's insurance marketplace. First Defiance Risk Management pools resources with several other similar insurance company subsidiaries of financial institutions to spread a limited amount of risk among themselves. First Defiance Risk Management was incorporated on December 20, 2012.

Financial Condition

Assets at December 31, 2013 totaled \$2.14 billion compared to \$2.05 billion at December 31, 2012, an increase of \$90.2 million or 4.4%. Cash and cash equivalents increased \$42.5 million to \$179.3 million at December 31, 2013 from \$136.8 million at December 31, 2012. The increase in assets was due to an increase in the deposit base as of December 31, 2013. The Company continues to deploy lower yielding overnight deposits into securities on the short to intermediate end of the yield curve until loan demand becomes more consistent.

Securities

The securities portfolio increased \$3.9 million to \$198.6 million at December 31, 2013. The 2013 activity in the portfolio included \$49.2 million of purchases, \$19.4 million of amortization and maturities, \$16.2 million of principal pay-downs and \$4.0 million of securities being sold. There was a net decrease of \$6.1 million in market value on available-for-sale securities. The Company also recorded \$337,000 of other-than-temporary impairment on two collateralized debt obligations in 2013. See Note 5 Investment Securities in the Notes to the financial statements for additional information.

Loans

Loans receivable, net of undisbursed loan funds and deferred fees and costs, increased \$55.2 million to \$1.58 billion at December 31, 2013. For more details on the loan balances, see Note 7 Loans Receivable in the Notes to the Financial Statements.

The majority of First Defiance's non-residential real estate and commercial loans are to small and mid-sized businesses. The combined commercial, non-residential real estate and multi-family real estate loan portfolios totaled \$1.21 billion and \$1.18 billion at December 31, 2013 and 2012, respectively, and accounted for approximately 74.9% and 76.5% of First Defiance's loan portfolio at the end of those respective periods. First Defiance believes it has been able to establish itself as a leader in its market area in the commercial and commercial real estate lending area by hiring experienced lenders and providing a high level of customer service to its commercial lending clients.

The one-to-four family residential portfolio totaled \$195.8 million at December 31, 2013, compared with \$200.8 million at the end of 2012. At the end of 2013, those loans comprised 12.1% of the total loan portfolio, down from 13.0% at December 31, 2012.

Construction loans, which include one to four family and commercial real estate properties, increased to \$86.1 million at December 31, 2013 compared to \$37.8 million at December 31, 2012. These loans accounted for approximately 5.3% and 2.5% of the total loan portfolio at December 31, 2013 and 2012, respectively.

Home equity and home improvement loans declined to \$106.9 million at December 31, 2013, from \$108.7 million at the end of 2012. At the end of 2013, those loans comprised 6.6% of the total loan portfolio, down from 7.0% at December 31, 2012.

Consumer finance and mobile home loans were \$16.9 million at December 31, 2013, up from \$15.9 million at the end of 2012. These loans comprised just 1.1% and 1.0% of the total portfolio at December 31, 2013 and 2012, respectively.

In order to properly assess the collateral dependent loans included in its loan portfolio, the Company has established policies regarding the monitoring of the collateral underlying such loans. The Company requires an appraisal that is less than one year old for all new collateral dependent real estate loans, and all renewed collateral dependent real estate loans where significant new money is extended. The appraisal process is handled by the Credit Department, which selects the appraiser and orders the appraisal. First Defiance's loan policy prohibits the account officer from talking or communicating with the appraiser to insure that the appraiser is not influenced by the account officer in any

way in making their determination of value.

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First Federal generally does not require updated appraisals for performing loans unless significant new money is requested by the borrower.

When a collateral dependent loan is downgraded to classified status, First Federal reviews the most current appraisal on file and if necessary, based on First Federal's assessment of the appraisal, such as age, market, etc, First Federal will discount this amount to a more appropriate current value based on inputs from lenders and realtors. This amount may then be discounted further by First Federal's estimation of the selling costs. In most instances, if the appraisal is more than twelve to fifteen months old, a new appraisal may be required. Finally, First Federal assesses whether there is any collateral short fall, taking into consideration guarantor support and liquidity, and determines if a charge off is necessary.

When a collateral dependent loan moves to non-performing status, First Federal generally gets a new third party appraisal and charges the loan down appropriately based upon the new appraisal and an estimate of costs to liquidate the collateral. All properties that are moved into the Other Real Estate Owned ("OREO") category are supported by current appraisals, and the OREO is carried at the lower of cost or fair value, which is determined based on appraised value less First Federal's estimate of the liquidation costs.

First Federal does not adjust any appraisals upward without written documentation of this valuation change from the appraiser. When setting reserves and charge offs on classified loans, appraisal values may be discounted downward based upon First Federal's experience with liquidating similar properties.

All loans over 90 days past due and/or on non-accrual are classified as non-performing loans. Non-performing status automatically occurs in the month in which the 90 day delinquency occurs.

As stated above, once a collateral dependent loan is identified as non-performing, First Federal generally gets an appraisal.

Appraisals are received within approximately 60 days after they are requested. The First Federal Loan Loss Reserve Committee reviews the amount of each new appraisal and makes any necessary charge off decisions at its meeting prior to the end of each quarter.

Any partially charged-off collateral dependent loans are considered non-performing, and as such, would need to show an extended period of time with satisfactory payment performance as well as cash flow coverage capability supported by current financial statements before First Federal will consider an upgrade to performing status. First Federal may consider moving the loan to accruing status after approximately six months of satisfactory payment performance.

For loans where First Federal determines that an updated appraisal is not necessary, other means are used to verify the value of the real estate, such as recent sales of similar properties on which First Federal had loans as well as calls to appraisers, brokers, realtors and investors. First Federal monitors and tracks its loan to value quarterly to determine accuracy and any necessary charge offs. Based on these results, changes may occur in the processes used.

Loan modifications constitute a Troubled Debt Restructuring if First Federal for economic or legal reasons related to the borrower's financial difficulties grants a concession to the borrower that it would not otherwise consider. For loans that are considered Troubled Debt Restructurings, First Federal either computes the present value of expected future cash flows discounted at the original loan's effective interest rate or it may measure impairment based on the fair value of the collateral. For those loans measured for impairment utilizing the present value of future cash flows method, any discount is carried as a reserve in the allowance for loan and lease losses. For those loans measured for impairment utilizing the fair value of the collateral, any shortfall is charged off. As of December 31, 2013 and December 31, 2012, First Federal Bank had \$27.6 million and \$28.2 million, respectively, of loans that were still performing and which were classified as Troubled Debt Restructurings.

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Allowance for Loan Losses

The allowance for loan losses represents management's assessment of the estimated probable incurred credit losses in the loan portfolio at each balance sheet date. Management analyzes the adequacy of the allowance for loan losses regularly through reviews of the loan portfolio. Consideration is given to economic conditions, changes in interest rates and the effect of such changes on collateral values and borrower's ability to pay, changes in the composition of the loan portfolio and trends in past due and non-performing loan balances. The allowance for loan losses is a material estimate that is susceptible to significant fluctuation and is established through a provision for loan losses based on management's evaluation of the inherent risk in the loan portfolio. In addition to extensive in-house loan monitoring procedures, the Company utilizes an outside party to conduct an independent loan review of all commercial loan and commercial real estate loan relationships that exceed \$1 million of aggregate exposure over a twelve month period. Management utilizes the results of this outside loan review to assess the effectiveness of its internal loan grading system as well as to assist in the assessment of the overall adequacy of the allowance for loan losses associated with these types of loans.

The provision for loan losses is determined by management as the amount to be added to the allowance for loan losses after net charge-offs have been deducted to bring the allowance to a level which, in management's best estimate, is necessary to absorb incurred credit losses within the existing loan portfolio in the normal course of business. The allowance for loan loss is made up of two basic components. The first component is the specific allowance in which the company sets aside reserves based on the analysis of individual credits that are cash flow dependent, yet there is a discount between the present value of the future cash flows and the carrying value. This was \$1.4 million at December 31, 2013. The second component is the general reserve. The general reserve is used to record loan loss reserves for groups of homogenous loans in which the Company estimates the losses incurred in the portfolios based on quantitative and qualitative factors. Due to the uncertainty of risks in the loan portfolio, the Company's judgment on the amount of the allowance necessary to absorb loans losses is approximate.

Due to regulatory guidance, the Company no longer carries specific reserves on collateral dependent loans, and instead usually charges off any shortfall. First Federal analyzes all loans on its classified and special mention lists at least quarterly and makes judgments about the risk of loss based on the cash flow of the borrower, the value of any collateral and the financial strength of any guarantor in determining the amount of impairment of individual loans and the charge off to be taken.

For purpose of the general reserve analysis, the loan portfolio is stratified into nine different loan pools based on loan type and by market area to allocate historic loss experience. The loss experience factor applied to the non-impaired loan portfolio was based upon historical losses of the most recent weighted rolling twelve quarters ending December 31, 2013.

The stratification of the loan portfolio resulted in a quantitative general allowance of \$11.2 million at December 31, 2013 compared to \$14.4 million at December 31, 2012. The decrease in the quantitative allowance was due to a decrease in the historical loss factors relating to commercial, commercial real estate, residential and consumer loans.

In addition to the quantitative analysis, a qualitative analysis is performed each quarter to provide additional general reserves on the non-impaired loan portfolio for various factors. The overall qualitative factors are based on nine sub-factors. The nine sub-factors have been aggregated into three qualitative factors: economic, environment and risk.

ECONOMIC

- 1) Changes in international, national and local economic business conditions and developments, including the condition of various market segments.
- 2) Changes in the value of underlying collateral for collateral dependent loans.

ENVIRONMENT

- 3) Changes in the nature and volume in the loan portfolio.
- 4) The existence and effect of any concentrations of credit and changes in the level of such concentrations.
- 5) Changes in lending policies and procedures, including underwriting standards and collection, charge-off and recovery practices.
- 6) Changes in the quality and breadth of the loan review process.
- 7) Changes in the experience, ability and depth of lending management and staff.

RISK

- 8) Changes in the trends of the volume and severity of delinquent and classified loans, and changes in the volume of non-accrual loans, trouble debt restructuring, and other loan modifications.
- 9) Changes in the political and regulatory environment.

The qualitative analysis at December 31, 2013 indicated a general reserve of \$12.3 million compared with \$10.8 million at December 31, 2012. Management reviewed the overall economic, environmental and risk factors and determined that it was appropriate to increase several of the factors as a result of recent experience indicating continued declines in commercial real estate appraised values, rising interest rates in 2013 coupled with the forecast for continued higher rates in 2014, and slightly rising unemployment rates in several Northwest Ohio counties. While management believes that the overall economy and operating environment has generally stabilized in 2013 and the risk of a further significant contraction in the near term is low in our markets, management still anticipates that economic growth will be slow to moderate over the next twelve months. Management also anticipates that past due levels and classified loan levels will possibly fluctuate over the next several quarters but directionally trend toward improvement until a sustainable improvement in the economy and asset quality metrics can be realized. First Defiance's general reserve percentages for main loan segments not otherwise classified ranged from 0.25% for construction loans to 1.68% for nonresidential real estate loans.

As a result of the quantitative and qualitative analysis, along with the change in specific reserves, the Company's provision for loan losses for 2013 was \$1.8 million compared to \$10.9 million for 2012. The allowance for loan losses was \$25.0 million at December 31, 2013 and \$26.7 million at December 31, 2012 and represented 1.58% and 1.75% of loans, net of undisbursed loan funds and deferred fees and costs, respectively. That decrease was mainly the result of the lower quantitative factors driven by lower charge offs and improvement in overall credit risk profile as well as the overall higher balance of loans. The pace of the decline in real estate values has slowed and in some markets has stabilized. While some collateral dependent loans no longer have enough collateral value to support the outstanding balance Management believes it has processes in place to identify and assess market values. Management has expanded its credit monitoring functions even further beyond its traditionally strong focus. Additional asset review functions and more delinquent loan reporting requirements have been added to assist in this monitoring. Management will continually review credit concentrations by industry and has placed lower limits on lending within certain types of loan categories. Management has also segmented the commercial real estate portfolio to track the general performance of these segments to further refine the predictive process of identifying potential problem loans. The provision was offset by charge offs of \$5.2 and recoveries of \$1.6 million resulting in a decrease to the overall allowance for loan loss of \$1.7 million. In management's opinion, the overall allowance for loan losses of \$25.0 million as of December 31, 2013 is adequate.

Management also assesses the value of real estate owned as of the end of each accounting period and recognizes write-downs to the value of that real estate in the income statement if conditions dictate. In 2013, First Defiance recorded real estate owned write-downs that totaled \$740,000. These amounts were included in other non-interest expense. Management believes that the values recorded at December 31, 2013 for real estate owned and repossessed assets represent the realizable value of such assets.

Total classified loans decreased to \$55.6 million at December 31, 2013, compared to \$78.1 million at December 31, 2012.

First Defiance's ratio of allowance for loan losses to non-performing loans was 89.6% at December 31, 2013 compared with 82.0% at December 31, 2012. Management monitors collateral values of all loans included on the watch list that are collateral dependent and believes that allowances for those loans at December 31, 2013 are appropriate.

At December 31, 2013, First Defiance had total non-performing assets of \$33.7 million, compared to \$36.4 million at December 31, 2012. Non-performing assets include loans that are 90 days past due, real estate owned and other assets held for sale.

The decrease in non-performing loans between December 31, 2012 and December 31, 2013 is in non-residential and multi-family residential real estate. The balance of non-residential and multi-family residential real estate non-performing loans was \$7.3 million higher at December 31, 2012 compared to December 31, 2013. This was partially offset by an increase in commercial loans of \$2.7 million from December 31, 2012 to December 31, 2013.

Non-performing loans in the single-family residential, non-residential and multi-family residential real estate and commercial loan categories represent 1.67%, 1.93% and 2.14% of the total loans in those categories respectively at December 31, 2013 compared to 1.79%, 2.90% and 1.47% respectively for the same categories at December 31, 2012. Management believes that the current allowance for loan losses is appropriate and that the provision for loan losses recorded in 2013 is consistent with both charge-off experience and the risk inherent in the overall credits in the portfolio.

First Federal's Asset Review Committee meets monthly to review the status of work-out strategies for all criticized relationships, which include all non-accrual loans. Based on such factors as anticipated collateral values in liquidation scenarios, cash flow projections, assessment of net worth of guarantors and all other factors which may mitigate risk of loss, the Asset Review Committee makes recommendations regarding proposed charge-offs which are approved by the Senior Loan Committee or the Loan Loss Reserve Committee.

For the twelve months ended and as of December 31, 2013, commercial real estate, which represented 50.80% of total loans, accounted for 45.69% of net charge-offs and 56.86% of nonaccrual loans, and commercial loans, which represented 24.06% of total loans, accounted for 26.22% of net charge-offs and 29.90% of nonaccrual loans. For the twelve months ended and as of December 31, 2012, commercial real estate, which represented 51.63% of total loans, accounted for 58.98% of net charge-offs and 70.89% of nonaccrual loans, and commercial loans, which represented 24.85% of total loans, accounted for 21.11% of net charge-offs and 17.38% of nonaccrual loans.

Table 1 Net Charge-offs and Non-accruals by Loan Type

	For the Twelve Months Ended December 31, 2013		As of December 31, 2013			
	Net Charge-offs (in thousands)	% of Total Net Charge-offs	Nonaccrual Loans (in thousands)	% of Total Non-Accrual Loans		
Residential	\$ 361	10.07	% \$ 3,273	11.76		
Construction	-	0.00	% -	0.00		
Commercial real estate	1,638	45.69	% 15,834	56.86		
Commercial	940	26.22	% 8,327	29.90		
Consumer finance	14	0.39	% -	0.00		
Home equity and improvement	632	17.63	% 413	1.48		
Total	\$ 3,585	100.00	% \$ 27,847	100.00		

	For the Twelve Months Ended December 31, 2012		As of December 31, 2012			
	Net Charge-offs (in thousands)	% of Total Net Charge-offs	Nonaccrual Loans (in thousands)	% of Total Non-Accrual Loans		
Residential	\$ 2,338	13.38	% \$ 3,602	11.06		
Construction	-	0.00	% -	0.00		
Commercial real estate	10,302	58.98	% 23,090	70.89		
Commercial	3,688	21.11	% 5,661	17.38		
Consumer finance	69	0.40	% -	0.00		
Home equity and improvement	1,070	6.13	% 217	0.67		
Total	\$ 17,467	100.00	% \$ 32,570	100.00		

The following table sets forth information concerning the allocation of First Defiance's allowance for loan losses by loan categories at December 31, 2013 and December 31, 2012.

Table 2 Allowance for Loan Loss Allocation by Loan Category

	December 31, 2013		December 31, 2012			
	Amount (dollars in thousands)	Percent of total loans by category	Amount	Percent of total loans by category		
Residential	\$ 2,847	12.13 %	\$ 3,506	13.00 %		
Construction	134	5.33 %	75	2.45 %		
Commercial real estate	14,508	50.80 %	14,899	51.63 %		
Commercial	5,678	24.06 %	6,325	24.85 %		
Consumer	148	1.05 %	147	1.03 %		
Home equity and improvement	1,635	6.63 %	1,759	7.04 %		
Total	\$ 24,950	100.00 %	\$ 26,711	100.00 %		

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Loans Acquired with Impairment

Certain loans acquired had evidence that the credit quality of the loan had deteriorated since its origination and, in management's assessment at the acquisition date, it was probable that First Defiance would be unable to collect all contractually required payments due. In accordance with FASB ASC Topic 310 Subtopic 30, *Loans and Debt Securities Acquired with Deteriorated Credit Quality*, these loans were recorded based on management's estimate of the fair value of the loans.

As of December 31, 2013, the total contractual receivable for those loans was \$503,000 and the recorded value was \$230,000.

High Loan-to-Value Mortgage Loans

The majority of First Defiance's mortgage loans are collateralized by one-to-four-family residential real estate, have loan-to-value ratios of 80% or less, and are made to borrowers in good credit standing. First Federal usually requires residential mortgage loan borrowers whose loan-to-value is greater than 80% to purchase private mortgage insurance (PMI). Management also periodically reviews and monitors the financial viability of its PMI providers.

First Federal originates and retains a limited number of residential mortgage loans with loan-to-value ratios that exceed 80% where PMI is not required if the borrower possesses other demonstrable strengths. The loan-to-value ratios on these loans are generally limited to 85% and exceptions must be approved by First Federal's senior loan committee. Management monitors the balance of one-to-four family residential loans, including home equity loans and committed lines of credit that exceed certain loan to value standards (90% for owner occupied residences, 85% for non-owner occupied residences and one-to-four family construction loans, 75% for developed land and 65% for raw land). Total loans that exceed those standards described above at December 31, 2013 totaled \$43.7 million, compared to \$45.2 million at December 31, 2012. These loans are generally paying as agreed.

First Defiance does not make interest-only first-mortgage residential loans, nor does it have residential mortgage loan products or other consumer products that allow negative amortization.

Goodwill and Intangible Assets

Goodwill was \$61.5 million at December 31, 2013 and 2012. No impairment of goodwill was recorded in 2013 or 2012. Core deposit intangibles and other intangible assets decreased to \$3.5 million at December 31, 2013 compared to \$4.7 million at December 31, 2012. During 2013, changes to the core deposit intangibles and other intangibles were due to the recognition of \$1.2 million of amortization expense.

Deposits

Total deposits at December 31, 2013 were \$1.74 billion compared to \$1.67 billion at December 31, 2012, an increase of \$68.3 million or 4.1%. Non-interest bearing deposits increased \$33.8 million or 10.7% while interest bearing deposits increased \$34.5 million or 2.6%. Non-interest bearing checking accounts grew by \$33.8 million, money market and interest bearing checking accounts grew by \$51.1 million, and savings grew by \$18.1 million while retail certificates of deposit declined by \$32.7 million. Management periodically utilizes the national market for certificates of deposit to supplement its funding needs. The balance of national CD's decreased to \$0 at December 31, 2013, from \$2.0 million at December 31, 2012. For more details on the deposit balances in general see Note 11 Deposits.

Borrowings

FHLB advances totaled \$22.5 million at December 31, 2013 compared to \$12.8 million at December 31, 2012. The balance at the end of 2013 includes \$12.0 million of convertible advances with rates ranging from 2.35% to 3.04%. These advances are all callable by the FHLB, at which point they would convert to a three-month LIBOR advance if not paid off. Those advances have final maturity dates ranging from 2015 to 2018. In addition, First Defiance has two fixed-rate advances totaling \$10.5 million with rates ranging from 1.78% to 4.10%. The change in FHLB advances is the result of securing an advance in the third quarter of 2013 in order to match fund certain fixed rate loan requests.

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At December 31, 2013, First Defiance also had \$51.9 million of securities that were sold with agreements to repurchase, compared to \$51.7 million at December 31, 2012.

Capital Resources

Total stockholders' equity increased \$14.0 million to \$272.1 million at December 31, 2013. This increase is a result of net income of \$22.2 million, partially offset by a decrease in the market value of the available-for-sale security portfolio in the amount of \$3.7 million and \$3.9 million in common stock dividends. On September 30, 2013, the Board of Directors authorized a new share repurchase program of up to 5%, or approximately 489,000 shares, of the common stock outstanding. During the fourth quarter 2013, 70,966 shares were repurchased, resulting in a \$1.8 million decrease in stockholders' equity, and a total of 39,330 stock options were exercised resulting in a \$350,000 increase in stockholders' equity. During 2012, no shares were repurchased, but a total of 500 stock options were exercised resulting in a \$4,000 increase in stockholders' equity.

Results of Operations

Summary

First Defiance reported net income of \$22.2 million for the year ended December 31, 2013 compared to \$18.7 million and \$15.5 million for the years ended December 31, 2012 and 2011, respectively. Net income applicable to common shares was \$22.2 million in 2013 compared with \$18.0 million in 2012 and \$13.5 million in 2011. On a diluted per common share basis, First Defiance earned \$2.19 in 2013, \$1.81 in 2012 and \$1.42 in 2011.

First Defiance's 2013 and 2012 net income of \$22.2 million and \$18.7 million respectively, did not include any acquisition related costs. The 2011 net income included \$234,000 of acquisition related costs resulting from the PDI acquisition. Excluding this item, core earnings were \$22.2 million, \$18.7 million and \$15.7 million for the years ended December 31, 2013, 2012 and 2011, respectively. On a diluted per share basis, core earnings amounted to \$2.19, \$1.81 and \$1.43 for those same three periods.

Net Interest Income

First Defiance's net interest income is determined by its interest rate spread (i.e. the difference between the yields on its interest-earning assets and the rates paid on its interest-bearing liabilities) and the relative amounts of interest-earning assets and interest-bearing liabilities.

As demand for new lending opportunities increased modestly in 2013 coupled with a surge in deposits, the Company continued to invest some of its liquidity into investment securities. This may continue into 2014 as management deems it appropriate within its liquidity strategy and consideration of overall loan demand and deposit growth.

Net interest income was \$67.6 million for the year ended December 31, 2013 compared to \$69.0 million and \$69.9 million for the years ended December 31, 2012 and 2011, respectively. The tax-equivalent net interest margin was 3.76%, 3.81% and 3.88% for the years ended December 31, 2013, 2012 and 2011, respectively. The margin was down slightly between 2012 and 2013. Interest-earning asset yields decreased 30 basis points (to 4.14% in 2013 from 4.44% in 2012) and the cost of interest bearing liabilities between the two periods decreased 30 basis points (to 0.49% in 2013 from 0.79% in 2012).

Total interest income decreased by \$6.1 million or 7.6% to \$74.8 million for the year ended December 31, 2013 from \$80.9 million for the year ended December 31, 2012. The decrease in interest income was due to a decline in asset yields, mainly as a result of a drop in yields on loans receivable which declined 46 basis points to 4.46% at December 31, 2013. Interest income from loans decreased to \$68.1 million for 2013 compared to \$72.6 million in 2012 which represents a decline of 6.3%.

During the same period, the average balance of investment securities decreased to \$191.0 million for 2013 from \$247.4 million for the year ended December 31, 2012. Interest income from the investment portfolio decreased to \$5.6 million for 2013 from \$7.1 million for 2012. The decline in average balance and interest income was a result of a balance sheet restructure that took place late in 2012. The tax-equivalent yield on the investment portfolio was 3.78% in 2013 compared to 3.63% in 2012. The overall duration of investments increased to 4.5 years at December 31, 2013 from 3.5 years at December 31, 2012.

Interest expense decreased by \$4.8 million in 2013 compared to 2012, to \$7.2 million from \$11.9 million. This decrease was due to a 30 basis point decline in the average cost of interest-bearing liabilities in 2013. Interest expense related to interest-bearing deposits was \$5.9 million in 2013 and \$8.2 million in 2012. Expenses on FHLB advances and other interest bearing funding sources were \$434,000 and \$222,000 respectively in 2013 and \$2.4 million and \$373,000 respectively in 2012. Interest expense recognized by the Company related to subordinated debentures was \$601,000 in 2013 and \$971,000 in 2012.

Total interest income decreased by \$6.1 million or 7.0% to \$80.9 million for the year ended December 31, 2012 from \$87.1 million for the year ended December 31, 2011. The decrease in interest income was due to a decline in asset yields, mainly as a result of a drop in yields on loans receivable which declined 57 basis points to 4.92% at December 31, 2012. Interest income from loans decreased to \$72.6 million for 2012 compared to \$78.6 million in 2011 which represents a decline of 7.7%.

During the same period, the average balance of investment securities increased to \$247.4 million for 2012 from \$205.6 million for the year ended December 31, 2011. Interest income from the investment portfolio remained flat at \$7.1 million from 2011 to 2012. The tax-equivalent yield on the investment portfolio was 3.63% in 2012 compared to 4.19% in 2011. The overall duration of investments decreased to 3.5 years at December 31, 2012 from 3.7 years at December 31, 2011.

Interest expense decreased by \$5.3 million in 2012 compared to 2011, to \$11.9 million from \$17.2 million. This decrease was due to a 33 basis point decline in the average cost of interest-bearing liabilities in 2012. Interest expense related to interest-bearing deposits was \$8.2 million in 2012 and \$12.2 million in 2011. Expenses on FHLB advances and other interest bearing funding sources were \$2.4 million and \$373,000 respectively in 2012 and \$3.2 million and \$530,000 respectively in 2011. Interest expense recognized by the Company related to subordinated debentures was \$1.0 million in 2012 and \$1.3 million in 2011.

The following table shows an analysis of net interest margin on a tax equivalent basis for the years ended December 31, 2013, 2012 and 2011:

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The following table shows an analysis of net interest margin on a tax equivalent basis for the years ended December 31, 2019 and 2018:

Table 3 Net Interest Margin

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Year Ended December 31
(In Thousands)

	2013				2012				2011		
	Average Balance	Interest (1)	Yield/ Rate (2)		Average Balance	Interest (1)	Yield/ Rate		Average Balance	Interest (1)	Yield/ Rate
Interest-Earning Assets:											
Loans receivable	\$ 1,528,176	\$ 68,147	4.46	%	\$ 1,477,681	\$ 72,724	4.92	%	\$ 1,437,588	\$ 78,773	5.49
Securities	191,039	7,158	3.78	%	247,442	8,675	3.63	%	205,609	8,440	4.19
Interest-earning deposits	106,742	282	0.26	%	116,562	300	0.26	%	184,126	466	0.25
FHLB stock	19,505	826	4.23	%	20,655	899	4.35	%	20,831	867	4.17
Total interest-earning assets	1,845,462	76,413	4.14	%	1,862,340	82,598	4.44	%	1,848,154	88,546	4.80
Non-interest-earning assets	206,788				201,212				210,216		
Total Assets	\$ 2,052,250				\$ 2,063,552				\$ 2,058,370		
Interest-Bearing Liabilities:											
Interest-bearing deposits	\$ 1,353,304	\$ 5,913	0.44	%	\$ 1,352,724	\$ 8,169	0.60	%	\$ 1,358,785	\$ 12,175	0.90
FHLB advances	17,733	434	2.45	%	66,121	2,424	3.67	%	93,669	3,203	3.43
Subordinated debentures	36,133	601	1.66	%	36,169	971	2.68	%	36,213	1,278	3.54
Other borrowings	50,877	222	0.44	%	53,155	373	0.70	%	56,464	530	0.94
Total interest-bearing liabilities	1,458,047	7,170	0.49	%	1,508,169	11,937	0.79	%	1,545,131	17,186	1.12
Non-interest bearing demand deposits	308,591	-			266,913	-			231,343	-	
Total including non- interest- bearing demand deposits	1,766,638	7,170	0.41	%	1,775,082	11,937	0.67	%	1,776,474	17,186	0.97
Other non-interest liabilities	20,547				21,276				17,983		
Total Liabilities	1,787,185				1,796,358				1,794,457		
Stockholders' equity	265,065				267,194				263,913		
Total liabilities and stockholders' equity	\$ 2,052,250				\$ 2,063,552				\$ 2,058,370		
Net interest income; interest rate spread (3)		\$ 69,243	3.65	%		\$ 70,661	3.64	%		\$ 71,360	3.69
Net interest margin (4)			3.76	%			3.81	%			3.88
Average interest-earning assets to average			126.6	%			123.5	%			119.0

interest-
bearing liabilities

(1) Interest on certain tax exempt loans (amounting to \$129,000, \$192,000 and \$231,000 in 2013, 2012 and 2011 respectively) and tax-exempt securities (\$2.9 million, \$2.9 million and \$2.5 million in 2013, 2012, and 2011) is not taxable for Federal income tax purposes. The average balance of such loans was \$4.2 million, \$4.9 million and \$5.5 million in 2013, 2012, and 2011 while the average balance of such securities was \$76.0 million, \$73.7 million and \$60.5 million in 2013, 2012, and 2011, respectively. In order to compare the tax-exempt yields on these assets to taxable yields, the interest earned on these assets is adjusted to a pre-tax equivalent amount based on the marginal corporate federal income tax rate of 35%.

(2) At December 31, 2013, the yields earned and rates paid were as follows: loans receivable, 4.30%; securities, 3.14%; FHLB stock, 4.00%; total interest-earning assets, 4.17%; deposits, 0.24%; FHLB advances, 2.36%; other borrowings, 0.29%, subordinated debentures, 1.67%; total including non-interest-bearing liabilities, 0.29%; and interest rate spread, 3.88%.

- (3) Interest rate spread is the difference in the yield on interest-earning assets and the cost of interest-bearing liabilities.
- (4) Net interest margin is net interest income divided by average interest-earning assets.

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The following table describes the extent to which changes in interest rates and changes in volume of interest-related assets and liabilities have affected First Defiance's tax-equivalent interest income and interest expense during the periods indicated. For each category of interest-earning assets and interest-bearing liabilities, information is provided on changes attributable to (i) changes in volume (change in volume multiplied by prior year rate), (ii) change in rate (change in rate multiplied by prior year volume), and (iii) total change in rate and volume. The combined effect of changes in both rate and volume has been allocated proportionately to the change due to rate and the change due to volume.

Table 4 Changes in Interest Rates and Volumes

	Year Ended December 31 2013 vs. 2012			2012 vs. 2011		
	Increase (decrease) due to rate	Increase (decrease) due to volume	Total increase (decrease)	Increase (decrease) due to rate	Increase (decrease) due to volume	Total increase (decrease)
Interest-Earning Assets						
Loans	\$ (7,000)	\$ 2,423	\$ (4,577)	\$ (8,198)	\$ 2,149	\$ (6,049)
Securities	565	(2,082)	(1,517)	(1,336)	1,571	235
Interest-earning deposits	8	(26)	(18)	8	(174)	(166)
FHLB stock	(24)	(49)	(73)	39	(7)	32
Total interest-earning assets	\$ (6,451)	\$ 266	\$ (6,185)	\$ (9,487)	\$ 3,539	\$ (5,948)
Interest-Bearing Liabilities						
Deposits	\$ (2,260)	\$ 4	\$ (2,256)	\$ (3,952)	\$ (54)	\$ (4,006)
FHLB advances	(620)	(1,370)	(1,990)	218	(997)	(779)
Subordinated Debentures	(369)	(1)	(370)	(305)	(2)	(307)
Notes Payable	(135)	(16)	(151)	(127)	(30)	(157)
Total interest-bearing liabilities	\$ (3,384)	\$ (1,383)	\$ (4,767)	\$ (4,166)	\$ (1,083)	\$ (5,249)
Increase (decrease) in net interest income			\$ (1,418)			\$ (699)

Provision for Loan Losses First Defiance's provision for loan losses was \$1.8 million for the year ended December 31, 2013 compared to \$10.9 million for December 31, 2012 and \$12.4 million for December 31, 2011.

Provisions for loan losses are charged to earnings to bring the total allowance for loan losses to a level deemed appropriate by management to absorb probable losses incurred in the loan portfolio. Factors considered by management include identifiable risk in the portfolios, historical experience, the volume and type of lending conducted by First Defiance, the amount of non-performing loans (including loans which meet the FASB ASC Topic

(2) At December 31, 2013, the yields earned and rates paid were as follows: loans receivable, 4.30%; securities, 3.98%.

310 definition of impaired), the amount of loans graded by management as substandard, doubtful, or loss, general economic conditions (particularly as they relate to First Defiance's market areas); and other factors related to the collectability of First Defiance's loan portfolio. See also Allowance for Loan Losses in Management's Discussion and Analysis and Note 7 to the audited financial statements.

Noninterest Income Noninterest income decreased by \$3.8 million or 11.1% in 2013 to \$30.6 million from \$34.4 million for the year ended December 31, 2012. That followed an increase of \$6.9 million or 24.9% in 2012 from \$27.5 million in 2011.

Service fees and other charges decreased to \$10.0 million for the year ended December 31, 2013 from \$10.8 million for 2012 and \$11.4 million for 2011. The decline in income in 2013 and 2012 from 2011 mainly related to a new rule issued by the Federal Reserve Board that became effective in the third quarter of 2010 as well as changes in customer behavior patterns. This rule prohibits financial institutions from charging consumers fees for paying overdrafts on automated teller machines and one-time debit card transactions, unless a consumer consents, or opts in, to the overdraft service for those types of transactions. Consumers must be provided a notice that explains the financial institution's overdraft services, including the fees associated with the service, and the consumer's choices.

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First Federal's overdraft privilege program generally provides for the automatic payment of modest overdraft limits on all accounts deemed to be in good standing when the account is accessed using paper-based check processing, a teller withdrawal, a point-of-sale terminal, an ACH transaction, an online banking or voice-response transfer, or an ATM. To be in good standing, an account must be brought to a positive balance within a 30-day period and have not excessively used the overdraft privilege program. Overdraft limits are established for all customers without discrimination using a risk assessment approach for each account classification. The approach includes a systematic review and evaluation of the normal deposit flows made to each account classification to establish reasonable and prudent negative balance limits that would be routinely repaid by normal, expected and reoccurring deposits. The risk assessment by portfolio approach assumes a minimal degree of undetermined credit risk associated with unidentified individual accounts that are overdrawn for 30 or more days. Consumer accounts overdrawn for more than 60 days are automatically charged off. Fees are charged as a one-time fee per occurrence, up to five charges per day, and the fee charged for an item that is paid is equal to the fee charged for a non-sufficient fund item that is returned.

Overdrawn balances, net of allowance for losses, are reflected as loans on First Defiance's balance sheet. The fees charged for this service are established based both on the return of processing costs plus a profit, and on the level of fees charged by competitors in the Company's market area for similar services. These fees are considered to be compensation for providing a service to the customer and therefore deemed to be noninterest income rather than interest income. Fee income recorded for the years ending December 31, 2013 and 2012 related to the overdraft privilege product, net of adjustments to the allowance for uncollectible overdrafts, were \$3.5 million and \$4.4 million, respectively. Accounts charged off are included in noninterest expense. The allowance for uncollectible overdrafts was \$22,000 at December 31, 2013 and \$4,000 at December 31, 2012.

Noninterest income also includes gains, losses and impairment on investment securities. In 2013, First Defiance realized a \$240,000 net loss on securities compared to a \$2.1 million net gain in 2012 and a \$216,000 net gain in 2011. In 2013, 2012 and 2011, First Defiance recognized other-than-temporary impairment ("OTTI") charges for certain impaired investment securities, where, in management's opinion, the value of the investment will not be recovered. The total OTTI charges in 2013 were \$337,000 and gains on sale or call of securities were \$97,000. Management recorded \$337,000 of OTTI on its investment of two trust preferred collateralized debt obligation ("CDOs") that were considered disallowed under the Interim Final Volcker Rule announced on January 14, 2014 and which required the Company to liquidate these securities. The Company held eight CDOs at December 31, 2013. Four of those CDOs were written down in full prior to January 1, 2010. The remaining four CDOs have a total amortized cost of \$3.4 million at December 31, 2013. Of these four, all were identified as having OTTI. In 2012, the total OTTI charges were \$5,000 and gains on sale or call of securities were \$2.1 million. The total OTTI charges in 2011 were \$2,000 and gains on sale or call of securities were \$218,000.

In October 2012, the Company executed a balance sheet restructuring strategy to enhance the Company's current and future profitability while increasing its capital ratios and protecting the balance sheet against rising rates. The strategy required taking an after tax loss of approximately \$260,000 through selling \$60.0 million in securities for a gain of \$1.6 million and paying off \$62.0 million in FHLB advances with a prepayment penalty of \$2.0 million.

Mortgage banking income includes gains from the sale of mortgage loans, fees for servicing mortgage loans for others an offset for amortization of mortgage servicing rights, and adjustments for impairment in the value of mortgage servicing rights. Mortgage banking income totaled \$8.4 million, \$9.7 million and \$6.4 million in 2013, 2012 and 2011, respectively. The \$1.2 million decrease in 2013 from 2012 is attributable to a \$4.9 million decrease in the gain on sale of loans, partially offset by a \$2.0 million positive change in the valuation adjustments on mortgage servicing rights and a decrease of \$1.5 million in mortgage servicing rights amortization expense. The positive valuation adjustment is a reflection of the increase in the fair value of certain sectors of the Company's portfolio of mortgage servicing rights. First Defiance originated \$291.7 million of residential mortgages for sale into the secondary market in 2013 compared with \$521.5 million in 2012. The \$3.3 million increase in mortgage banking income in 2012 from 2011 is attributable to a \$5.0 million increase in the gain on sale of loans, offset by a \$355,000

(2) At December 31, 2013, the yields earned and rates paid were as follows: loans receivable, 4.30%; securities, 3.10%

negative change in the valuation adjustments on mortgage servicing rights and an increase of \$1.4 million in mortgage servicing rights amortization expense. The negative change of \$355,000 in servicing rights valuation adjustments was due to an impairment charge of \$759,000 in 2012 compared with an impairment charge of \$404,000 in 2011. The impairment charge is a reflection of the decline in the fair value of certain sectors of the Company's portfolio of mortgage servicing rights. First Defiance originated \$521.5 million of residential mortgages for sale into the secondary market in 2012 compared with \$262.8 million in 2011. The balance of the mortgage servicing right valuation allowance stands at \$1.0 million at the end of 2013. See Note 8 to the financial statements.

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Insurance and investment commission income increased \$951,000 or 11.0% to \$9.6 million in 2013 from \$8.7 million in 2012 in large part due to an increase in contingent income of \$436,000. Contingent commissions are bonus payments received by First Defiance's insurance subsidiary for effective underwriting. Insurance and investment commission income increased \$1.6 million or 22.0% to \$8.7 million in 2012 from \$7.1 million in 2011 primarily due to the acquisition of PDI on July 1, 2011, allowing 2012 to be the first year to realize a full year's income from the acquisition, coupled with an increase in contingent income of \$179,000.

Noninterest Expense Total noninterest expense for 2013 was \$64.8 million compared to \$65.8 million for the year ended December 31, 2012 and \$62.8 million for the year ended December 31, 2011. The 2011 total includes \$234,000 of acquisition related charges. Noninterest expense, excluding the acquisition related charges in 2011 was \$62.5 million.

Compensation and benefits increased \$1.7 million or 5.3% in 2013 to \$34.3 million from \$32.6 million in 2012. The increase in compensation and benefits is due to merit increases and an increase in incentive expense of \$481,000 as a direct reflection of the improved financial performance of the Company as well as increased medical insurance costs. FDIC insurance costs decreased \$1.1 million or 40.0% to \$1.6 million from \$2.7 million in 2012. The FDIC decrease is due to the improvement in the Company's risk category in 2013. State franchise tax decreased \$172,000 or 6.9% in 2013 to \$2.3 million from \$2.5 million in 2012. Occupancy costs decreased \$816,000 or 10.8% in 2013 to \$6.8 million from \$7.6 million in 2012 due to an increase in deferred rent liabilities in 2012. Data processing increased \$465,000 or 10.0% in 2013 to \$5.1 million from \$4.7 million in 2012 from the Company's ongoing projects to enhance product offerings and gain efficiencies through the utilization of technology. The other noninterest expense category decreased \$1.2 million primarily due to a one-time penalty of \$2.0 million for the prepayment of \$62 million in FHLB advances as part of the Company's balance sheet restructure in 2012. This was partially offset by higher real estate owned expenses and an increase in management consulting.

Compensation and benefits increased \$1.0 million or 3.2% in 2012 to \$32.6 million from \$31.6 million in 2011. The increase in compensation and benefits was due to the full impact of the acquisition of PDI, and an increase in incentive expense of \$490,000 as a direct reflection of the improved financial performance of the Company. FDIC insurance costs decreased \$231,000 or 7.9% to \$2.7 million from \$2.9 million in 2011. The decrease reflects the change in the assessment rate calculation per the Dodd-Frank regulations. State franchise tax increased \$485,000 or 24.1% in 2012 to \$2.5 million from \$2.0 million in 2011. This increase is due to new rates being issued by the state of Ohio. Occupancy costs increased \$412,000 or 5.8% in 2012 to \$7.6 million from \$7.2 million in 2011 due to an increase in deferred rent liabilities. Data processing increased \$403,000 or 9.5% in 2012 to \$4.7 million from \$4.3 million in 2011 as the Company initiated projects to help gain efficiencies and utilize technology. The other noninterest expense category (including acquisition related charges in 2011) increased \$1.4 million primarily due to a one-time prepayment penalty of \$2.0 million in relation to the prepayment of \$62 million in FHLB advances as part of the Company's balance sheet restructure in 2012.

Income Taxes Income taxes amounted to \$9.3 million in 2013 compared to \$8.0 million in 2012 and \$6.7 million in 2011. The effective tax rates for those years were 29.4%, 30.0%, and 30.0%, respectively. The tax rate is lower than the statutory 35% tax rate for the Company mainly because of investments in tax-exempt securities. The earnings on tax-exempt securities are not subject to federal income tax. See Note 18 Income Taxes in the Notes to the financial statements for further details.

Concentrations of Credit Risk

Financial institutions such as First Defiance generate income primarily through lending and investing activities. The risk of loss from lending and investing activities includes the possibility that losses may occur from the failure of another party to perform according to the terms of the loan or investment agreement. This possibility is known as credit risk.

Lending or investing activities that concentrate assets in a way that exposes the Company to a material loss from any single occurrence or group of occurrences increases credit risk. Diversifying loans and investments to prevent concentrations of risks is one way a financial institution can reduce potential losses due to credit risk. Examples of asset concentrations would include multiple loans made to a single borrower and loans of inappropriate size relative to the total capitalization of the institution. Management believes adherence to its loan and investment policies allows it to control its exposure to concentrations of credit risk at acceptable levels. First Defiance's loan portfolio is concentrated geographically in its northwest Ohio, northeast Indiana and southeast Michigan market areas. Management has also identified lending for income-generating rental properties as an industry concentration. Total loans for income generating property totaled \$408.4 million at December 31, 2013, which represents 25.3% of the Company's loan portfolio. Management believes it has the skill and experience to manage any risks associated with this type of lending. Loans in this category are generally paying as agreed without any unusual or unexpected levels of delinquency. The delinquency rate in this category, which is any loan 30 days or more past due, was 0.82% at December 31, 2013. There are no other industry concentrations that exceed 10% of the Company's loan portfolio.

Liquidity and Capital Resources

The Company's primary source of liquidity is its core deposit base, raised through First Federal's branch network, along with wholesale sources of funding and its capital base. These funds, along with investment securities, provide the ability to meet the needs of depositors while funding new loan demand and existing commitments.

Cash generated from operating activities was \$42.6 million, \$31.9 million and \$38.5 million in 2013, 2012 and 2011, respectively. The adjustments to reconcile net income to cash provided by or used in operations during the periods presented consist primarily of proceeds from the sale of loans (less the origination of loans held for sale), the provision for loan losses, depreciation expense, the origination, amortization and impairment of mortgage servicing rights and increases and decreases in other assets and liabilities.

The primary investing activity of First Defiance is lending, which is funded with cash provided from operating and financing activities, as well as proceeds from payment on existing loans and proceeds from maturities of investment securities. On July 1, 2011, First Defiance completed the acquisition of Payak-Dubbs Insurance Agency, Inc. ("PDI"), a full insurance agency, for \$4.0 million in cash. Also in 2011, the Company purchased \$25.8 million in portfolio residential home loans.

In considering the more typical investing activities, during 2013, \$35.1 million and \$4.0 million was generated from the combination of maturity or pay-downs and the sale or call of available-for-sale investment securities, respectively and \$78.6 million was used by an increase in loans while \$49.2 million was used to purchase available-for-sale investment securities. During 2012, \$60.1 million and \$72.3 million was generated from the combination of maturity or pay-downs and the sale or call of available-for-sale investment securities, respectively, and \$65.0 million was used

(2) At December 31, 2013, the yields earned and rates paid were as follows: loans receivable, 4.30%; securities, 3.10%

by an increase in loans while \$91.5 million was used to purchase available-for-sale investment securities. During 2011, \$52.1 million and \$8.7 million was generated from the combination of maturity or pay-downs and the sale or call of available-for-sale investment securities, respectively and \$31.1 million was provided by a decline in loan growth while \$120.5 million was used to purchase available-for-sale investment securities.

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Principal financing activities include the gathering of deposits, the utilization of FHLB advances, and the sale of securities under agreements to repurchase such securities and borrowings from other banks. For 2013, total deposits increased by \$68.4 million. The amount of deposits acquired from out of market sources decreased in 2013 by \$2.0 million. For 2012, total deposits increased by \$71.3 million. The amount of deposits acquired from out of market sources decreased in 2012 by \$8.6 million. For 2011, total deposits increased by \$21.3 million. The amount of deposits acquired from out of market sources decreased in 2011 by \$31.1 million. In 2013, securities sold under repurchase arrangements increased by \$217,000 and the Company acquired \$10.0 million in FHLB advances and paid \$3.9 million in common stock dividends. In 2012, securities sold under repurchase arrangements decreased by \$8.7 million and the Company paid off \$69.0 million in FHLB advances primarily as a result of the balance sheet restructure and paid \$36.4 million as a result of redeeming its preferred stock both decreasing the financing activity. In 2011, securities sold under repurchase arrangements increased by \$4.1 million and the Company completed its common stock offering that increased the financing activities by \$19.9 million. For additional information about cash flows from First Defiance's operating, investing and financing activities, see the Consolidated Statements of Cash Flows included in the Consolidated Financial Statements.

At December 31, 2013, First Defiance had the following commitments to fund deposit, advance, borrowing obligations and post-retirement benefits:

Table 5 Contractual Obligations

Contractual Obligations	Maturity Dates by Period at December 31, 2013				
	Total (In Thousands)	Less than 1 year	1-3 years	4-5 years	After 5 years
Certificates of deposit	\$ 485,789	\$ 296,186	\$ 138,843	\$ 50,611	\$ 149
FHLB fixed advances including interest (1)	23,935	1,502	10,156	12,277	-
Subordinated debentures	36,083	-	-	-	36,083
Securities sold under repurchase agreements	51,919	51,919	-	-	-
Lease obligations	7,648	706	1,214	983	4,745
Post-retirement benefits	1,605	140	260	313	892
Total contractual obligations	\$ 606,979	\$ 350,453	\$ 150,473	\$ 64,184	\$ 41,869

(1) Includes principal payments of \$22,520 and interest payments of \$1,415

At December 31, 2013, First Defiance had the following commitments to fund loan or line of credit obligations:

Table 6 - Commitments

Commitments	Total Amounts Committed (In Thousands)	Amount of Commitment Expiration by Period			
		Less than 1 year	1-3 years	4-5 years	After 5 years
Fixed commitments to make loans	\$ 57,914	\$ 48,866	\$ 1,630	\$ 2,537	\$ 4,881
Variable commitments to make loans	59,632	39,120	3,095	438	16,979
Fixed unused lines of credit	18,047	6,746	5,648	5,651	2
Variable unused lines of credit	257,939	161,093	33,357	13,362	50,127
Total loan commitments	393,532	255,825	43,730	21,988	71,989
Standby letters of credit	17,680	3,490	13,750	440	-
Total Commitments	\$ 411,212	\$ 259,315	\$ 57,480	\$ 22,428	\$ 71,989

In addition to the above commitments, at December 31, 2013 First Defiance had commitments to sell \$12.1 million of loans to Freddie Mac, Fannie Mae, FHLB of Cincinnati or BB&T Mortgage.

To meet its obligations management can adjust the rate of savings certificates to retain deposits in changing interest rate environments; it can sell or securitize mortgage and non-mortgage loans; and it can turn to other sources of financing including FHLB advances, the Federal Reserve Bank, and brokered certificates of deposit. At December 31, 2013, First Defiance had \$428.7 million capacity under its agreements with the FHLB.

First Federal is subject to various capital requirements of the OCC. At December 31, 2013, First Federal had capital ratios that exceeded the standard to be considered "well capitalized." For additional information about First Defiance and First Federal's capital requirements, see Note 17 Regulatory Matters to the Consolidated December 31, 2013 Financial Statements.

Critical Accounting Policies

First Defiance has established various accounting policies that govern the application of accounting principles generally accepted in the United States in the preparation of its financial statements. The significant accounting policies of First Defiance are described in the footnotes to the consolidated financial statements. Certain accounting policies involve significant judgments and assumptions by management, which have a material impact on the carrying value of certain assets and liabilities; Management considers such accounting policies to be critical accounting policies. The judgments and assumptions used by management are based on historical experience and other factors, which are believed to be reasonable under the circumstances. Because of the nature of the judgments and assumptions made by management, actual results could differ from these judgments and estimates, which could have a material impact on the carrying value of assets and liabilities and the results of operations of First Defiance.

Allowance for Loan Losses - First Defiance believes the allowance for loan losses is a critical accounting policy that requires the most significant judgments and estimates used in preparation of its consolidated financial statements. In determining the appropriate estimate for the allowance for loan losses, management considers a number of factors relative to both specific credits in the loan portfolio and macro-economic factors relative to the economy of the United States as a whole and the economy of the northwest Ohio, northeast Indiana and southeast Michigan regions in which the Company does business.

(2) At December 31, 2013, the yields earned and rates paid were as follows: loans receivable, 4.30%; securities, 3.10%.

Factors relative to specific credits that are considered include a customer's payment history, a customer's recent financial performance, an assessment of the value of collateral held, knowledge of the customer's character, the financial strength and commitment of any guarantors, the existence of any customer or industry concentrations, changes in a customer's competitive environment and any other issues that may impact a customer's ability to meet his obligations.

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Economic factors that are considered include levels of unemployment and inflation, specific plant or business closings in the Company's market area, the impact of strikes or other work stoppages, the impact of weather or environmental conditions, especially relative to agricultural borrowers, and other matters that may have an impact on the economy as a whole.

In addition to the identification of specific customers who may be potential credit problems, management considers its historical losses, the results of independent loan reviews, an assessment of the adherence to underwriting standards, and other factors in providing for loan losses that have not been specifically classified. Management believes that the level of its allowance for loan loss is sufficient to cover the estimates loss incurred but not yet recognized on the loan portfolio. Refer to the section titled "Allowance for Loan Losses" and Note 2, Statement of Accounting Policies for a further description of the Company's estimation process and methodology related to the allowance for loan losses.

Valuation of Mortgage Servicing Rights - First Defiance believes the valuation of mortgage servicing rights is a critical accounting policy that requires significant estimates in preparation of its consolidated financial statements. First Defiance recognizes as separate assets the value of mortgage servicing rights, which are acquired through loan origination activities. First Defiance does not purchase any mortgage servicing rights.

Key assumptions made by management relative to the valuation of mortgage servicing rights include the stratification policy used in valuing servicing, assumptions relative to future prepayments of mortgages, the potential value of any escrow deposits maintained or ancillary income received as a result of the servicing activity and discount rates used to value the present value of a future cash flow stream. In assessing the value of the mortgage servicing rights portfolio, management utilizes a third party that specializes in valuing servicing portfolios. That third party reviews key assumptions with management prior to completing the valuation. Prepayment speeds are determined based on projected median prepayment speeds for 15 and 30 year mortgage backed securities. Those speeds are then adjusted up or down based on the size of the loan. The discount rate used in this analysis is the pretax yield generally required by purchasers of bulk servicing rights as of the valuation date. The value of mortgage servicing rights is especially vulnerable in a falling interest rate environment. Refer also to the section entitled Mortgage Servicing Rights and Note 2 - Statement of Accounting Policies, and Note 8 - Mortgage Banking, for a further description of First Defiance's valuation process, methodology and assumptions along with sensitivity analyses.

Valuation of Securities - First Defiance believes the valuation of certain securities is a critical accounting policy that requires significant estimates in preparation of its consolidated financial statements. This is pertaining to the Company's investment in certain trust preferred debt obligations securities ("CDOs"). As required by FASB ASC Topic 320, declines in the fair value of held-to-maturity and available-for-sale securities below their cost that are deemed to be other-than-temporary, are reflected in earnings as realized losses to the extent the impairment is related to credit losses. The amount of other-than-temporary impairment that does not relate to the credit losses is recognized in other comprehensive income. The fair values of these CDOs, which are backed by trust preferred securities issued by banks, thrifts and insurance companies, have a fair value of \$2.2 million as of December 31, 2013. Two of the collateralized debt obligations backed by insurance companies were disallowed under the Final Interim Volcker Rule that was announced January 14, 2014 and were classified as Level 1 in the fair value hierarchy at December 31, 2013 due to receiving a final selling price and subsequently being sold on January 15, 2014. The remaining two collateralized debt obligations are backed by financial institutions are allowed under the Final Interim Volcker Rule and classified as Level 3 in the fair value hierarchy based on the lack of observable market.

The market values for these securities (and any securities other than those issued or guaranteed by the U.S. Treasury) are very depressed relative to historical levels. Thus in today's market, a low market price for a particular bond may only provide evidence of stress in the credit markets in general versus being an indicator of credit problems with a particular issue.

(2) At December 31, 2013, the yields earned and rates paid were as follows: loans receivable, 4.30%; securities, 3.10%.

(2) At December 31, 2013, the yields earned and rates paid were as follows: loans receivable, 4.30%; securities, 3.10%.

Given the conditions in the debt markets today and the absence of observable transactions in the secondary and new issue markets, management has determined: 1) The few observable transactions and market quotations that are available are not reliable for the purpose of determining fair value at December 31, 2013; 2) An income valuation approach technique (present value technique) that maximizes the use of relevant observable inputs and minimizes the use of observable inputs will be equally or more representative of fair value than the market approach valuation used at the prior measurement dates and 3) The Company's CDOs will be classified within Level 3 of the fair value hierarchy because management determined that significant adjustments were required to determine fair value at the measurement date.

The Company's Level 3 CDO valuations were supported by an analysis prepared by an independent third party. Their approach to determining fair value involved several steps: 1) Detailed credit and structural evaluation of each piece of collateral in the CDO; 2) Collateral performance projections for each piece of collateral in the CDO (default, recovery and prepayment/amortization probabilities) and 3) Discounted cash flow modeling.

Goodwill - First Defiance has two reporting units: First Federal and First Insurance. At December 31, 2013, First Defiance had goodwill of \$61.5 million, including \$51.0 million in First Federal, representing 83% of total goodwill and \$10.5 million in First Insurance, representing 17% of total goodwill. The carrying value of goodwill is tested annually for impairment or more frequently if it is determined appropriate. The evaluation for impairment involves comparing the current estimated fair value of each reporting unit to its carrying value, including goodwill. If the current estimated fair value of a reporting unit exceeds its carrying value, no additional testing is required and impairment loss is not recorded. If the estimated fair value of a reporting unit is less than the carrying value, further valuation procedures are performed and could result in impairment of goodwill being recorded. Further valuation procedures would include allocating the estimated fair value to all assets and liabilities of the reporting unit to determine an implied goodwill value. If the implied value of goodwill of a reporting unit is less than the carrying amount of that goodwill, an impairment loss is recognized in an amount equal to that excess.

If for any future period First Defiance determines that there has been impairment in the carrying value of goodwill balances, First Defiance will record a charge to earnings, which could have a material adverse effect on net income, but not risk-based capital ratios.

First Defiance has core deposit and other intangible assets resulting from acquisitions which are subject to amortization. First Defiance determines the amount of identifiable intangible assets based upon independent core deposit and customer relationship analyses at the time of the acquisition. Intangible assets with finite useful lives are evaluated for impairment whenever events or changes in circumstances indicate that their carrying amount may not be recoverable. No events or changes in circumstances that would indicate that the carrying amount of any identifiable intangible assets may not be recoverable had occurred during the years ended December 31, 2013 and 2012.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

Asset/Liability Management

A significant portion of the Company's revenues and net income is derived from net interest income and, accordingly, the Company strives to manage its interest-earning assets and interest-bearing liabilities to generate an appropriate contribution from net interest income. Asset and liability management seeks to control the volatility of the Company's performance due to changes in interest rates. The Company attempts to achieve an appropriate relationship between rate sensitive assets and rate sensitive liabilities. First Defiance does not presently use off balance sheet derivatives to enhance its risk management.

First Defiance monitors interest rate risk on a monthly basis through simulation analysis that measures the impact changes in interest rates can have on net interest income. The simulation technique analyzes the effect of a presumed 100 basis point shift in interest rates (which is consistent with management's estimate of the range of potential interest rate fluctuations) and takes into account prepayment speeds on amortizing financial instruments, loan and deposit volumes and rates, non-maturity deposit assumptions and capital requirements. At December 31, 2013, the results of the simulation indicate that in an environment where interest rates rise 100 basis points over a 24 month period, First Defiance's net interest income would increase by 3.23% over the base case scenario. It should be noted that other areas of First Defiance's income statement, such as gains from sales of mortgage loans and amortization of mortgage servicing rights are also impacted by fluctuations in interest rates but are not considered in the simulation of net interest income.

The majority of First Federal's lending activities are in non-residential real estate and commercial loan areas. While such loans carry higher credit risk than residential mortgage lending, they tend to be more rate sensitive than residential mortgage loans. The balance of First Federal's non-residential and multi-family real estate loan portfolio was \$819.6 million, which was split between \$154.4 million of fixed-rate loans and \$665.2 million of adjustable-rate loans at December 31, 2013. The commercial loan portfolio increased to \$388.2 million, which is split between \$167.4 million of fixed-rate loans and \$220.8 million of adjustable-rate loans at December 31, 2013. Certain loans classified as adjustable have fixed rates for an initial term that may be as long as five years. The maturities on fixed-rate loans are generally less than seven years. First Federal also has significant balances of home equity and improvement loans (\$106.9 million at December 31, 2013) of which \$75.5 million fluctuate with changes in the prime lending rate and \$31.4 million of home equity and improvement loans have fixed rates. First Federal also has consumer loans (\$16.9 million at December 31, 2013) which tend to have a shorter duration than residential mortgage loans. Also, to limit its interest rate risk, as well as to provide liquidity, First Federal sells a majority of its fixed-rate mortgage originations into the secondary market.

In addition to the simulation analysis, First Federal also prepares an "economic value of equity" ("EVE") analysis. This analysis generally calculates the net present value of First Federal's assets and liabilities in rate shock environments that range from -400 basis points to +400 basis points. However, the likelihood of a decrease in interest rates beyond 100 basis points as of December 31, 2013 was considered to be remote given the current interest rate levels and therefore was not included in this analysis. The results of this analysis are reflected in the following table.

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(2) At December 31, 2013, the yields earned and rates paid were as follows: loans receivable, 4.30%; securities, 3.

Table 7 Economic Value of Equity Analysis

December 31, 2013

Change in Rates	Economic Value of Equity		% Change	Economic Value of Equity as % of Present Value of Assets			
	\$ Amount	\$ Change		Ratio		Change	
	(Dollars in Thousands)						
+ 400 bp	474,469	41,679	9.63	%	23.83	%	350 bp
+ 300 bp	467,691	34,901	8.06	%	23.10	%	277 bp
+ 200 bp	458,844	26,054	6.02	%	22.28	%	195 bp
+ 100 bp	447,701	14,911	3.45	%	21.38	%	105 bp
0 bp	432,790	-	-		20.33	%	
- 100 bp	413,917	(18,873)	(4.36)	%	19.19	%	(114) bp

December 31, 2012

Change in Rates	Economic Value of Equity		% Change	Economic Value of Equity as % of Present Value of Assets			
	\$ Amount	\$ Change		Ratio		Change	
	(Dollars in Thousands)						
+ 400 bp	415,094	46,835	12.72	%	21.49	%	356 bp
+ 300 bp	407,337	39,078	10.61	%	20.76	%	283 bp
+ 200 bp	398,150	29,891	8.12	%	19.97	%	204 bp
+ 100 bp	387,482	19,223	5.22	%	19.12	%	119 bp
0 bp	368,259	-	-		17.93	%	
- 100 bp	343,745	(24,514)	(6.66)	%	16.57	%	(136) bp

Based on the above analysis, in the event of a 200 basis point increase in interest rates as of December 31, 2013, First Federal would experience a 6.02% increase in its economic value of equity. During periods of rising rates, the value of monetary assets declines. Conversely, during periods of falling rates, the value of monetary assets increases. It should be noted that the amount of change in value of specific assets and liabilities due to changes in rates is not the same in a rising rate environment as in a falling rate environment. Based on the EVE analysis, the change in the economic value of equity in both rising and falling rate environments is relatively low because both its assets and liabilities have relatively short durations. The average duration of its assets at December 31, 2013 was 1.59 years while the average duration of its liabilities was 2.91 years.

In evaluating First Federal's exposure to interest rate risk, certain shortcomings inherent in each of the methods of analysis presented must be considered. For example, although certain assets and liabilities may have similar maturities or periods to repricing, they may react in different degrees to changes in market interest rates. Also, the interest rates on certain types of assets and liabilities may fluctuate in advance of changes in market rates while interest rates on other types of financial instruments may lag behind current changes in market rates. Furthermore, in the event of changes in rates, prepayments and early withdrawal levels could differ significantly from the assumptions in calculating the table and the results therefore may differ from those presented.

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Item 8. Financial Statements and Supplementary Data

Management's Report on Internal Control Over Financial Reporting

The management of First Defiance Financial Corp. is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rules 13a-15(f). Under the supervision and with the participation of management, we conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework in the 1992 Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

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

Based on our evaluation under the framework in the 1992 Internal Control Integrated Framework, management concluded that our internal control over financial reporting was effective as of December 31, 2013.

Crowe Horwath LLP, the independent registered public accounting firm that audited the consolidated financial statements of the Company included in this Annual Report on Form 10-K, has issued a report on the effectiveness of the Company's internal control over financial reporting as of December 31, 2013. The report, which expresses an unqualified opinion on the effectiveness of the Company's internal control over financial reporting as of December 31, 2013, is included below.

Donald P. Hileman
Executive Vice President and
Chief Executive Officer

Kevin T. Thompson
Executive Vice President and
Chief Financial Officer

Report of Independent Registered Public Accounting Firm

We have audited the accompanying consolidated statements of financial condition of First Defiance Financial Corp. (the Company) as of December 31, 2013 and 2012 and the related consolidated statements of income, comprehensive income, changes in stockholders' equity and cash flows for each of the three years in the period ended December 31, 2013. We also have audited First Defiance Financial Corp.'s internal control over financial reporting as of December 31, 2013, based on criteria established in the 1992 Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for these financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on these financial statements and an opinion on the Company's internal control over financial reporting based on our audits.

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

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

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of First Defiance Financial Corp. as of December 31, 2013 and 2012, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2013 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, First Defiance Financial Corp. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2013, based on criteria established in the 1992 Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

Based on the above analysis, in the event of a 200 basis point increase in interest rates as of December 31, 2013,

Crowe Horwath LLP
South Bend, Indiana
February 28, 2014

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First Defiance Financial Corp

Consolidated Statements of Financial Condition (continued)

December 31
2013 2012

(Dollars In Thousands, except share
and per share data)

Liabilities and stockholders' equity

Liabilities:

Deposits:

Noninterest-bearing	\$ 348,943	\$ 315,132
Interest-bearing	1,386,849	1,352,340
Total	1,735,792	1,667,472
Advances from the Federal Home Loan Bank	22,520	12,796
Securities sold under agreements to repurchase and other	51,919	51,702
Subordinated debentures	36,083	36,083
Advance payments by borrowers	1,519	1,473
Other liabilities	17,168	19,294
Total liabilities	1,865,001	1,788,820

Commitments and Contingent (Note 6)

Stockholders' equity:

Preferred stock, \$.01 par value per share: 37,000 shares
authorized;

no shares issued

Preferred stock, \$.01 par value per share:

4,963,000 shares authorized; no shares issued

Common stock, \$.01 par value per share:

25,000,000 shares authorized; 12,735,313 and 12,739,496
shares issued 127 127

and 9,719,521 and 9,729,466 shares outstanding, respectively

Common stock warrant 878 878

Additional paid-in capital 136,403 136,046

Accumulated other comprehensive income, net of tax of \$294
and \$2,301, 545 4,274

respectively

Retained earnings 182,290 164,103

Treasury stock, at cost, 3,015,792 and 3,010,030 shares
respectively (48,096) (47,300)

Total stockholders' equity 272,147 258,128

Total liabilities and stockholders' equity \$ 2,137,148 \$ 2,046,948

See accompanying notes.

Based on the above analysis, in the event of a 200 basis point increase in interest rates as of December 31, 2013, 118

FIRST DEFIANCE FINANCIAL CORP.
Consolidated Statements of Income
(Amounts in Thousands, except per share data)

	Years Ended December 31		
	2013	2012	2011
Interest Income			
Loans	\$ 68,077	\$ 72,621	\$ 78,648
Investment securities:			
Taxable	2,695	4,241	4,571
Tax-exempt	2,901	2,882	2,515
Interest-bearing deposits	282	300	466
FHLB stock dividends	826	899	867
Total interest income	74,781	80,943	87,067
Interest Expense			
Deposits	5,913	8,169	12,175
Federal Home Loan Bank advances and other	434	2,424	3,203
Subordinated debentures	601	971	1,278
Securities sold under agreement to repurchase	222	373	530
Total interest expense	7,170	11,937	17,186
Net interest income	67,611	69,006	69,881
Provision for loan losses	1,824	10,924	12,434
Net interest income after provision for loan losses	65,787	58,082	57,447
Noninterest Income			
Service fees and other charges	10,045	10,779	11,387
Mortgage banking income	8,443	9,665	6,437
Insurance commissions	9,627	8,676	7,109
Gain on sale of non-mortgage loans	101	70	361
Gain (loss) on sale or call of securities	97	2,139	218
Other-than-temporary impairment (OTTI) losses on investment securities			
Total gains (impairment losses) on investment securities	(337)	(31)	(44)
Losses recognized in other comprehensive income	-	26	42
Net impairment loss recognized in earnings	(337)	(5)	(2)
Trust income	761	616	599
Income from bank owned life insurance	883	924	929
Other noninterest income	950	1,510	478
Total noninterest income	30,570	34,374	27,516
Noninterest Expense			
Compensation and benefits	34,301	32,566	31,554
Occupancy	6,762	7,578	7,166
FDIC insurance	1,616	2,691	2,922
Data processing	5,125	4,660	4,257
Acquisition related charges	-	-	234
Other noninterest expense	17,040	18,285	16,631

Based on the above analysis, in the event of a 200 basis point increase in interest rates as of December 31, 2013, 120

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Total noninterest expense	64,844	65,780	62,764
Income before income taxes	31,513	26,676	22,199
Federal income taxes	9,278	8,012	6,665
Net Income	\$ 22,235	\$ 18,664	\$ 15,534
Dividends Accrued on Preferred Shares	\$ -	\$ (900)	\$ (1,850)
Accretion on Preferred Shares	\$ -	\$ (359)	\$ (178)
Redemption of Preferred Shares	\$ -	\$ 642	\$ -
Net Income Applicable to Common Shares	\$ 22,235	\$ 18,047	\$ 13,506
Earnings per common share:			
Basic	\$ 2.28	\$ 1.86	\$ 1.44
Diluted	\$ 2.19	\$ 1.81	\$ 1.42
Dividends declared per common share	\$ 0.40	\$ 0.20	\$ 0.05

See accompanying notes

FIRST DEFIANCE FINANCIAL CORP.
Consolidated Statements of Comprehensive Income
(Amounts in Thousands)

	For the Years Ended December 31		
	2013	2012	2011
	(In Thousands)		
Net income	\$ 22,235	\$ 18,664	\$ 15,534
Change in securities available-for-sale (AFS):			
Unrealized holding gains (losses) on available-for-sale securities arising during the period	(6,309)	2,360	7,404
Reclassification adjustment for (gains) losses realized in income	(97)	(2,139)	(218)
Other-than-temporary impairment losses on AFS securities realized in income	337	5	2
Net unrealized gains (losses)	(6,069)	226	7,188
Income tax effect	2,124	(79)	(2,516)
Net of tax amount	(3,945)	147	4,672
Change in unrealized gain on postretirement benefit:			
Net gain (loss) on defined benefit postretirement medical plan realized during the period	287	148	(537)
Net amortization and deferral	46	51	25
Net gain (loss) activity during the period	333	199	(512)
Income tax effect	(117)	(69)	179
Net of tax amount	216	130	(333)
Total other comprehensive income (loss)	(3,729)	277	4,339
Comprehensive income	\$ 18,506	\$ 18,941	\$ 19,873

FIRST DEFIANCE FINANCIAL CORP.
Consolidated Statements of Changes in Stockholders' Equity
(In Thousands, except number of shares)

	Preferred Stock	Common Stock	Common Stock Warrant	Additional Paid-In Capital	Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Treasury Stock	Total Stockholder's Equity
Balance at December 31, 2010	\$ 36,463	\$ 127	\$ 878	\$ 140,845	\$ (342)	\$ 134,988	\$ (72,628)	\$ 240,331
Net income						15,534		15,534
Other comprehensive income					4,339			4,339
Stock option expense				144				144
850 stock options exercised, with no income tax benefit						(3)	14	11
1,600,800 shares issued capital stock				(5,297)			25,156	19,859
Restricted share activity under stock incentive plans				136			75	211
2,085 shares issued direct purchases				(3)			32	29
Preferred stock dividends accrued						(1,850)		(1,850)
Accretion on preferred shares	178					(178)		-
Common stock dividends declared						(481)		(481)
Balance at December 31, 2011	\$ 36,641	\$ 127	\$ 878	\$ 135,825	\$ 3,997	\$ 148,010	\$ (47,351)	\$ 278,127
Net income						18,664		18,664
Other comprehensive income					277			277
Stock option expense				104				104

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500 shares issued under stock option plan, with no income tax benefit						(4)	8	4
Restricted share activity under stock incentive Plans				116			30	146
836 shares issued direct purchases				1			13	14
Preferred stock dividends accrued						(900)		(900)
Accretion on preferred shares	359					(359)		-
16,560 shares purchased in Treasury auction	(16,560)					618		(15,942)
20,440 shares purchased in open market	(20,440)					24		(20,416)
Common stock dividends declared						(1,950)		(1,950)
Balance at December 31, 2012	\$ -	\$ 127	\$ 878	\$ 136,046	\$ 4,274	\$ 164,103	\$ (47,300)	\$ 258,128
Net income						22,235		22,235
Other comprehensive loss					(3,729)			(3,729)
Stock option expense				44				44
35,147 shares issued under stock option plan, with \$54 in income tax benefit				(34)		(97)	481	350
Restricted share activity under stock incentive Plans				327		(44)	500	783
2,768 shares issued direct purchases				20			44	64
							(1,821)	(1,821)

70,966 shares
repurchased
Common stock
dividends
declared

(3,907)

(3,907)

Balance at

December 31,	\$ -	\$ 127	\$ 878	\$ 136,403	\$ 545	\$ 182,290	\$ (48,096)	\$ 272,147
2013								

See accompanying notes

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FIRST DEFIANCE FINANCIAL CORP.
Consolidated Statements of Cash Flows
(Amounts in Thousands)

	Years Ended December 31		
	2013	2012	2011
Operating Activities			
Net income	\$ 22,235	\$ 18,664	\$ 15,534
Adjustments to reconcile net income to net cash provided by operating activities:			
Provision for loan losses	1,824	10,924	12,434
Provision for depreciation	3,110	3,416	3,436
Net amortization of premium and discounts on loans, securities, deposits and debt obligations	1,235	1,497	396
Amortization of mortgage servicing rights	2,098	3,562	2,169
Net (recovery) impairment of mortgage servicing rights	(1,261)	759	404
Amortization of intangibles	1,241	1,413	1,442
Gain on sale of loans	(5,817)	(10,669)	(5,968)
Loss on sale or disposals of property, plant and equipment	1	179	59
Loss on sale or write-down of REO	883	427	947
OTTI losses on investment securities	337	5	2
(Gain) loss on sale or call of securities	(97)	(2,139)	(218)
Change in deferred taxes	1,519	779	2,839
Proceeds from sale of loans held for sale	308,260	520,376	263,336
Stock option expense	44	104	144
Restricted stock unit expense	783	146	211
Origination of loans held for sale	(294,941)	(521,464)	(262,825)
Income from bank owned life insurance	(883)	(924)	(929)
Change in interest receivable and other assets	1,327	17	2,961
Change in accrued interest and other liabilities	(2,535)	4,838	2,365
Net cash provided by operating activities	39,363	31,910	38,739
Investing Activities			
Proceeds from maturities, calls and paydowns of held-to-maturity securities	121	152	178
Proceeds from maturities, calls and paydowns of available-for-sale securities	35,072	60,057	52,097
Proceeds from sale of available-for-sale securities	4,027	72,262	8,719
Proceeds from sale of REO	2,899	3,444	9,630
Proceeds from sale of office properties and equipment	-	10	17
Purchases of available-for-sale securities	(49,230)	(91,513)	(120,499)
Purchases of office properties and equipment	(2,045)	(3,223)	(2,041)
Investment in bank owned life insurance	-	(5,000)	-
Proceeds from FHLB stock redemption	1,305	-	357

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Net cash paid in Payak-Dubbs acquisition	-	-	(3,914)
Purchase of portfolio mortgage loans	(4,545)	-	(25,842)
Proceeds from sale of non-mortgage loans	13,369	4,644	9,212
Net decrease (increase) in loans receivable	(70,845)	(65,005)	31,137
Net cash provided by (used) in investing activities	(69,872)	(24,172)	(40,949)

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FIRST DEFIANCE FINANCIAL CORP.
Consolidated Statements of Cash Flows (continued)
(Amounts in Thousands)

	Years Ended December 31		
	2013	2012	2011
Financing Activities			
Net increase (decrease) in deposits	68,368	71,318	21,314
Repayment of Federal Home Loan Bank long-term advances	(276)	(69,045)	(35,044)
Proceeds from Federal Home Loan Bank long-term advances	10,000	-	-
Cash paid for redemption of preferred stock	-	(36,358)	-
Increase (decrease) in securities sold under repurchase agreements	217	(8,684)	4,139
Cash dividends paid on common stock	(3,907)	(1,950)	(481)
Cash dividends paid on preferred stock	-	(1,136)	(1,850)
Net cash received from common stock issuance	-	-	19,859
Net cash paid for repurchase of common stock	(1,821)	-	-
Proceeds from exercise of stock options	350	4	11
Proceeds from treasury stock sales	64	14	29
Net cash (used) provided by financing activities	72,995	(45,837)	7,977
Increase (decrease) in cash and cash equivalents	42,486	(38,099)	5,767
Cash and cash equivalents at beginning of period	136,832	174,931	169,164
Cash and cash equivalents at end of period	\$ 179,318	\$ 136,832	\$ 174,931
Supplemental cash flow information:			
Interest paid	\$ 7,179	\$ 12,251	\$ 17,464
Income taxes paid	\$ 10,500	\$ 4,000	\$ 4,875
Transfers from loans to other real estate owned and other assets held for sale	\$ 5,836	\$ 4,048	\$ 4,614
Transfer from loans held for sale to loans	\$ 3,231	\$ -	\$ 7,596
Securities traded but not yet settled	\$ 742	\$ 405	\$ -

See accompanying notes.

Notes to the Consolidated Financial Statements

1. Basis of Presentation

First Defiance Financial Corp. (First Defiance or the Company) is a unitary thrift holding company that conducts business through its three wholly owned subsidiaries, First Federal Bank of the Midwest (First Federal), First Insurance Group of the Midwest, Inc. (First Insurance), and First Defiance Risk Management, Inc. (First Defiance Risk Management). All significant intercompany transactions and balances are eliminated in consolidation.

First Federal is primarily engaged in attracting deposits from the general public through its offices and using those and other available sources of funds to originate loans primarily in the counties in which its offices are located. First Federal's traditional banking activities include originating and servicing residential, commercial and consumer loans and providing a broad range of depository, trust and wealth management services. First Insurance is an insurance agency that does business in the Defiance, Bryan, Bowling Green, Maumee and Oregon, Ohio areas, offering property and casualty, and group health and life insurance products. First Defiance Risk Management was incorporated on December 20, 2012, as a wholly-owned insurance company subsidiary of the Company to insure the Company and its subsidiaries against certain risks unique to the operations of the Company and for which insurance may not be currently available or economically feasible in today's insurance marketplace.

2. Statement of Accounting Policies

Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates. Significant areas where First Defiance uses estimates are the valuation of certain investment securities, the determination of the allowance for loan losses, the valuation of mortgage servicing rights and goodwill, the determination of unrecognized income tax benefits, and the fair value of financial instruments.

Earnings Per Common Share

Basic earnings per common share is computed by dividing net income applicable to common shares (net income less dividend requirements for preferred stock, accretion of preferred stock discount and redemption of preferred stock) by the weighted average number of shares of common stock outstanding during the period. All outstanding unvested share-based payment awards that contain rights to nonforfeitable dividends are considered participating securities for the calculation. Diluted earnings per common share include the dilutive effect of additional potential common shares issuable under stock options, warrants, restricted stock awards and stock grants. Also see Note 4.

Comprehensive Income

Comprehensive income (loss) consists of net income and other comprehensive income (loss). Other comprehensive income includes unrealized gains and losses on available-for-sale securities and the net unrecognized actuarial losses and unrecognized prior service costs associated with the Company's Defined Benefit Postretirement Medical Plan. All items included in other comprehensive income are reported net of tax. See also Notes 5 and 16 and the Statements of Comprehensive Income.

Cash Flows

Cash and cash equivalents include amounts due from banks and overnight investments with the Federal Home Loan Bank (FHLB) and the Federal Reserve Bank (FRB). Cash and amounts due from depository institutions include required balances on hand or on deposit at the FHLB and Federal Reserve of approximately \$2,295,000 and \$4,200,000, respectively, at December 31, 2013 to meet regulatory reserve and clearing requirements. Net cash flows are reported for customer loan and deposit transactions, interest bearing deposits in other financial institutions and repurchase agreements.

Investment Securities

Management determines the appropriate classification of debt securities at the time of purchase and evaluates such designation as of each balance sheet date. Debt securities are classified as held-to-maturity when First Defiance has the positive intent and ability to hold the securities to maturity and are reported at cost, adjusted for premiums and discounts that are recognized in interest income using the interest method over the period to maturity.

Debt securities not classified as held-to-maturity and equity securities are classified as available-for-sale. Available-for-sale securities are stated at fair value, with the unrealized gains and losses, net of tax, reported in other comprehensive income (loss) until realized. Realized gains and losses are included in gains (losses) on securities or other-than-temporary impairment losses on securities. Realized gains and losses on securities sold are recognized on the trade date based on the specific identification method.

Interest income includes amortization of purchase premiums and discounts. Premiums and discounts are amortized on the level-yield method without anticipating prepayments, except for mortgage-backed securities where prepayments are expected. Securities with unrealized losses are reviewed quarterly to determine if value impairment is other than-temporary. In performing this review management considers the length of time and extent that fair value has been less than cost, the financial condition of the issuer, the impact of changes in market interest rates on market value and whether the Company intends to sell or it would be more than likely required to sell the securities prior to their anticipated recovery. If either of the criteria regarding intent or requirement to sell is met, the entire difference between amortized cost and fair value is recognized as impairment through earnings. For debt securities that do not meet the aforementioned criteria, the amount of impairment is split into two components as follows: 1) OTTI related to credit loss, which must be recognized in the income statement and 2) other-than-temporary impairment (OTTI) related to other factors, which is recognized in other comprehensive income. The credit loss is defined as the difference between the present value of the cash flows expected to be collected and the amortized cost basis. For equity securities, the entire amount of impairment is recognized through earnings.

FHLB Stock

As a member of the FHLB System, First Federal is required to own stock of the FHLB of Cincinnati in an amount principally equal to 0.15% of total assets plus an amount of at least 2% but no more than 4% of its non-grandfathered mission asset activity (as defined in the FHLB's regulations). First Federal is permitted to own stock in excess of the minimum requirement. FHLB stock is a restricted equity security that does not have a readily determinable fair value and is carried at cost. It is evaluated for impairment based upon the ultimate recovery of par value. Both cash and stock dividends are reported as income. At December 31, 2013, the Company holds \$19.3 million at the FHLB of Cincinnati and \$10,000 at the FHLB of Indianapolis.

Loans Receivable

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are reported at the principal amount outstanding, net of deferred loan fees and costs, purchase premiums and discounts and the allowance for loan losses. Deferred fees net of deferred incremental loan origination costs, are amortized to interest income generally over the contractual life of the loan using the interest method without anticipating prepayments. The recorded investment in loans includes accrued interest receivable and net deferred fees and costs and undisbursed loan amounts.

Mortgage loans originated and intended for sale in the secondary market are classified as loans held for sale and are carried at the lower of aggregate cost or fair value, as determined by outstanding commitments from investors. Net unrealized losses, if any, are recorded as a valuation allowance and charged to earnings. Mortgage loans held for sale are generally sold with servicing rights retained. The carrying value of mortgage loans sold is reduced by the amount allocated to the servicing right. Gains or losses on sales of mortgage loans are based on the difference between the selling price and the carrying value of the related loan sold.

During 2013, 2012 and 2011, the Company realized losses totaling \$597,000, \$73,000 and \$413,000 pertaining to loans sold to Fannie Mae and Freddie Mac but repurchased due to underwriting issues. Repurchase losses are recognized when the Company determines they are probable and estimable. \$67,000 was accrued at December 31, 2013 while no amount was accrued at December 31, 2012 and 2011 for such losses.

Interest receivable is accrued on loans and credited to income as earned. The accrual of interest on loans 90 days delinquent or impaired is discontinued when, in management's opinion, the borrower may be unable to meet payments as they become due. For these loans, interest accrual is only to the extent cash payments are received. The accrual of interest on these loans is generally resumed after a pattern of repayment has been established and the collection of principal and interest is reasonably assured.

Acquired Loans

Valuation allowances for all acquired loans subject to FASB ASC Topic 310 reflect only those losses incurred after acquisition that is, the present value of cash flows expected at acquisition that are not expected to be collected.

The Company acquires loans individually and in groups or portfolios. At acquisition, the Company reviews each loan to determine whether there is evidence of deterioration of credit quality since origination and if it is probable that it will be unable to collect all amounts due according to the loan's contractual terms. If both conditions exist, the Company determines whether each such loan is to be accounted for individually or whether such loans will be assembled into pools of loans based on common risk characteristics (credit score, loan type and date of origination). The Company considers expected prepayments, and estimates the amount and timing of undiscounted expected principal, interest, and other cash flows (expected at acquisition) for each loan and subsequently aggregated pool of loans.

The Company determines the excess of the loan's or pool's scheduled contractual principal and contractual interest payments over all cash flows expected at acquisition as an amount that should not be accreted (nonaccretable difference). The remaining amount representing the excess of the loan's cash flows expected to be collected over the amount paid is accreted into interest income over the remaining life of the loan or pool (accretable yield).

Over the life of the loan or pool, the Company continues to estimate cash flows expected to be collected, and evaluates whether the present value of its loans determined using the effective interest rates has decreased and, if so, recognizes a loss. The present value of any subsequent increase in the loan's or pool's actual cash flows or cash flows expected to be collected is used first to reverse any existing valuation allowance for that loan or pool. For any

remaining increases in cash flows expected to be collected, the Company adjusts the amount of accretable yield recognized on a prospective basis over the loan's or pool's remaining life.

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Allowance for Loan Losses

The allowance for loan losses is maintained at a level believed adequate by management to absorb probable incurred losses in the loan portfolio and is based on the size and current risk characteristics of the loan portfolio, an assessment of individual problem loans, actual loss experience, current economic events in specific industries and geographical areas and other pertinent factors, including general economic conditions. Determination of the allowance is inherently subjective as it requires significant estimates, including the amounts and timing of expected future cash flows on impaired loans, estimated losses on pools of homogeneous loans based on historical loss experience and consideration of economic trends, all of which may be susceptible to significant change. 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.

During 2012, First Defiance changed the process used to calculate the historical loss percentages included in the general allocation. Previously, all charge offs processed against loans were included in the period they were incurred with no consideration given to when a specific reserve was established. During 2012, the historical loss calculation included specific reserves on collaterally dependent impaired loans in the quarter in which the loss was identified and included charge-offs on loans that did not previously have specific reserves.

During 2013, management elected to return to using a three year look-back period in calculating the historical loss ratio. Management is not certain that the relatively low levels of charge offs incurred in the recent quarters are sustainable given the continued low levels of economic growth in the Company's markets warranting the need to return to a three year look-back. All quarters are given equal weighting in the calculation, which is unchanged from 2012.

Loan losses are charged off against the allowance when in management's estimation it is unlikely that the loan will be collected, while recoveries of amounts previously charged off are credited to the allowance. A provision for loan loss is charged to operations based on management's periodic evaluation of the factors previously mentioned, as well as other pertinent factors in order to maintain the allowance for loan losses at the level deemed adequate by management. The determination of whether a loan is considered past due or delinquent is based on the contractual payment terms. Loans are considered past due when the contractual amounts due with respect to principal and interest are not received within 30 days of the contractual due date. All loans are placed on nonaccrual status at 90 days past due unless the loan is adequately secured and is in process of collection. Any loan in the portfolio may be placed on nonaccrual status prior to becoming 90 days past due when collection of principal or interest is in doubt.

The allowance consists of specific and general components. The specific component relates to loans that are individually classified as impaired. Impaired loans have been recognized in conformity with FASB ASC Topic 310.

A loan is impaired when, based on current information and events, it is probable that the Company will be unable to collect all amounts due according to the contractual terms of the loans agreement. Loans, for which terms have been modified and for which the borrower is experiencing financial difficulties, are considered troubled debt restructurings and classified as impaired. A cash flow analysis of the net present value is performed and an allowance may be established based on the outcome of that analysis, or if the loan is deemed to be collateral dependent an allowance is established based on the fair value of collateral. All modifications are reviewed by the First Federal's senior loan committee to determine whether or not the modification constitutes a troubled debt restructure. Commercial and commercial real estate loans are individually evaluated for impairment. If a loan is impaired, a portion of the allowance is allocated so that the loan is reported net of the allowance allocation which is determined based on the present value of estimated future cash flows using the loan's existing rate or at the fair value of collateral if repayment is expected solely from the collateral. Large groups of smaller balance homogeneous loans, such as consumer and residential real estate loans, are collectively evaluated for impairment, and accordingly, they are not separately identified for impairment disclosures.

The general component covers non-impaired loans and is based on historical loss experience adjusted for current factors. The historical loss experience is determined by portfolio segment and is based on the actual loss history experienced by the Company over the most recent three years. Loss experience is adjusted for other economic factors based on the identified risks, credit related or trends present for each portfolio segment. These economic 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. The following portfolio segments have been identified:

Commercial Real Estate Loans (consisting of multi-family residential and non-residential): Commercial real estate loans are subject to underwriting standards and processes similar to commercial and industrial loans. These loans are viewed primarily as cash flow loans and the repayment of these loans is largely dependent on the successful operation of the property. Loan performance may be adversely affected by factors impacting the general economy or conditions specific to the real estate market such as geographic location and/or property type.

Commercial Loans: Commercial credit is extended primarily to middle market customers. Such credits are typically comprised of working capital loans, loans for physical asset expansion, asset acquisition loans and other business loans. Loans to closely held businesses will generally be guaranteed in full or for a meaningful amount by the businesses' principal owners. Commercial loans are made based primarily on the historical and projected cash flow of the borrower and secondarily on the underlying collateral provided by the borrower. The cash flows of borrowers, however, may not behave as forecasted and collateral securing loans may fluctuate in value due to economic or individual performance factors. Minimum standards and underwriting guidelines have been established for all commercial loan types.

Consumer: Consumer loans are generally made to borrowers for a specific consumer purchase and are made based on their ability to repay with their current debt to income as well as the underlying collateral value of the item being purchased. Credit scores are part of the decision process of whether or not credit is extended. Minimum standards and underwriting guidelines have been established for all consumer loan types.

1-4 Family Residential Real Estate: 1-4 family residential real estate loans can be categorized two different ways. One part of this portfolio is owner occupied and are made based primarily on the ability of the individual borrower to support the payments as well as the payments of any other debt the borrower may have outstanding at the time the loan is made. The other part of this portfolio is non-owner occupied income producing property and is made primarily based on the cash flow stream from rental income as well as the cash flow support from the borrower's unrelated cash flow. Both types of loans have a secondary repayment source of the underlying collateral and generally the loans are not extended at higher than an 80% LTV. Minimum standards and underwriting guidelines have been established for all 1-4 family residential real estate loan types.

Construction: The Company defines construction loans as loans where the loan proceeds are controlled by the Company and used exclusively for the improvement of real estate in which the Company holds a mortgage.

Home Equity and Improvement: Home Equity and Improvement loans are made to borrowers based on their ability to repay with their current debt to income as well as the underlying collateral value of the real estate taken as security. Minimum standards and underwriting guidelines have been established for all 1-4 family residential real estate loan types.

Consumer, 1-4 family residential real estate (including construction) and home equity and improvement loans are subject to adverse employment conditions in the local economy which could increase default rate on loans.

Servicing Rights

Servicing rights are recognized separately when they are acquired through sales of loans. Servicing rights are initially recorded at fair value with the income statement effect recorded in gains on sales of loans. Fair value is based on market prices for comparable mortgage servicing contracts, when available, or alternatively, is based on a valuation model that calculates the present value of estimated future net servicing income. The valuation model incorporates assumptions that market participants would use in estimating future net servicing income, such as the cost to service, the discount rate, the custodial earnings rate, an inflation rate, ancillary income, prepayment speeds and default rates and losses. The Company compares the valuation model inputs and results to published industry data in order to validate the model results and assumptions. All classes of servicing assets are subsequently measured using the amortization method which requires servicing rights to be amortized into non-interest income in proportion to, and over the period of, the estimated future net servicing income of the underlying loans, driven, generally, by changes in market interest rates.

Servicing assets are evaluated for impairment based upon the fair value of the rights as compared to carrying amount. Impairment is determined by stratifying rights into groupings based on predominant risk characteristics, such as interest rate, loan type and investor type. Impairment is recognized through a valuation allowance for an individual grouping, to the extent that fair value is less than the carrying amount. If the Company later determines that all or a portion of the impairment no longer exists for a particular grouping, a reduction of the allowance may be recorded as an increase to income. Changes in valuation allowances are reported with mortgage banking income on the income statement. The fair values of servicing rights are subject to significant fluctuations as a result of changes in estimated and actual prepayment speeds and default rates and losses.

Servicing fee income, which is reported on the income statement with mortgage banking income, is recorded for fees earned for servicing loans. The fees are based on a contractual percentage of the outstanding principal, or a fixed amount per loan, and are recorded as income when earned. The amortization of mortgage servicing rights is netted against loan servicing fee income. Servicing fees totaled \$3.6 million, \$3.4 million and \$3.4 million for the years ended December 31, 2013, 2012 and 2011. Late fees and ancillary fees related to loan servicing are not material. See Note 8.

Bank Owned Life Insurance

The Company has purchased life insurance policies on certain key employees. Bank owned life insurance is recorded at the amount that can be realized under the insurance contract at the balance sheet date, which is the cash surrender value adjusted for other charges or other amounts due that are probable at settlement.

Premises and Equipment and Long Lived Assets

Land is carried at cost. Premises and equipment are carried at cost less accumulated depreciation and amortization computed principally by the straight-line method over the following estimated useful lives:

Buildings and improvements	20 to 50 years
Furniture, fixtures and equipment	3 to 15 years

Long-lived assets to be held and those to be disposed of and certain intangibles are periodically evaluated for impairment. See Note 9.

Goodwill and Other Intangibles

Goodwill resulting from business combinations prior to January 1, 2009 represents the excess of the purchase price over the fair value of the net assets of businesses acquired. Goodwill resulting from business combinations after January 1, 2009, is generally determined as the excess of the fair value of the consideration transferred, plus the fair value of any noncontrolling interests in the acquiree, over the fair value of the net assets acquired and liabilities assumed as of the acquisition date. Goodwill and intangible assets acquired in a purchase business combination and determined to have an indefinite useful life are not amortized, but tested for impairment at least annually. The Company has selected November 30 as the date to perform the annual impairment test. Intangible assets with definite useful lives are amortized over their estimated useful lives to their estimated residual values. Goodwill is the only intangible asset with an indefinite life on First Defiance's balance sheet.

Other intangible assets consist of core deposit and acquired customer relationship intangible assets arising from whole bank, insurance and branch acquisitions. They are initially recorded at fair value and then amortized on an accelerated basis over their estimated lives, which range from five years for non-compete agreements to 10 to 20 years for core deposit and customer relationship intangibles. See Note 10.

Real Estate and Other Assets Held for Sale

Other assets held for sale are comprised of properties acquired through foreclosure proceedings or acceptance of a deed in lieu of foreclosure. These assets are initially recorded at fair value less costs to sell when acquired, establishing a new cost basis. Losses arising from the acquisition of such property are charged against the allowance for loan losses at the time of acquisition. These properties are carried at the lower of cost or fair value, less estimated costs to dispose. If fair value declines subsequent to foreclosure, the property is written down against expense. Costs after acquisition are expensed.

Stock Compensation Plans

Compensation cost is recognized for stock options and restricted share awards issued to employees and directors, based on the fair value of these awards at the date of grant. A Black-Scholes model is utilized to estimate the fair value of stock options. Restricted stock awards are valued at the market value of Company stock at the date of the grant. Compensation cost is recognized over the required service period, generally defined as the vesting period. For awards with graded vesting, compensation cost is recognized on a straight-line basis over the requisite service period for the entire award. See Note 20.

Fair Value of Financial Instruments

Fair values of financial instruments are estimated using relevant market information and other assumptions, as more fully disclosed in Note 22. Fair value estimates involve uncertainties and matters of significant judgment regarding interest rates, credit risk, prepayments, and other factors, especially in the absence of broad markets for particular items. Changes in assumptions or in market conditions could significantly affect the estimates.

Transfers of Financial Assets

Transfers of financial assets are accounted for as sales, when control over the assets has been relinquished. Control over transferred assets is deemed to be surrendered when the assets have been isolated from the Company, the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets and the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

Mortgage Banking Derivatives

Commitments to fund mortgage loans (interest rate locks) to be sold into the secondary market and forward commitments for the future delivery of these mortgage loans are accounted for as free standing derivatives. Fair values of these mortgage derivatives are estimated based on changes in mortgage interest rates from the date the interest on the loan is locked. The Company enters into forward commitments for the future delivery of mortgage loans when interest rate locks are entered into, in order to hedge the change in interest rates resulting from its commitments to fund the loans. Changes in fair values of these derivatives are included in mortgage banking income.

Operating Segments

Management considers the following factors in determining the need to disclose separate operating segments: 1) The nature of products and services, which are all financial in nature; 2) The type and class of customer for the products and services; in First Defiance's case retail customers for retail bank and insurance products and commercial customers for commercial loan, deposit, life, health and property and casualty insurance needs; 3) The methods used to distribute products or provide services; such services are delivered through banking and insurance offices and through bank and insurance customer contact representatives. Retail and commercial customers are frequently targets for both banking and insurance products; 4) The nature of the regulatory environment; both banking and insurance entities are subject to various regulatory bodies and a number of specific regulations.

Quantitative thresholds as stated in Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") Topic 280, *Segment Reporting* are monitored. For the year ended December 31, 2013, the reported revenue for First Insurance was 9.1% of total revenue for First Defiance. Total revenue includes net interest income (before provision for loan losses) plus non-interest income. Net income for First Insurance for the year ended December 31, 2013 was 4.4% of consolidated net income. Total assets of First Insurance at December 31, 2013 were 0.7% of total assets. First Insurance does not meet any of the quantitative thresholds of FASB ASC Topic 280. Accordingly, all of the financial service operations are considered by management to be aggregated in one reportable segment.

Dividend Restriction

Banking regulations require maintaining certain capital levels and may limit the dividends paid by the savings bank to the holding company. See Note 17 for further details on restrictions.

Loan Commitments and Related Financial Instruments

Financial instruments include off-balance sheet credit instruments, such as commitments to make loans and commercial letters of credit, issued to meet customer financing needs. The face amount for these items represents the exposure to loss, before considering customer collateral or ability to repay. Such financial instruments are recorded when they are funded.

Loss Contingencies

Loss contingencies, including claims and legal actions arising in the ordinary course of business, are recorded as liabilities when the likelihood of loss is probable and an amount or range of loss can be reasonably estimated. Management does not believe there are any such matters that will have a material effect on the financial statements.

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 the expected future tax amounts for the temporary differences between carrying amounts and tax bases of assets and liabilities, computed using enacted tax rates. A valuation allowance, if needed, reduces deferred tax assets to the amount expected to be realized. Realization of deferred tax assets is dependent upon the generation of a sufficient level of future taxable income and recoverable taxes paid in prior years. Although realization is not assured, management believes it is more likely than not that all of the deferred tax assets will be realized.

An effective tax rate of 35% is used to determine after-tax components of other comprehensive income (loss) included in the statements of stockholders' equity. See Note 18.

A tax position is recognized as a benefit only if it is "more likely than not" that the tax position would be sustained in a tax examination, with a tax examination being presumed to occur. The amount recognized is the largest amount of tax benefit that is greater than 50% likely of being realized on examination. For tax positions not meeting the "more likely than not" test, no tax benefit is recorded.

The Company recognizes interest and/or penalties related to income tax matters in income tax expense.

Retirement Plans

Pension expense is the net of service and interest cost, return on plan assets and amortization of gains and losses not immediately recognized. Employee 401(k) plan expense is the amount of matching contributions. Deferred compensation and supplemental retirement plan expense allocates the benefits over years of service.

Reclassifications

Some items in the prior year financial statements were reclassified to conform to the current presentation.

Accounting Standards Updates

In February 2013, the FASB issued ASU 2013-02, "*Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income*." This update requires entities to provide information about the amounts reclassified out of accumulated other comprehensive income by component. In addition, entities are required to present, either on the face of the statement where net income is presented or in the notes, significant amounts reclassified out of accumulated other comprehensive income by the respective line items of net income. The Company adopted this standard on January 1, 2013. The effect of adopting this standard increased the Company's disclosure surrounding reclassification items out of accumulated other comprehensive income.

In January 2014, the FASB issued ASU 2014-04, "*Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure*." The objective of the amendments in ASU 2014-04 to Topic 310, "*Receivables - Troubled Debt Restructurings by Creditors*," is to reduce diversity by clarifying when an in substance repossession or foreclosure occurs, that is, when a creditor should be considered to have received physical possession of residential

real estate property collateralizing a consumer mortgage loan such that the loan receivable should be derecognized and the real estate property recognized. The amendments are effective for fiscal years, and interim periods within those years, beginning after December 31, 2014. An entity can elect to adopt the amendments using either a modified retrospective transition method or a prospective transition method. Early adoption is permitted. The adoption of this guidance is not expected to have a material impact on the Company's Consolidated Financial Statements.

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3. Acquisitions

On July 1, 2011, First Defiance acquired PDI, an insurance agency headquartered in Maumee and Oregon, Ohio, for a cash purchase price of \$4.8 million and future consideration to be paid in cash in 2012, 2013, and 2014. As of December 31, 2013, management has reported goodwill of approximately \$4.0 million and identifiable intangible assets of \$810,000 consisting of a customer relationship intangible of \$551,000 and a non-compete intangible of \$259,000. The transaction included a contingent payable with a maximum cash payout of \$822,800, of which \$596,000 and \$70,000 was paid in 2013 and 2012, respectively. The accrued liability was adjusted at December 31, 2013 and ended the year at \$137,000 representing the present value of the remaining cash eligible for payment of \$157,000. The remaining \$20,000 will be expensed in 2014 with the final payout. The Company accounted for the transaction under the acquisition method of accounting which requires purchased assets and assumed liabilities to be recorded at their respective acquisition date fair value. Disclosure of pro forma results of this acquisition is not material to the Company's consolidated financial statements.

4. Earnings Per Common Share

The following table sets forth the computation of basic and diluted earnings per common share:

	2013	2012	2011
	(In Thousands, Except Per Share Amounts)		
Numerator for basic and diluted earnings per common share-net income applicable to common shares	\$ 22,235	\$ 18,047	\$ 13,506
Denominator:			
Denominator for basic earnings per common share-weighted-average common shares, including participating securities	9,764	9,728	9,371
Effect of dilutive securities:			
Employee stock options	87	51	15
Warrants	320	219	154
Dilutive potential common shares	407	270	169
Denominator for diluted earnings per common share	10,171	9,998	9,540
Basic earnings per common share	\$ 2.28	\$ 1.86	\$ 1.44
Diluted earnings per common share	\$ 2.19	\$ 1.81	\$ 1.42

Shares under option of 132,750 in 2013, 229,550 in 2012 and 255,700 in 2011 were excluded from the diluted earnings per common share calculation as they were anti-dilutive.

5. Investment Securities

The following tables summarize the amortized cost and fair value of available-for-sale securities and held-to-maturity investment securities portfolio at December 31, 2013 and 2012 and the corresponding amounts of gross unrealized gains and losses were as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
(In Thousands)				
2013				
Available-for-sale				
Obligations of U.S. government corporations and agencies	\$ 5,000	\$ -	\$ (79)	\$ 4,921
Mortgage-backed securities - residential	41,368	765	(841)	41,292
Collateralized mortgage obligations	59,865	739	(763)	59,841
Trust preferred stock and preferred stock	3,264	683	(993)	2,954
Corporate bonds	8,854	129	(41)	8,942
Obligations of state and political subdivisions	78,426	2,704	(910)	80,220
Total Available-for-Sale	\$ 196,777	\$ 5,020	\$ (3,627)	\$ 198,170

	Amortized Cost	Gross Unrecognized Gains	Gross Unrecognized Losses	Fair Value
(In Thousands)				
Held-to-Maturity				
FHLMC certificates	\$ 31	\$ -	\$ -	\$ 31
FNMA certificates	120	4	-	124
GNMA certificates	50	2	-	52
Obligations of states and political subdivisions	186	-	-	186
Total Held-to-Maturity	\$ 387	\$ 6	\$ -	\$ 393

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
(In Thousands)				
2012				
Available-for-sale				
Obligations of U.S. government corporations and agencies	\$ 11,000	\$ 69	\$ -	\$ 11,069
U.S. treasury bonds	1,000	2	-	1,002
Mortgage-backed securities - residential	30,020	1,441	-	31,461
Collateralized mortgage obligations	55,962	1,504	-	57,466
Trust preferred stock and preferred stock	3,600	99	(2,091)	1,608
Corporate bonds	8,717	167	-	8,884
	76,339	6,277	(5)	82,611

Obligations of state and political
subdivisions

Total Available-for-Sale	\$ 186,638	\$ 9,559	\$ (2,096)	\$ 194,101
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	Amortized Cost (In Thousands)	Gross Unrecognized Gains	Gross Unrecognized Losses	Fair Value
Held-to-Maturity				
FHLMC certificates	\$ 69	\$ -	\$ (1)	\$ 68
FNMA certificates	162	6	-	168
GNMA certificates	60	3	-	63
Obligations of states and political subdivisions	217	-	-	217
Total Held-to-Maturity	\$ 508	\$ 9	\$ (1)	\$ 516

The amortized cost and fair value of the investment securities portfolio at December 31, 2013 and 2012 are shown below by contractual maturity. Expected maturities will differ from contractual maturities if borrowers have the right to call or prepay obligations with or without call or prepayment penalties. For purposes of the maturity tables below, mortgage-backed securities and collateralized mortgage obligations, which are not due at a single maturity date, have not been allocated over maturity groupings.

	Available-for-Sale Amortized Cost (In Thousands)	Fair Value
2013		
Available-for-sale		
Due in one year or less	\$ 2,135	\$ 2,137
Due after one year through five years	8,198	8,526
Due after five years through ten years	38,707	40,016
Due after ten years	46,504	46,358
MBS/CMO	101,233	101,133
Total	\$ 196,777	\$ 198,170
Held-to-maturity		
Due after five years through ten years	\$ 186	\$ 186
MBS/CMO	201	207
Total	\$ 387	\$ 393

	Available-for-Sale Amortized Cost (In Thousands)	Fair Value
2012		
Available-for-sale		
Due in one year or less	\$ 1,252	\$ 1,258
Due after one year through five years	15,719	15,996
	33,743	36,024

Due after five years through
ten years

Due after ten years	49,942	51,896
MBS/CMO	85,982	88,927
	\$ 186,638	\$ 194,101

Held-to-maturity

Due after five years through ten years	\$ 217	\$ 217
MBS/CMO	291	299
Total	\$ 508	\$ 516

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Securities pledged at year-end 2013 and 2012 had a carrying amount of \$132.7 million and \$135.0 million and were pledged to secure public deposits, securities sold under repurchase agreements and FHLB advances.

As of December 31, 2013, the Company's investment portfolio consisted of 337 securities, 88 of which were in an unrealized loss position. The Company does not hold any single security that is greater than 10% of the Company's equity at December 31, 2013.

The following table summarizes First Defiance's securities that were in an unrealized loss position at December 31, 2013 and December 31, 2012:

	Duration of Unrealized Loss Position				Total	
	Less than 12 Months		12 Months or Longer			
	Fair Value	Gross Unrealized Loss	Fair Value	Gross Unrealized Loss	Fair Value	Unrealized Loses
(In Thousands)						
At December 31, 2013						
Available-for-sale securities:						
Obligations of U.S. government corporations and agencies	\$ 4,921	\$ (79)	\$ -	\$ -	\$ 4,921	\$ (79)
Mortgage-backed securities - residential	24,846	(841)	-	-	24,846	(841)
Collateralized mortgage obligations	26,530	(763)	-	-	26,530	(763)
Corporate bonds	2,959	(41)	-	-	2,959	(41)
Obligations of state and political subdivisions	19,209	(871)	375	(39)	19,584	(910)
Trust preferred stock and preferred stock	-	-	582	(993)	582	(993)
Total temporarily impaired securities	\$ 78,465	\$ (2,595)	\$ 957	\$ (1,032)	\$ 79,422	\$ (3,627)

At December 31, 2012

Available-for-sale securities:

Mortgage-backed securities - residential	\$ 1	\$ -	\$ -	\$ -	\$ 1	\$ -
Obligations of state and political subdivisions	949	(5)	-	-	949	(5)
Trust preferred stock and preferred stock	-	-	1,474	(2,091)	1,474	(2,091)
Total temporarily impaired	\$ 950	\$ (5)	\$ 1,474	\$ (2,091)	\$ 2,424	\$ (2,096)

securities

With the exception of trust preferred stock, the above securities all have fixed interest rates, and all securities have defined maturities. Their fair value is sensitive to movements in market interest rates. First Defiance has the ability and intent to hold these investments for a time necessary to recover the amortized cost without impacting its liquidity position and it is not more than likely that the Company will be required to sell the investments before anticipated recovery.

Realized gains from the sales and calls of investment securities totaled \$97,000 (\$68,000 after tax) in 2013 while there were realized gains of \$2.1 million (\$1.4 million after tax) and \$218,000 (\$142,000 after tax) in 2012 and 2011, respectively.

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Management evaluates securities for other-than-temporary impairment (“OTTI”) at least on a quarterly basis, and more frequent when economic or market conditions warrant such an evaluation. The investment portfolio is evaluated for OTTI by segregating the portfolio into two general segments. Investment securities classified as available for sale or held-to-maturity are generally evaluated for OTTI under FASB ASC Topic 320. Certain collateralized debt obligations (“CDOs”) are evaluated for OTTI under FASB ASC Topic 325, *Investment Other*.

When OTTI occurs under either model, the amount of the OTTI recognized in earnings depends on whether an entity intends to sell the security or more likely than not will be required to sell the security before recovery of its amortized cost basis less any current period credit loss. If an entity intends to sell or more likely than not will be required to sell the security before recovery of its amortized cost basis less any current period credit loss, the OTTI shall be recognized in earnings equal to the entire difference between the investment’s amortized cost basis and its fair value at the balance sheet date. If an entity does not intend to sell the security and it is not more likely than not that the entity will be required to sell the security before recovery of its amortized cost basis less any current period loss, the OTTI shall be separated into the amount representing the credit loss and the amount related to all other factors. The amount of OTTI related to the credit loss is determined based on the present value of cash flows expected to be collected compared to the book value of the security and is recognized in earnings. The amount of OTTI related to other factors shall be recognized in other comprehensive income, net of applicable taxes. The previous amortized cost basis less the OTTI recognized in earnings shall become the new amortized cost basis of the investment.

In 2013, management determined that two CDOs had OTTI resulting in a write-down of \$337,000 (\$219,000 after tax). The 2013 OTTI is related to two CDOs that were disallowed under the Final Interim Volcker Rule of the Dodd-Frank Act released on January 14, 2014 requiring the Company to liquidate these securities before a certain date. The Company received Level 1 pricing and wrote these two CDOs to that value as of December 31, 2013 and subsequently sold these two securities on January 15, 2014. In 2012, management determined that one CDO had OTTI resulting in a write-down of \$4,500 (\$2,900 after tax). In 2011, management determined that one CDO had OTTI resulting in a write-down of \$2,200 (\$1,400 after tax).

The Company held eight CDOs at December 31, 2013. Four of those CDOs were written down in full prior to January 1, 2010. The remaining four CDOs have a total amortized cost of \$3.2 million at December 31, 2013. Of these, two, with a total amortized cost of \$1.7 million, have been sold in January 2014 as stated above. The final two CDOs, with a total amortized cost of \$1.5 million, had OTTI in prior periods.

Given the conditions in the debt markets today and the absence of observable transactions in the secondary and new issue markets, the Company’s CDOs, excluding the two CDOs sold in January 2014, will be classified within Level 3 of the fair value hierarchy because management determined that significant adjustments were required to determine fair value at the measurement date. The two CDOs sold in January 2014, will be classified within Level 1 of the fair value hierarchy.

As required under FASB ASC Topic 320, declines in the fair value of held-to-maturity and available-for-sale securities below their cost that are deemed to be other than temporary are reflected in earnings as realized losses to the extent the impairment is related to credit losses.

The Company’s Level 3 CDO valuations were supported by analysis prepared by an independent third party. Their approach to determining fair value involved several steps: 1) detailed credit and structural evaluation of each piece of collateral in the CDO; 2) collateral performance projections for each piece of collateral in the CDO (default, recovery and prepayment/amortization probabilities) and 3) discounted cash flow modeling.

Trust Preferred CDOs Discount Rate Methodology

First Defiance uses market-based yield indicators as a baseline for determining appropriate discount rates, and then adjusts the resulting discount rates on the basis of its credit and structural analysis of specific CDO instruments. The next step is to make a series of adjustments to reflect the differences that nevertheless exist between these products (both credit and structural) and, most importantly, to reflect idiosyncratic credit performance differences (both actual and projected) between these products and the underlying collateral in the specific CDOs.

Fundamental to this evaluation is an assessment of the likelihood of CDO coverage test failures that would have the effect of diverting cash flow away from the relevant CDO bond for some period of time. Generally speaking, the Company adjusts indicative credit spreads upwards in the case of CDOs that have relatively weaker collateral and/or less cushion with respect to overcollateralization and interest coverage test ratios and downwards if the reverse is true. This aspect of the Company's discount rate methodology is important because there is frequently a great difference in the risks present in CDO instruments that are otherwise very similar (i.e. CDOs with the same basic type of collateral, the same manager, the same vintage, etc., may exhibit vastly different performance characteristics).

The Company believes its valuation methodology is appropriate for all of its CDOs in accordance with FASB ASC Topic 320 as well as other related guidance. The default and recovery probabilities for each piece of collateral were formed based on the evaluation of the collateral credit and a review of historical industry default data and current/near-term operating conditions. For collateral that has already deferred, the Company assumed a recovery of 10% of par for banks, thrifts or other depository institutions, and 15% for insurance companies. The Company's assumed average lifetime default rate declined to 26.2% at the end of 2013 from 27.9% at the end of 2012.

The amount of OTTI recognized in accumulated other comprehensive income ("AOCI") was \$645,000 for the above eight securities at December 31, 2013. There was \$749,000 recognized in accumulated other comprehensive income at December 31, 2012.

The following table provides additional information related to the four CDO investments for which a balance remains as of December 31, 2013 (dollars in thousands):

CDO	Class	Amortized Cost	Fair Value	Unrealized Loss	OTTI Losses 2013	Lowest Rating	Current Number of Banks and Insurance Companies	Actual Deferrals and Defaults as a % of Current Collateral	Expected Deferrals and Defaults as a % of Remaining Performing Collateral	Excess Subordination as a % of Current Performing Collateral
TPREF Funding II	B	\$ 673	\$ 266	\$ 407	\$ 0	Caa3	16	41.10 %	13.48 %	-
I-Preferred Term Sec I	B-1	839	839	-	161	CCC-	14	17.24 %	11.72 %	* 23.61
Dekania II CDO	C-1	815	815	-	176	CCC	30	- %	13.16 %	* 26.03
Preferred Term Sec XXVII	C-1	902	316	586	0	C	32	26.18 %	18.29 %	6.39
Total		\$ 3,229	\$ 2,236	\$ 993	\$ 337					

*Assumption not applicable as Level 1 pricing was utilized at December 31, 2013.

The table below presents a roll-forward of the credit losses relating to debt securities recognized in earnings for the years ended December 31, 2013, 2012 and 2011 (in thousands):

	2013	2012	2011
Beginning balance, January 1	\$ 3,176	\$ 3,251	\$ 3,249
Additions for amounts related to credit loss for which an OTTI was not previously recognized	337	-	-
Reductions for amounts realized for securities sold/redeemed during the period	-	(80)	-
Reductions for amounts related to securities for which the Company intends to sell or that it will be more likely than not that the Company will be required to sell prior to recovery of amortized cost basis	-	-	-
Reductions for increase in cash flows expected to be collected that are Recognized over the remaining life of the security	-	-	-
Increases to the amount related to the credit loss for which Other-than-temporary was previously recognized	-	5	2
Ending balance, December 31	\$ 3,513	\$ 3,176	\$ 3,251

The proceeds from sales and calls of securities and the associated gains and losses are listed below:

	2013 (In Thousands)	2012	2011
Proceeds	\$ 4,027	\$ 72,262	\$ 8,719
Gross realized gains	97	2,163	218
Gross realized losses	-	(24)	-

6. Commitments and Contingent Liabilities

Loan Commitments

Loan commitments are made to accommodate the financial needs of First Federal's customers; however, there are no long-term, fixed-rate loan commitments that result in market risk. Standby letters of credit commit the Company to make payments on behalf of customers when certain specified future events occur. They primarily are issued to facilitate customers' trade transactions.

Both arrangements have credit risk, essentially the same as that involved in extending loans to customers, and are subject to the Company's normal credit policies. Collateral (e.g., securities, receivables, inventory and equipment) is obtained based on management's credit assessment of the customer.

The Company's maximum obligation to extend credit for loan commitments (unfunded loans and unused lines of credit) and standby letters of credit outstanding on December 31 was as follows (in thousands):

2013	2012
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	Fixed Rate	Variable Rate	Fixed Rate	Variable Rate
Commitments to make loans	\$ 57,914	\$ 59,632	\$ 50,205	\$ 48,035
Unused lines of credit	18,047	257,939	21,975	228,269
Standby letters of credit	-	17,680	-	18,166
Total	\$ 75,962	\$ 335,251	\$ 72,180	\$ 294,470

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Commitments to make loans are generally made for periods of 60 days or less. The fixed rate loan commitments at December 31, 2013 have interest rates ranging from 2.00% to 18.00% and maturities ranging from less than 1 year to 30 years.

In addition to the above commitments, at December 31, 2013, First Defiance had commitments to sell \$12.1 million of loans to Freddie Mac, Fannie Mae, FHLB of Cincinnati or BB&T Mortgage.

7. Loans

Loans receivable consist of the following:

	December 31, 2013 (In Thousands)	December 31, 2012
Real Estate:		
Secured by 1-4 family residential	\$ 195,752	\$ 200,826
Secured by multi-family residential	148,952	122,275
Secured by commercial real estate	670,666	675,110
Construction	86,058	37,788
	1,101,428	1,035,999
Other Loans:		
Commercial	388,236	383,817
Home equity and improvement	106,930	108,718
Consumer Finance	16,902	15,936
	512,068	508,471
Total loans	1,613,496	1,544,470
Deduct:		
Undisbursed loan funds	(32,290)	(18,478)
Net deferred loan origination fees and costs	(758)	(735)
Allowance for loan loss	(24,950)	(26,711)
Totals	\$ 1,555,498	\$ 1,498,546

Loan segments have been identified by evaluating the portfolio based on collateral and credit risk characteristics.

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The following table discloses allowance for loan loss activity year to date as of December 31, 2013, December 31, 2012, and December 31, 2011 by portfolio segment and impairment method (in thousands):

Year to Date December 31,	1-4 Family Residential Real Estate	Multi-Family Residential Real Estate	Commercial Real Estate	Construction	Commercial	Home Equity and Improvement	Consumer Finance	Total
2013								
Beginning Allowance	\$ 3,506	\$ 2,197	\$ 12,702	\$ 75	\$ 6,325	\$ 1,759	\$ 147	\$ 26,711
Charge-Offs	(643)	(6)	(2,469)	-	(1,230)	(757)	(94)	(5,199)
Recoveries	282	-	837	-	290	125	80	1,614
Provisions	(298)	317	930	59	293	508	15	1,824
Ending Allowance	\$ 2,847	\$ 2,508	\$ 12,000	\$ 134	\$ 5,678	\$ 1,635	\$ 148	\$ 24,950
2012								
Beginning Allowance	\$ 4,095	\$ 2,850	\$ 17,640	\$ 63	\$ 6,576	\$ 1,856	\$ 174	\$ 33,254
Charge-Offs	(2,515)	(555)	(10,764)	-	(4,047)	(1,165)	(133)	(19,179)
Recoveries	177	122	895	-	359	95	64	1,712
Provisions	1,749	(220)	4,931	12	3,437	973	42	10,924
Ending Allowance	\$ 3,506	\$ 2,197	\$ 12,702	\$ 75	\$ 6,325	\$ 1,759	\$ 147	\$ 26,711
2011								
Beginning Allowance	\$ 5,956	\$ 2,147	\$ 20,208	\$ 73	\$ 10,871	\$ 1,528	\$ 297	\$ 41,080
Charge-Offs	(2,753)	(792)	(12,358)	-	(4,398)	(1,052)	(95)	(21,448)
Recoveries	127	-	533	-	393	65	70	1,188
Provisions	765	1,495	9,257	(10)	(290)	1,315	(98)	12,434
Ending Allowance	\$ 4,095	\$ 2,850	\$ 17,640	\$ 63	\$ 6,576	\$ 1,856	\$ 174	\$ 33,254

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 December 31, 2013:

(In Thousands)

	1-4 Family Residential Real Estate	Multi Family Residential Real Estate	Commercial Real Estate	Commercial Real Estate	Construction	Home Equity & Improvements	Consumer Finance	Total
Allowance for loan losses: Ending allowance balance attributable to loans:								
Individually evaluated for impairment	\$ 220	\$ -	\$ 1,121	\$ -	\$ 6	\$ 45	\$ -	\$ 1,392
Collectively evaluated for impairment	2,627	2,508	10,879	134	5,672	1,590	148	23,558
Acquired with deteriorated credit quality	-	-	-	-	-	-	-	-
Total ending allowance balance	\$ 2,847	\$ 2,508	\$ 12,000	\$ 134	\$ 5,678	\$ 1,635	\$ 148	\$ 24,950
Loans:								
Loans individually evaluated for impairment	\$ 10,245	\$ 840	\$ 34,874	\$ 263	\$ 8,737	\$ 2,429	\$ 53	\$ 57,441
Loans collectively evaluated for impairment	185,923	148,294	637,657	53,467	380,711	104,958	16,838	1,527,848
Loans acquired with deteriorated credit quality	29	-	174	-	27	-	-	230
Total ending loans balance	\$ 196,197	\$ 149,134	\$ 672,705	\$ 53,730	\$ 389,475	\$ 107,387	\$ 16,891	\$ 1,585,519

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 December 31, 2012:

(In Thousands)

	1-4 Family Residential Real Estate	Multi Family Residential Real Estate	Commercial Real Estate	Commercial Real Estate	Home Equity Construction & Improvements	Consumer Finance	Total
Allowance for loan losses: Ending allowance balance attributable to loans:							
Individually evaluated for impairment	\$ 281	\$ -	\$ 1,070	\$ -	\$ 138	\$ 2	\$ 1,491
Collectively evaluated for impairment	3,225	2,197	11,632	75	6,187	1,757	25,220
Acquired with deteriorated credit quality	-	-	-	-	-	-	-
Total ending allowance balance	\$ 3,506	\$ 2,197	\$ 12,702	\$ 75	\$ 6,325	\$ 1,759	\$ 26,711
Loans:							
Loans individually evaluated for impairment	\$ 11,930	\$ 1,626	\$ 46,053	\$ 45	\$ 8,830	\$ 2,678	\$ 71,286
Loans collectively evaluated for impairment	189,348	120,829	630,534	19,251	376,007	106,516	1,458,300
Loans acquired with deteriorated credit quality	36	-	436	-	32	-	504
Total ending loans balance	\$ 201,314	\$ 122,455	\$ 677,023	\$ 19,296	\$ 384,869	\$ 109,194	\$ 1,530,090

The following table presents the average balance, interest income recognized and cash basis income recognized on impaired loans by class of loans. *(In Thousands)*

	Twelve Months Ended December 31, 2013		
	Average Balance	Interest Income Recognized	Cash Basis Income Recognized
Residential Owner Occupied	\$ 6,529	\$ 345	\$ 343
Residential Non Owner Occupied	4,453	162	163
Total 1-4 Family Residential Real Estate	10,982	507	506
Multi-Family Residential Real Estate	1,176	27	28
CRE Owner Occupied	14,313	376	386
CRE Non Owner Occupied	22,339	901	909
Agriculture Land	987	26	16
Other CRE	4,162	43	38
Total Commercial Real Estate	41,801	1,346	1,349
Construction	165	10	8
Commercial Working Capital	2,085	33	36
Commercial Other	6,521	75	70
Total Commercial	8,606	108	106
Consumer Finance	83	6	6
Home Equity and Home Improvement	2,631	121	117
Total Impaired Loans	\$ 65,444	\$ 2,125	\$ 2,120

The following table presents the average balance, interest income recognized and cash basis income recognized on impaired loans by class of loans. *(In Thousands)*

	Twelve Months Ended December 31, 2012		
	Average Balance	Interest Income Recognized	Cash Basis Income Recognized
Residential Owner Occupied	\$ 2,946	\$ 137	\$ 136
Residential Non Owner Occupied	5,291	173	177
Total 1-4 Family Residential Real Estate	8,237	310	313
Multi-Family Residential Real Estate	826	22	21
CRE Owner Occupied	11,755	190	176
CRE Non Owner Occupied	17,156	540	559
Agriculture Land	1,062	31	23
Other CRE	6,672	15	15
Total Commercial Real Estate	36,645	776	773
Construction	9	-	-
Commercial Working Capital	2,021	26	29
Commercial Other	5,018	87	90
Total Commercial	7,039	113	119
Consumer Finance	25	3	3
Home Equity and Home Improvement	563	33	33
Total Impaired Loans	\$ 53,344	\$ 1,257	\$ 1,262

The following table presents the average balance, interest income recognized and cash basis income recognized on impaired loans by class of loans: *(In Thousands)*

	Twelve Months Ended December 31, 2011		
	Average Balance	Interest Income Recognized	Cash Basis Income Recognized
Residential Owner Occupied	\$ 2,689	\$ 68	\$ 67
Residential Non Owner Occupied	2,646	85	87
Total 1-4 Family Residential Real Estate	5,335	153	154
Multi-Family Residential Real Estate	2,097	88	83
CRE Owner Occupied	10,631	302	282
CRE Non Owner Occupied	19,351	777	724
Agriculture Land	1,932	47	47
Other CRE	7,952	54	43
Total Commercial Real Estate	39,866	1,180	1,096
Construction	25	-	-
Commercial Working Capital	3,758	74	77
Commercial Other	9,660	194	191
Total Commercial	13,418	268	268
Consumer Finance	-	-	-
Home Equity and Home Improvement	258	12	12
Total Impaired Loans	\$ 60,999	\$ 1,701	\$ 1,613

The following table presents loans individually evaluated for impairment by class of loans: *(In Thousands)*

	December 31, 2013			December 31, 2012		
	Unpaid Principal Balance*	Recorded Investment	Allowance for Loan Losses Allocated	Unpaid Principal Balance*	Recorded Investment	Allowance for Loan Losses Allocated
With no allowance recorded:						
Residential Owner Occupied	\$ 4,744	\$ 4,729	\$ -	\$ 5,427	\$ 5,357	\$ -
Residential Non Owner Occupied	4,844	4,329	-	4,211	3,420	-
Total 1-4 Family Residential Real Estate	9,588	9,058	-	9,638	8,777	-
Multi-Family Residential Real Estate	989	840	-	1,775	1,626	-
CRE Owner Occupied	11,105	8,376	-	12,314	9,782	-
CRE Non Owner Occupied	9,399	7,740	-	11,054	9,105	-
Agriculture Land	629	488	-	1,176	993	-
Other CRE	3,274	2,452	-	8,741	5,527	-
Total Commercial Real Estate	24,407	19,056	-	33,285	25,407	-
Construction	300	263	-	300	45	-
Commercial Working Capital	3,147	3,146	-	1,565	1,565	-
Commercial Other	6,063	5,415	-	6,367	5,338	-
Total Commercial	9,210	8,561	-	7,932	6,903	-
Consumer	53	53	-	125	124	-
Home Equity and Home Improvement	1,985	1,992	-	2,777	2,642	-
Total loans with no allowance recorded	\$ 46,532	\$ 39,823	\$ -	\$ 55,832	\$ 45,524	\$ -
With an allowance recorded:						
Residential Owner Occupied	\$ 1,100	\$ 1,103	\$ 218	\$ 1,697	\$ 1,701	\$ 257
Residential Non Owner Occupied	84	84	2	1,449	1,452	24
Total 1-4 Family Residential Real Estate	1,184	1,187	220	3,146	3,153	281
Multi-Family Residential Real Estate	-	-	-	-	-	-
CRE Owner Occupied	3,212	2,765	166	5,735	5,118	245
CRE Non Owner Occupied	12,756	12,803	946	15,301	15,357	820
Agriculture Land	195	197	7	111	112	3
Other CRE	82	53	2	88	59	2
Total Commercial Real Estate	16,245	15,818	1,121	21,235	20,646	1,070

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Construction	-	-	-	-	-	-
Commercial Working Capital	-	-	-	300	301	10
Commercial Other	176	176	6	1,623	1,626	128
Total Commercial	176	176	6	1,923	1,927	138
Consumer	-	-	-	-	-	-
Home Equity and Home Improvement	436	437	45	36	36	2
Total loans with an allowance recorded	\$ 18,041	\$ 17,618	\$ 1,392	\$ 26,340	\$ 25,762	\$ 1,491

* Presented gross of charge offs

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The following table presents the current balance of the aggregate amounts of non-performing assets, comprised of non-performing loans and real estate owned on the dates indicated:

	December 31, 2013 (in thousands)	December 31, 2012
Non-accrual loans	\$ 27,847	\$ 32,570
Loans over 90 days past due and still accruing	-	-
Total non-performing loans	27,847	32,570
Real estate and other assets held for sale	5,859	3,805
Total non-performing assets	\$ 33,706	\$ 36,375

Troubled debt restructuring, still accruing \$ 27,630 \$ 28,203

The following table presents the aging of the recorded investment in past due and non-accrual loans as of December 31, 2013 by class of loans: *(In Thousands)*

	Current	30-59 days	60-89 days	90+ days	Total Past Due	Total Non Accrual
Residential Owner Occupied	\$ 126,855	\$ 1,530	\$ 191	\$ 1,009	\$ 2,730	\$ 1,329
Residential Non Owner Occupied	65,292	531	403	386	1,320	1,943
Total 1-4 Family Residential Real Estate	192,147	2,061	594	1,395	4,050	3,272
Multi-Family Residential Real Estate	149,134	-	-	-	-	583
CRE Owner Occupied	311,253	334	495	3,671	4,500	7,492
CRE Non Owner Occupied	225,433	1,067	918	902	2,887	4,717
Agriculture Land	81,954	21	-	73	94	630
Other Commercial Real Estate	45,297	-	-	1,287	1,287	2,412
Total Commercial Real Estate	663,937	1,422	1,413	5,933	8,768	15,251
Construction	53,730	-	-	-	-	-
Commercial Working Capital	155,373	-	-	419	419	2,917
Commercial Other	230,054	37	26	3,566	3,629	5,419
Total Commercial	385,427	37	26	3,985	4,048	8,336
Consumer Finance	16,759	131	-	-	131	-
Home Equity/Home Improvement	105,657	1,163	155	413	1,731	413

Total Loans	\$	1,566,791	\$	4,814	\$	2,188	\$	11,726	\$	18,728	\$	27,855
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The following table presents the aging of the recorded investment in past due and non-accrual loans as of December 31, 2012 by class of loans: *(In Thousands)*

	Current	30-59 days	60-89 days	90+ days	Total Past Due	Total Non Accrual
Residential Owner Occupied	\$ 125,362	\$ 1,238	\$ 604	\$ 945	\$ 2,787	\$ 1,125
Residential Non Owner Occupied	71,777	413	126	849	1,388	2,473
Total 1-4 Family Residential Real Estate	197,139	1,651	730	1,794	4,175	3,598
Multi-Family Residential Real Estate	122,455	-	-	-	-	1,178
CRE Owner Occupied	321,071	1,248	382	1,622	3,252	9,652
CRE Non Owner Occupied	235,592	134	1,321	2,480	3,935	6,674
Agriculture Land	72,092	84	31	-	115	813
Other Commercial Real Estate	36,510	21	875	3,560	4,456	4,761
Total Commercial Real Estate	665,265	1,487	2,609	7,662	11,758	21,900
Construction	19,296	-	-	-	-	-
Commercial Working Capital	161,110	-	155	1,204	1,359	1,528
Commercial Other	218,477	584	1,201	2,138	3,923	4,136
Total Commercial	379,587	584	1,356	3,342	5,282	5,664
Consumer Finance	15,702	229	8	-	237	-
Home Equity/Home Improvement	106,458	2,294	225	217	2,736	217
Total Loans	\$ 1,505,902	\$ 6,245	\$ 4,928	\$ 13,015	\$ 24,188	\$ 32,557

Troubled Debt Restructurings

As of December 31, 2013 and 2012, the Company has a recorded investment in troubled debt restructurings (“TDRs”) of \$33.4 million and \$35.5 million, respectively. The Company has allocated \$1.2 million and \$1.1 million, of specific reserves to those loans at December 31, 2013 and 2012, and has committed to lend additional amounts totaling up to \$300,000 and \$41,000 at December 31, 2013 and 2012.

The Company offers various types of concessions when modifying a loan, however, forgiveness of principal is rarely granted. Each TDR is uniquely designed to meet the specific needs of the borrower. Commercial and industrial loans modified in a TDR often involve temporary interest-only payments, term extensions, and converting revolving credit lines to term loans. Additional collateral or an additional guarantor is often requested when granting a concession. Commercial mortgage loans modified in a TDR often involve temporary interest-only payments, re-amortization of

remaining debt in order to lower payments, and sometimes reducing the interest rate lower than the current market rate. Residential mortgage loans modified in a TDR are comprised of loans where monthly payments are lowered, either through interest rate reductions or principal only payments for a period of time, to accommodate the borrowers' financial needs, interest is capitalized into principal, or the term and amortization are extended. Home equity modifications are made infrequently and usually involve providing an interest rate that is lower than the borrower would be able to obtain due to credit issues. All retail loans where the borrower is in bankruptcy are classified as TDRs regardless of whether or not a concession is made.

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Of the loans modified in a TDR, \$5.7 million are on non-accrual status and partial charge-offs have in some cases been taken against the outstanding balance. Loans modified as a TDR may have the financial effect of increasing the allowance associated with the loan. If the loan is determined to be collateral dependent, the estimated fair value of the collateral, less any selling costs is used to determine if there is a need for a specific allowance or charge-off. If the loan is determined to be cash flow dependent, the allowance is measured based on the present value of expected future cash flows discounted at the loan's pre-modification effective interest rate.

The following table presents loans by class modified as TDRs that occurred during the years ending December 31, 2013, 2012, and 2011 (Dollars in Thousands):

Troubled Debt Restructurings	Loans Modified as a TDR for the Twelve Months Ended December 31, 2013			Loans Modified as a TDR for the Twelve Months Ended December 31, 2012			Loans Modified as a TDR for the Twelve Months Ended December 31, 2011		
	Number of Loans	Recorded Investment (as of period end)	Number of Loans	Recorded Investment (as of period end)	Number of Loans	Recorded Investment (as of period end)	Number of Loans	Recorded Investment (as of period end)	Recorded Investment (as of period end)
1-4 Family Owner Occupied	10	\$ 752	87	\$ 6,052	4	\$ 250			
1-4 Family Non Owner Occupied	5	390	8	666	1	305			
CRE Owner Occupied	9	714	9	3,859	6	426			
CRE Non Owner Occupied	2	1,364	13	13,942	6	4,628			
Agriculture Land	2	269	3	474	-	-			
Other CRE	3	417	1	59	-	-			
Commercial Working Capital or Other	8	1,602	7	1,196	6	2,379			
Home Equity and Improvement	15	561	127	2,663	1	22			
Consumer Finance	3	15	27	124	-	-			
Total	57	\$ 6,084	282	\$ 29,035	24	\$ 8,010			

The loans described above increased the ALLL by \$27,000 for the year ended December 31, 2013, decreased the ALLL by \$1.2 million for the year ended December 31, 2012, and decreased the ALLL by \$479,000 for the year ended December 31, 2011.

Of the 2013 modifications, 10 were made TDRs due to the fact that the borrower has been in bankruptcy, 7 were made TDRs due to a rate reduction, 5 were made TDRs due to interest only periods, 2 were made TDRs due to extending the amortization, 18 were made TDRs due to an extension of maturity, 4 were made TDRs due to a reduction in the payment, 4 were made to advance funds to a substandard credit, 6 were made to refinance current debt, and 1 loan was made for a different modification.

The following table presents loans by class modified as TDRs for which there was a payment default within twelve months following the modification during the years ending December 31, 2013, 2012, and 2011:

Troubled Debt Restructurings That Subsequently Defaulted:	Twelve Months Ended December 31, 2013 (\$ in thousands)		Twelve Months Ended December 31, 2012 (\$ in thousands)		Twelve Months Ended December 31, 2011 (\$ in thousands)	
	Number of Loans	Recorded Investment (as of Period End)	Number of Loans	Recorded Investment (as of Period End)	Number of Loans	Recorded Investment (as of Period End)
Residential Owner Occupied	6	\$ 409	6	\$ 462	2	\$ 206
Residential Non Owner Occupied	-	-	2	203	-	-
CRE Owner Occupied	2	290	-	-	1	1,495
CRE Non Owner Occupied	1	212	3	555	-	-
Agriculture Land	-	-	-	-	-	-
Other CRE	1	323	-	-	-	-
Commercial / Industrial	5	889	5	2,129	1	53
Home Equity / Improvement	3	315	7	166	-	-
Consumer	-	-	-	-	-	-
Total	18	\$ 2,438	23	\$ 3,515	4	\$ 1,754

The TDRs that subsequently defaulted described above increased the ALLL by \$21,000 after \$58,000 in charge-offs for the year ended December 31, 2013, decreased the ALLL by \$631,000 after \$1.5 million in charge-offs for the year ended December 31, 2012, and increased the ALLL by \$29,000 after \$500,000 in charge-offs for the year ended December 31, 2011.

A default for purposes of this disclosure is a TDR loan in which the borrower is 90 days contractually past due under the modified terms.

The terms of certain other loans were modified during the periods ending December 31, 2013 and 2012 that did not meet the definition of a TDR. The modification of these loans involved a modification of the terms of a loan to borrowers who were not experiencing financial difficulties. A total of 152 loans were modified under this definition during the twelve month period ended December 31, 2013 and a total of 343 loans were modified under this definition during the twelve month period ended December 31, 2012.

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

Credit Quality Indicators

Loans are categorized 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. Loans are analyzed individually by classifying the loans as to credit risk. This analysis includes all non-homogeneous loans, such as commercial and commercial real estate loans and certain homogenous mortgage, home equity and consumer loans. This analysis is performed on a quarterly basis. First Defiance 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.

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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.

Not Graded. Loans classified as not graded are generally smaller balance residential real estate, home equity and consumer installment loans which are originated primarily by using an automated underwriting system. These loans are monitored based on their delinquency status and are evaluated individually only if they are seriously delinquent.

Loans not meeting the criteria above that are analyzed individually as part of the above described process are considered to be pass rated loans. As of December 31, 2013, and based on the most recent analysis performed, the risk category of loans by class of loans is as follows: *(In Thousands)*

Class	Pass	Special Mention	Substandard	Doubtful	Not Graded	Total
1-4 Family Owner Occupied	\$ 4,287	\$ 18	\$ 3,515	\$ -	\$ 121,765	\$ 129,585
1-4 Family Non Owner Occupied	51,660	2,894	5,699	-	6,359	66,612
Total 1-4 Family Real Estate	55,947	2,912	9,214	-	128,124	196,197
Multi-Family Residential Real Estate	145,407	875	1,888	-	964	149,134
CRE Owner Occupied	291,770	10,584	11,665	-	1,734	315,753
CRE Non Owner Occupied	200,790	10,254	17,185	-	91	228,320
Agriculture Land	80,418	578	1,051	-	-	82,047
Other CRE	40,676	2,074	3,104	-	731	46,585
Total Commercial Real Estate	613,654	23,490	33,005	-	2,556	672,705
Construction	43,465	-	263	-	10,002	53,730
Commercial Working Capital	148,703	3,429	3,660	-	-	155,792
Commercial Other	219,790	6,994	6,899	-	-	233,683
Total Commercial	368,493	10,423	10,559	-	-	389,475
	-	-	755	45	106,587	107,387

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Home Equity and Home
Improvement

Consumer Finance	-	-	31	-	16,860	16,891
Total Loans	\$ 1,226,966	\$ 37,700	\$ 55,715	\$ 45	\$ 265,093	\$ 1,585,519

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As of December 31, 2012, and based on the most recent analysis performed, the risk category of loans by class of loans is as follows: *(In Thousands)*

Class	Pass	Special Mention	Substandard	Doubtful	Not Graded	Total
1-4 Family Owner Occupied	\$ 4,221	\$ 75	\$ 3,617	\$ 234	\$ 120,002	\$ 128,149
1-4 Family Non Owner Occupied	55,771	2,453	8,248	-	6,693	73,165
Total 1-4 Family Real Estate	59,992	2,528	11,865	234	126,695	201,314
Multi-Family Residential Real Estate	118,121	910	2,404	-	1,020	122,455
CRE Owner Occupied	292,765	10,440	18,740	-	2,378	324,323
CRE Non Owner Occupied	207,745	9,077	22,615	-	90	239,527
Agriculture Land	69,924	769	1,514	-	-	72,207
Other CRE	31,875	891	7,222	-	978	40,966
Total Commercial Real Estate	602,309	21,177	50,091	-	3,446	677,023
Construction	11,360	-	45	-	7,891	19,296
Commercial Working Capital	156,433	3,587	2,449	-	-	162,469
Commercial Other	208,783	5,204	8,413	-	-	222,400
Total Commercial	365,216	8,791	10,862	-	-	384,869
Home Equity and Home Improvement	-	-	668	64	108,462	109,194
Consumer Finance	-	-	70	-	15,869	15,939
Total Loans	\$ 1,156,998	\$ 33,406	\$ 76,005	\$ 298	\$ 263,383	\$ 1,530,090

Certain loans acquired had evidence that the credit quality of the loan had deteriorated since its origination and in management's assessment at the acquisition date it was probable that the First Defiance would be unable to collect all contractually required payments due. In accordance with FASB ASC Topic 310 Subtopic 30, *Loans and Debt Securities Acquired with Deteriorated Credit Quality*, these loans have been recorded based on management's estimate of the fair value of the loans. Details of these loans are as follows:

	Contractual Amount Receivable (In Thousands)	Impairment Discount	Recorded Loan Receivable
Balance at January 1, 2011	\$ 3,482	\$ 1,286	\$ 2,196
Principal payments received	(413)	-	(413)
Loans charged off	(250)	(250)	-
Additional provision for loan loss	(613)	-	(613)
Loan accretion recorded	-	(33)	33
Balance at December 31, 2011	2,206	1,003	1,203
Principal payments received	(697)	-	(697)
Loans charged off	(487)	(487)	-
Additional provision for loan loss	(167)	-	(167)
Loan accretion recorded	-	(173)	173
Balance at December 31, 2012	855	343	512
Principal payments received	(108)	-	(108)
Loans charged off	(41)	(41)	-
Additional provision for loan loss	(203)	-	(203)
Loan accretion recorded	-	(29)	29
Balance at December 31, 2013	\$ 503	\$ 273	\$ 230

Loans to executive officers, directors, and their affiliates are as follows (in thousands):

	Years Ended December 31	
	2013	2012
Beginning balance	\$ 3,489	\$ 4,775
New loans	8,874	5,036
Effect of changes in composition of related parties	-	(878)
Repayments	(8,651)	(5,444)
Ending Balance	\$ 3,712	\$ 3,489

8. Mortgage Banking

Net revenues from the sales and servicing of mortgage loans consisted of the following:

	Years Ended December 31		
	2013	2012	2011
	(In Thousands)		
Gain from sale of mortgage loans	\$ 5,716	\$ 10,599	\$ 5,607
Mortgage loan servicing revenue (expense):			
Mortgage loan servicing revenue	3,564	3,387	3,403
Amortization of mortgage servicing rights	(2,098)	(3,562)	(2,169)
Mortgage servicing rights valuation adjustments	1,261	(759)	(404)
	2,727	(934)	830
Net revenue from sale and servicing of mortgage loans	\$ 8,443	\$ 9,665	\$ 6,437

The unpaid principal balance of residential mortgage loans serviced for third parties was \$1.4 billion at December 31, 2013 and \$1.3 billion at December 31, 2012.

Activity for capitalized mortgage servicing rights and the related valuation allowance follows:

	Years Ended December 31		
	2013	2012	2011
	(In Thousands)		
Mortgage servicing assets:			
Balance at beginning of period	\$ 10,121	\$ 10,219	\$ 10,602
Loans sold, servicing retained	2,110	3,464	1,786
Amortization	(2,098)	(3,562)	(2,169)
Carrying value before valuation allowance at end of period	10,133	10,121	10,219
Valuation allowance:			
Balance at beginning of period	(2,288)	(1,529)	(1,125)
Impairment recovery (charges)	1,261	(759)	(404)
Balance at end of period	(1,027)	(2,288)	(1,529)
Net carrying value of MSRs at end of period	\$ 9,106	\$ 7,833	\$ 8,690
Fair value of MSRs at end of period	\$ 9,686	\$ 7,833	\$ 8,690

Amortization of mortgage servicing rights is computed based on payments and payoffs of the related mortgage loans serviced.

The Company's servicing portfolio is comprised of the following:

Investor	December 31 2013		2012	
	Number of Loans (In Thousands)	Principal Outstanding	Number of Loans	Principal Outstanding
Fannie Mae	5,304	\$ 527,666	5,190	\$ 522,978
Freddie Mac	8,873	829,594	8,550	786,124
Federal Home Loan Bank	116	12,093	166	18,330
Other	26	1,888	21	1,285
Totals	14,319	\$ 1,371,241	13,927	\$ 1,328,717

Custodial escrow balances maintained in connection with serviced loans were \$10.4 million and \$9.7 million at December 31, 2013 and 2012, respectively.

Significant assumptions at December 31, 2013 used in determining the value of MSRs include a weighted average prepayment rate of 212 prepayment speed assumption ("PSA") and a weighted average discount rate of 10.04%. Significant assumptions at December 31, 2012 used in determining the value of MSRs include a weighted average prepayment rate of 328 PSA and a weighted average discount rate of 10.04%.

A sensitivity analysis of the current fair value to immediate 10% and 20% adverse changes in those assumptions as of December 31, 2013 is presented below. These sensitivities are hypothetical. Changes in fair value based on 10% and 20% variation in assumptions generally cannot be extrapolated because the relationship of the change in the assumption to the change in fair value may not be linear. Also, the effect of a variation in a particular assumption on the fair value of the MSR is calculated independently without changing any other assumption. In reality, changes in one factor may result in changes in another (for example, changes in mortgage interest rates, which drive changes in prepayment rate estimates, could result in changes in the discount rates), which might magnify or counteract the sensitivities.

	10% Adverse Change (In Thousands)	20% Adverse Change
Assumption:		
Decline in fair value from increase in prepayment rate	\$ 454	\$ 861
Declines in fair value from increase in discount rate	318	725

9. Premises and Equipment

Premises and equipment are summarized as follows:

	December 31 2013 (In Thousands)	2012
Cost:		
Land	\$ 7,960	\$ 7,376
Land improvements	1,310	1,310
Buildings	39,716	39,691
Leasehold improvements	469	435
Furniture, fixtures and equipment	28,654	27,596
Construction in process	514	262
	78,623	76,670
Less allowances for depreciation and amortization	40,026	37,007
	\$ 38,597	\$ 39,663

Depreciation expense was \$3.1 million, \$3.4 million and \$3.4 million for the years ended December 31, 2013, 2012 and 2011, respectively.

Lease Agreements

The Company has entered into lease agreements covering the five First Insurance Group's offices, two banking center locations, two land leases for which the Company owns the banking centers, one land lease which is primarily used for parking, one land lease for future branch development and numerous stand-alone Automated Teller Machine sites with varying terms and options to renew.

Future minimum commitments under non-cancelable operating leases are as follows (in thousands):

2014	\$ 706
2015	613
2016	601
2017	512
2018	471
Thereafter	4,745
Total	\$ 7,648

Rentals under operating leases amounted to \$723,000, \$1.2 million and \$669,000 in 2013, 2012, and 2011, respectively.

10. Goodwill and Intangible Assets**Goodwill**

The change in the carrying amount of goodwill for the year is as follows (In Thousands):

	December 31 2013	2012
Beginning balance	\$ 61,525	\$ 61,525
Goodwill acquired or adjusted during the year	-	-
Ending balance	\$ 61,525	\$ 61,525

Acquired Intangible Assets

Activity in intangible assets for the years ended December 31, 2013, 2012 and 2011 was as follows:

	Gross Carrying Amount (In Thousands)	Accumulated Amortization	Net Value
Balance as of January 1, 2011	\$ 12,837	\$ (6,709)	\$ 6,128
Intangible assets acquired	1,465	-	1,465
Amortization of intangible assets	-	(1,442)	(1,442)
Balance as of December 31, 2011	14,302	(8,151)	6,151
Amortization of intangible assets	-	(1,413)	(1,413)
Balance as of December 31, 2012	14,302	(9,564)	4,738
Amortization of intangible assets	-	(1,241)	(1,241)
Balance as of December 31, 2013	\$ 14,302	\$ (10,805)	\$ 3,497

Estimated amortization expense for each of the next five years and thereafter (in thousands) is as follows:

2014	\$ 1,102
2015	687
2016	501
2017	372
2018	301
Thereafter	534
Total	\$ 3,497

11. Deposits

The following schedule sets forth interest expense by type of deposit:

	Years Ended December 31		
	2013	2012	2011
	(In Thousands)		
Checking and money market accounts	\$ 1,125	\$ 1,368	\$ 2,144
Savings accounts	90	116	249
Certificates of deposit	4,698	6,685	9,782
Totals	\$ 5,913	\$ 8,169	\$ 12,175

Accrued interest payable on deposit accounts amounted to \$48,000 and \$71,000 December 31, 2013 and 2012, respectively, which was comprised of \$34,000 and \$14,000 for certificates of deposit and checking and money market accounts, respectively, at December 31, 2013 and \$58,000 and \$13,000 for certificates of deposit and checking and money market accounts, respectively, at December 31, 2012.

A summary of deposit balances is as follows:

	December 31 2013 (In Thousands)	2012
Non-interest bearing checking accounts	\$ 348,943	\$ 315,132
Interest bearing checking and money market accounts	715,939	664,857
Savings deposits	185,121	166,945
Retail certificates of deposit less than \$100,000	313,335	342,472
Retail certificates of deposit greater than \$100,000	172,454	176,029
Brokered or national certificates of deposit	-	2,037
	\$ 1,735,792	\$ 1,667,472

Scheduled maturities of certificates of deposit at December 31, 2013 are as follows (in thousands):

2014	\$ 296,186
2015	87,059
2016	51,784
2017	8,980
2018	41,631
2019 and thereafter	149
Total	\$ 485,789

At December 31, 2013 and 2012, deposits of \$823.7 million and \$749.2 million, respectively, were in excess of \$100,000. Of these same deposits at December 31, 2013 and 2012, deposits of \$393.0 million and \$387.0 million, respectively, were in excess of the \$250,000 FDIC insurance limit. At December 31, 2013 and 2012, \$54.1 million and \$57.5 million, respectively, in investment securities were pledged as collateral against public deposits for certificates in excess of \$100,000 and an additional \$78.5 million and \$77.5 million of securities were pledged at December 31, 2013 and December 31, 2012, respectively, as collateral against deposits from private entities in excess of \$100,000.

12. Advances from Federal Home Loan Bank

First Federal has the ability to borrow funds from the FHLB. First Federal pledges its single-family residential mortgage loan portfolio, certain investment securities, certain first mortgage home equity loans, certain multi-family or non-residential real estate loans, and certain agriculture real estate loans as security for these advances. Advances secured by investment securities must have collateral of at least 105% of the borrowing. Advances secured by residential mortgages must have collateral of at least 125% of the borrowings. Advances secured by multi-family or non-residential real estate loans, and agriculture real estate loans must have 300% collateral coverage. The total level of borrowing is also limited to 50% of total assets and at least 50% of the borrowings must be secured by either one-to-four family residential mortgages or investment securities. Total loans pledged to the FHLB at December 31, 2013 and December 31, 2012 were \$676.6 million and \$666.5 million, respectively. First Federal may obtain advances of up to approximately \$428.7 million from the FHLB at December 31, 2013.

At year-end, advances from the FHLB were as follows:

Principal Terms	Advance Amount	Range of Maturities	Weighted Average Interest Rate	
	(in Thousands)			
December 31, 2013				
Putable advances	\$ 12,000	January 2015 to March 2018	2.72	%
Amortizable mortgage advances	10,520	December 2015 to September 2018	1.95	%
	\$ 22,520			
December 31, 2012				
Putable advances	\$ 12,000	January 2015 to March 2018	2.72	%
Amortizable mortgage advances	796	December 2015	4.10	%
	\$ 12,796			

Putable advances are callable at the option of the FHLB on a quarterly basis.

Estimated future minimum payments by fiscal year based on maturity date and current interest rates are as follows (in thousands):

2014	\$ 1,502
2015	8,944
2016	1,212
2017	1,212
2018	11,065
Total minimum payments	23,935
Less amounts representing interest	1,415
Totals	\$ 22,520

First Defiance also utilizes short-term advances from the FHLB to meet cash flow needs and for short-term investment purposes. First Defiance borrows short-term advances under a variety of programs at FHLB. At December 31, 2013 and December 31, 2012, there were no amounts outstanding under First Defiance's Cash Management Advance line of credit. The total available under this line is \$15.0 million. In addition, First Defiance has a \$100.0 million REPO Advance line of credit available. There were no borrowings against this line at December 31, 2013 and December 31, 2012. Amounts are generally borrowed under the Cash Management and REPO lines on an overnight basis.

13. Junior Subordinated Debentures Owed to Unconsolidated Subsidiary Trust

In March 2007, the Company sponsored an affiliated trust, First Defiance Statutory Trust II (Trust Affiliate II) that issued \$15 million of Guaranteed Capital Trust Securities (Trust Preferred Securities). In connection with the transaction, the Company issued \$15.5 million of Junior Subordinated Deferrable Interest Debentures (Subordinated Debentures) to Trust Affiliate II. The Company formed Trust Affiliate II for the purpose of issuing Trust Preferred Securities to third-party investors and investing the proceeds from the sale of these capital securities solely in Subordinated Debentures of the Company. The Subordinated Debentures held by Trust Affiliate II are the sole assets of that trust. The Company is not considered the primary beneficiary of this Trust (variable interest entity), therefore the trust is not consolidated in the Company's financial statements, but rather the subordinated debentures are shown as a liability. Distributions on the Trust Preferred Securities issued by Trust Affiliate II are payable quarterly at a variable rate equal to the three-month LIBOR rate plus 1.5%. The Coupon rate payable on the Trust Preferred Securities issued by Trust Affiliate II was 1.75% and 1.89% as of December 31, 2013 and 2012 respectively.

The Trust Preferred Securities issued by Trust Affiliate II are subject to mandatory redemption, in whole or part, upon repayment of the Subordinated Debentures. The Company has entered into an agreement that fully and unconditionally guarantees the Trust Preferred Securities subject to the terms of the guarantee. The Trust Preferred Securities and Subordinated Debentures mature on June 15, 2037, but may be redeemed at the Company's option at any time on or after June 15, 2012, or at any time upon certain events.

The Company also sponsors an affiliated trust, First Defiance Statutory Trust I (Trust Affiliate I), that issued \$20 million of Trust Preferred Securities in 2005. In connection with this transaction, the Company issued \$20.6 million of Subordinated Debentures to Trust Affiliate I. Trust Affiliate I was formed for the purpose of issuing Trust Preferred Securities to third-party investors and investing the proceeds from the sale of these capital securities solely in Subordinated Debentures of the Company. The Junior Debentures held by Trust Affiliate I are the sole assets of the trust. The Company is not considered the primary beneficiary of this Trust (variable interest entity), therefore the trust is not consolidated in the Company's financial statements, but rather the subordinated debentures are shown as a liability. Distributions on the Trust Preferred Securities issued by Trust Affiliate I are payable quarterly at a variable rate equal to the three-month LIBOR rate plus 1.38%. The Coupon rate payable on the Trust Preferred Securities issued by Trust Affiliate I was 1.63% and 1.77% as of December 31, 2013 and 2012 respectively.

The Trust Preferred Securities issued by Trust Affiliate I are subject to mandatory redemption, in whole or in part, upon repayment of the Subordinated Debentures. The Company has entered into an agreement that fully and unconditionally guarantees the Trust Preferred Securities subject to the terms of the guarantee. The Trust Preferred Securities and Junior Debentures mature December 15, 2035 but may be redeemed by the issuer at par after October 28, 2010.

The subordinated debentures may be included in Tier 1 capital (with certain limitations applicable) under current regulatory guidelines and interpretations.

A summary of all junior subordinated debentures issued by the Company to affiliates follows. These amounts represent the par value of the obligations owed to these affiliates, including the Company's equity interest in the trusts. Junior subordinated debentures owed to the following affiliates were as follows (In Thousands):

	December 31	
	2013	2012
First Defiance Statutory Trust I due December 2035	\$ 20,619	\$ 20,619
First Defiance Statutory Trust II due June 2037	15,464	15,464
Total junior subordinated debentures owed to unconsolidated subsidiary Trusts	\$ 36,083	\$ 36,083

Interest on both issues of Trust Preferred Securities may be deferred for a period of up to five years at the option of the issuer.

14. Notes Payable and Other Short-term Borrowings

Total short-term borrowings, revolving and term debt is summarized as follows:

	Years Ended December 31			
	2013		2012	
	(In Thousands, Except Percentages)			
Securities sold under agreement to repurchase				
Amounts outstanding at year-end	\$	51,919	\$	51,702
Year-end interest rate		0.31	%	0.63
Average daily balance during year		50,877		53,171
Maximum month-end balance during the year		57,182		57,050
Average interest rate during the year		0.44	%	0.70

As of December 31, 2013 and December 31, 2012, First Federal had the following lines of credit facilities available for short-term borrowing purposes:

A \$10.8 million line of credit with the Federal Reserve Bank Discount Window at an interest rate of 50 basis points over the fed funds rate. The fed funds rate as of December, 31, 2013 was 0.25%.

A \$15 million line of credit with the Bank of America. The rate on this line of credit is Bank of America's fed funds rate, which floats daily.

15. Other Noninterest Expense

The following is a summary of other noninterest expense:

	Years Ended December 31		
	2013	2012	2011
	(In Thousands)		
Legal and other professional fees	\$ 2,947	\$ 2,571	\$ 2,473
Marketing	1,563	1,400	1,392
State franchise taxes	2,323	2,495	2,010
REO expenses and write-downs	1,584	1,121	2,453
Printing and office supplies	449	527	502
Amortization of intangibles	1,241	1,413	1,442
Postage	531	567	674
Check charge-offs and fraud losses	172	153	493
Credit and collection expense	915	948	874
Other *	5,315	7,090	4,318
Total other noninterest expense	\$ 17,040	\$ 18,285	\$ 16,631

*Included in Other for 2012 is \$2.0 million in FHLB pre-payment penalties.

16. Postretirement Benefits

First Defiance sponsors a defined benefit postretirement plan that is intended to supplement Medicare coverage for certain retirees who meet minimum age requirements. First Federal employees who retired prior to April 1, 1997 who completed 20 years of service after age 40 receive full medical coverage at no cost. Such coverage continues for surviving spouses of those participants for one year, after which coverage may be continued provided the spouse pays 50% of the average cost. First Federal employees retiring after April 1, 1997 are provided medical benefits at a cost based on their combined age and years of service at retirement. Surviving spouses are also eligible for continued coverage after the retiree is deceased at a subsidy level that is 10% less than what the retiree is eligible for. First

Federal employees retiring before July 1, 1997 receive dental and vision care in addition to medical coverage. First Federal employees who retire after July 1, 1997 are not eligible for dental or vision care, but those retirees and their spouses each receive up to \$200 annually in a medical spending account. Funds in that account may be used for payment of uninsured medical expenses.

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First Federal employees who were born after December 31, 1950 are not eligible for the medical coverage described above at retirement. Rather, a medical spending account of up to \$10,000 (based on the participant's age and years of service) will be established to reimburse medical expenses for those individuals. First Insurance employees who were born before December 31, 1950 can continue coverage until they reach age 65, or in lieu of continuing coverage, can elect the medical spending account option, subject to eligibility requirements. Employees hired or acquired after January 1, 2003 are eligible only for the medical spending account option.

Included in accumulated other comprehensive income at December 31, 2013, 2012 and 2011 are the following amounts that have not yet been recognized in net periodic benefit cost:

	December 31 2013 (In Thousands)	2012	2011
Unrecognized prior service cost	\$ 78	\$ 30	\$ 46
Unrecognized actuarial losses	477	858	1,041
Total recognized in Accumulated Other Comprehensive Income	555	888	1,087
Income tax effect	(194)	(311)	(380)
Net amount recognized in Accumulated Other Comprehensive Income	\$ 361	\$ 577	\$ 707

The prior service cost and actuarial loss included in other comprehensive income and expected to be recognized in net postretirement benefit cost during the fiscal year-ended December 31, 2014 is \$12,000 (\$8,000 net of tax) and \$14,000 (\$9,000 net of tax), respectively.

Reconciliation of Funded Status and Accumulated Benefit Obligation

The plan is not currently funded. The following table summarizes benefit obligation and plan asset activity for the plan measured as of December 31 each year:

	December 31 2013 (In Thousands)	2012
Change in benefit obligation:		
Benefit obligation at beginning of year	\$ 3,140	\$ 3,117
Service cost	82	88
Interest cost	118	120
Participant contribution	25	16
Actuarial (gains) / losses	(347)	(148)
Acquisition	-	60
Benefits paid	(139)	(113)
Benefit obligation at end of year	2,878	3,140
Change in fair value of plan assets:		
Balance at beginning of year	-	-
Employer contribution	114	97
Participant contribution	25	16
Benefits paid	(139)	(113)
Balance at end of year	-	-
Funded status at end of year	\$ (2,878)	\$ (3,140)

Net periodic postretirement benefit cost includes the following components:

	Years Ended December 31		
	2013	2012	2011
	(In Thousands)		
Service cost-benefits attributable to service during the period	\$ 82	\$ 88	\$ 73
Interest cost on accumulated postretirement benefit obligation	118	120	128
Net amortization and deferral	46	51	25
Net periodic postretirement benefit cost	246	259	226
Net (gain) / loss during the year	(347)	(148)	537
Impact of prior year acquisition	60	-	-
Amortization of prior service cost and actuarial losses	(46)	(51)	(25)
Total recognized in comprehensive income	(333)	(199)	512
Total recognized in net periodic postretirement benefit cost and other comprehensive income	\$ (87)	\$ 60	\$ 738

The following assumptions were used in determining the components of the postretirement benefit obligation:

	2013		2012		2011	
Weighted average discount rates:						
Used to determine benefit obligations at December 31	4.75	%	4.00	%	4.25	%
Used to determine net periodic postretirement benefit cost for years ended December 31	4.00	%	4.25	%	5.25	%
Assumed health care cost trend rates at December 31:						
Health care cost trend rate assumed for next year	7.50	%	8.00	%	7.50	%
Rate to which the cost trend rate is assumed to decline (the ultimate trend rate)	5.00	%	5.00	%	4.00	%
Year that rate reaches ultimate trend rate	2019		2019		2019	

The following benefits are expected to be paid over the next five years and in aggregate for the next five years thereafter. Because the plan is unfunded, the expected net benefits to be paid and the estimated Company contributions are the same amount.

	Expected to be Paid (In Thousands)
2014	\$ 140
2015	128
2016	132
2017	160
2018	153
2019 through 2023	892

Assumed health care cost trend rates have a significant effect on the amounts reported for the health care plans. A one-percentage-point change in assumed health care cost trend rates would have the following effect:

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	One-Percentage-Point Increase Year Ended December 31		One-Percentage-Point Decrease Year Ended December 31	
	2013	2012	2013	2012
	(In Thousands)			
Effect on total of service and interest cost	\$ 28	\$ 30	\$ (24)	\$ (25)
Effect on postretirement benefit obligation	351	406	(299)	(344)

The Company expects to contribute \$140,000 before reflecting expected Medicare retiree drug subsidy payments in 2014.

17. Regulatory Matters

First Federal is subject to minimum capital adequacy guidelines. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators, which could have a material impact on First Federal's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, First Federal must maintain capital amounts in excess of specified minimum ratios based on quantitative measures of First Federal's assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting practices.

Quantitative measures to ensure capital adequacy require First Federal to maintain minimum amounts and ratios (as set forth in the table below) of total and Tier 1 capital (as defined in the regulations) to risk-weighted assets, and Tier 1 capital to adjusted total assets.

The following schedule presents First Defiance consolidated and First Federal's regulatory capital ratios as of December 31, 2013 and December 31, 2012:

	December 31, 2013									
	Actual				Minimum Required for Adequately Capitalized			Minimum Required for Well Capitalized		
	Amount	Ratio			Amount	Ratio		Amount	Ratio	
Tier 1 Capital (1)										
Consolidated	\$ 246,258	11.86	%		\$ 83,045	4.0	%	N/A	N/A	
First Federal	\$ 235,699	11.36	%		\$ 82,978	4.0	%	\$ 103,722	5.0	%
Tier 1 Capital (to Risk Weighted Assets) (1)										
Consolidated	\$ 246,258	13.98	%		\$ 70,473	4.0	%	N/A	N/A	
First Federal	\$ 235,699	13.39	%		\$ 70,418	4.0	%	\$ 105,627	6.0	%
Total Capital (to Risk Weighted Assets) (1)										
Consolidated	\$ 268,317	15.23	%		\$ 140,947	8.0	%	N/A	N/A	
First Federal	\$ 257,741	14.64	%		\$ 140,836	8.0	%	\$ 176,046	10.0	%

Core capital is computed as a percentage of adjusted total assets of \$2.08 billion and \$2.07 billion for consolidated (1) and the bank, respectively. Risk-based capital is computed as a percentage of total risk-weighted assets of \$1.76 billion and \$1.76 billion for consolidated and First Federal, respectively.

	December 31, 2012								
	Actual			Minimum Required for Adequately Capitalized			Minimum Required for Well Capitalized		
	Amount	Ratio		Amount	Ratio		Amount	Ratio	
Tier 1 Capital (1)									
Consolidated	\$ 226,931	11.48	%	\$ 79,056	4.0	%	N/A	N/A	
First Federal Bank	\$ 215,432	10.92	%	\$ 78,914	4.0	%	\$ 98,642	5.0	%

Tier 1 Capital (to
Risk
Weighted Assets)
(1)

Consolidated	\$	226,931	13.41	%	\$	67,715	4.0	%	N/A	N/A	
First Federal Bank	\$	215,432	12.74	%	\$	67,632	4.0	%	\$	101,448	6.0 %

Total Capital (to
Risk
Weighted Assets)
(1)

Consolidated	\$	248,161	14.66	%	\$	135,430	8.0	%	N/A	N/A	
First Federal Bank	\$	236,635	14.00	%	\$	135,264	8.0	%	\$	169,080	10.0 %

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Core capital is computed as a percentage of adjusted total assets of \$2.00 billion and \$1.99 billion for consolidated (1) and the bank, respectively. Risk-based capital is computed as a percentage of total risk-weighted assets of \$1.64 billion and \$1.64 billion for consolidated and First Federal, respectively.

Management believes that, as of December, 31, 2013, First Federal was “well capitalized” based on the ratios presented above. There are no conditions or events since the most recent notification from any of the regulatory agencies regarding those capital standards that management believes have changed any of the well capitalized categorizations of First Federal. First Defiance does not have capital requirements at this time.

First Federal is subject to the regulatory capital requirements administered by the OCC and FDIC. Regulatory authorities can initiate certain mandatory actions if First Federal fails to meet the minimum capital requirements, which could have a direct material effect on the Corporation’s financial statements. Management believes, as of December 31, 2013, that First Federal meets all capital adequacy requirements to which they are subject.

First Defiance is a unitary thrift holding company and is regulated by the Federal Reserve. First Defiance is subject to regulatory capital requirements under the Federal Reserve.

Dividend Restrictions - Dividends paid by First Federal to First Defiance are subject to various regulatory restrictions. First Federal paid \$3.0 million in dividends in 2013 and \$37.0 million in 2012. First Federal can initiate dividend payments equal to its net profits (as defined by statute) for 2012 and 2013 plus 2014 net profits. During 2014, First Federal can declare dividends in the amount of \$360,000 from its earnings in 2012 and 2013 and from any of its 2014 net profits to First Defiance. First Insurance paid \$1.5 million in dividends in 2013 and \$300,000 in dividends to First Defiance in 2012.

18. Income Taxes

The components of income tax expense are as follows:

	Years Ended December 31		
	2013	2012	2011
	(In Thousands)		
Current:			
Federal	\$ 7,751	\$ 7,862	\$ 3,714
State and local	9	(50)	(91)
Deferred	1,518	200	3,042
	\$ 9,278	\$ 8,012	\$ 6,665

The provision for income taxes differs from that computed at the statutory corporate tax rate as follows:

	Years Ended December 31		
	2013	2012	2011
	(In Thousands)		
Tax expense at statutory rate (35%)	\$ 11,030	\$ 9,337	\$ 7,769
Increases (decreases) in taxes from:			
State income tax net of federal tax benefit	4	(32)	(59)
Tax exempt interest income, net of TEFRA	(1,043)	(1,047)	(926)
Bank owned life insurance	(449)	(374)	(230)
Stock option expense	12	22	36
Captive insurance	(415)	-	-
Other	139	106	75
Totals	\$ 9,278	\$ 8,012	\$ 6,665

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Deferred federal income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes.

Significant components of First Defiance's deferred federal income tax assets and liabilities are as follows:

	December 31 2013 (In Thousands)	2012
Deferred federal income tax assets:		
Allowance for loan losses	\$ 8,798	\$ 9,349
Postretirement benefit costs	1,013	1,078
Deferred compensation	1,412	1,095
Impaired loans	986	1,531
Capital loss carry-forward	555	596
Impaired investments	971	846
Accrued vacation	581	499
Allowance for real estate held for sale losses	277	484
Deferred loan origination fees and costs	265	251
Other	718	844
Total deferred federal income tax assets	15,576	16,573
Deferred federal income tax liabilities:		
FHLB stock dividends	3,238	3,259
Goodwill	4,586	4,293
Mortgage servicing rights	3,211	2,742
Fixed assets	1,693	1,353
Other intangible assets	607	954
Loan mark to market	515	766
Net unrealized gains on available-for-sale securities	488	2,612
Prepaid expenses	617	464
Other	56	52
Total deferred federal income tax liabilities	15,011	16,495
Net deferred federal income tax asset (liability)	\$ 565	\$ 78

The realization of the Company's deferred tax assets is dependent upon the Company's ability to generate taxable income in future periods and the reversal of deferred tax liabilities during the same period and the ability to carryback any losses. The Company has evaluated the available evidence supporting the realization of its deferred tax assets and determined it is more likely than not that the assets will be realized and thus no valuation allowance was required at December 31, 2013.

At December 31, 2013, the Company had capital loss carry-forwards of \$1.7 million which will expire on December 31, 2014. No valuation allowance has been recorded as management has evaluated evidence supporting the realization of this asset and determined it is more likely than not that the asset will be realized.

Retained earnings at December 31, 2013 include approximately \$11.0 million for which no tax provision for federal income taxes has been made. This amount represents the tax bad debt reserve at December 31, 1987, which is the end of the Company's base year for purposes of calculating the bad debt deduction for tax purposes. If this portion of retained earnings is used in the future for any purpose other than to absorb bad debts, the amount used will be added to future taxable income. The unrecorded deferred tax liability on the above amount at December 31, 2013 was approximately \$3.85 million.

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A reconciliation of the beginning and ending amount of unrecognized tax benefits is as follows (in thousands):

Balance at January 1, 2011	\$ 281
Additions based on tax positions related to the current year	-
Additions for tax positions of prior years	-
Reductions for tax positions of prior years	-
Reductions due to the statute of limitations	(140)
Settlements	-
Balance at December 31, 2011	\$ 141
Balance at January 1, 2012	\$ 141
Additions based on tax positions related to the current year	-
Additions for tax positions of prior years	-
Reductions for tax positions of prior years	-
Reductions due to the statute of limitations	(76)
Settlements	-
Balance at December 31, 2012	\$ 65
Balance at January 1, 2013	\$ 65
Additions based on tax positions related to the current year	-
Additions for tax positions of prior years	-
Reductions for tax positions of prior years	-
Reductions due to the statute of limitations	(65)
Settlements	-
Balance at December 31, 2013	\$ -

The Company does not expect the total amount of unrecognized tax benefits to significantly increase in the next twelve months.

The total amount of interest and penalties recorded in the income statement, net of the related federal tax effect, for the year ended December 31, 2013 was a net reversal of \$26,000, and the amount accrued for interest and penalties (net of the related federal tax effect) at December 31, 2013 was zero.

The total amount of interest and penalties recorded in the income statement, net of the related federal tax effect, for the year ended December 31, 2012 was a net reversal of \$22,000, and the amount accrued for interest and penalties (net of the related federal tax effect) at December 31, 2012 was \$26,000.

The total amount of interest and penalties recorded in the income statement, net of the related federal tax effect, for the year ended December 31, 2011 was \$14,000, and the amount accrued for interest and penalties (net of the related federal tax effect) at December 31, 2011 was \$73,000.

The Company and its subsidiaries are subject to U.S. federal income tax as well as income tax in the state of Indiana. The Company is no longer subject to examination by taxing authorities for years before 2009. The Company currently operates primarily in the states of Ohio and Michigan, which tax financial institutions based on their equity rather than their income.

19. Employee Benefit Plans

401(k) Plan

Employees of First Defiance are eligible to participate in the First Defiance Financial Corp. 401(k) Employee Savings Plan (First Defiance 401(k)) if they meet certain age and service requirements. Beginning in 2009, under the First Defiance 401(k), First Defiance matches 100% of the participants' contributions up to 3% of compensation and then 50% of the participants' contributions for the next 2% of compensation. Previously, matching contributions were 50% of the first 3% of participants contributions. The First Defiance 401(k) also provides for a discretionary First Defiance contribution in addition to the First Defiance matching contribution. First Defiance matching contributions totaled \$868,000, \$799,000 and \$717,000 for the years ended December 31, 2013, 2012 and 2011, respectively. There were no discretionary contributions in any of those years.

Group Life Plan

On June 30, 2010, First Federal adopted the First Federal Bank of the Midwest Executive Group Life Plan Post Separation (the "Group Life Plan") in which various employees, including the Company's named executive officers, may participate. Under the terms of the Group Life Plan, First Federal will purchase and own life insurance policies covering the lives of employees selected by the board of directors of First Federal as participants. There was (\$35,000), \$76,000, and \$137,000 of expense recorded for the years ended December 31, 2013, 2012 and 2011, respectively, with a liability of \$724,000, \$760,000 and \$683,000 for future benefits recorded at December 31, 2013, 2012 and 2011, respectively. In 2013, management changed the discount rate to 4.75% to reflect the current interest rate environment which resulted in a reduction of the group life plan liability as of December 31, 2013.

20. Stock Compensation Plans

First Defiance has established equity based compensation plans for its directors and employees. On March 15, 2010, the Board adopted, and the shareholders approved at the 2010 Annual Shareholders Meeting, the First Defiance Financial Corp. 2010 Equity Incentive Plan (the "2010 Equity Plan"). The 2010 Equity Plan replaces all existing plans. All awards currently outstanding under prior plans will remain in effect in accordance with their respective terms. Any new awards will be made under the 2010 Equity Plan. The 2010 Equity Plan allows for issuance of up to 350,000 common shares through the award of options, stock grants, restricted stock units ("RSU"), stock appreciation rights or other stock-based awards.

As of December 31, 2013, 251,020 options have been granted pursuant to the 2010 equity plan and previous plans, and remain outstanding at option prices based on the market value of the underlying shares on the date the options were granted. Options granted under all plans vest 20% per year except for the 2009 grant to the Company's executive officers, which vested 40% in 2011 and then 20% annually. All options expire ten years from the date of grant. Vested options of retirees expire on the earlier of the scheduled expiration date or three months after the retirement date.

In August 2011, the Company approved a 2011 Short-Term ("STIP") Equity Incentive Plan and a 2011 Long-Term ("LTIP") Equity Incentive Plan for selected members of management. The Plans were effective January 1, 2011 and provide for cash and/or equity benefits if certain performance targets are achieved. Equity awards issued under these plans will reduce the amount of the awards available to be issued under the 2010 Equity Plan.

In March 2012, the Company approved a 2012 STIP and a 2012 LTIP for selected members of management. The plans were effective January 1, 2012 and provide for cash and/or equity benefits if certain performance targets are achieved. Equity awards issued under these plans will reduce the amount of awards available to be issued under the 2010 Equity Plan.

Under the 2011 and 2012 STIPs the participants may earn up to 25% to 45% of their salary for potential payout based on the achievement of certain corporate and/or market area performance targets during the calendar year. The final value of the awards to be made under the 2012 STIP will be determined as of December 31 of each year and will be paid out in cash and/or equity, as elected by the participant, in accordance with the following vesting schedule: 50% in the first quarter after the calendar year, 25% on the one-year anniversary of the grant date, and 25% on the second-year anniversary. The participants are required to be employed on the day of payout in order to receive an award. In December 2012, the Company amended the 2011 STIP and accelerated the payout, so that the remaining 50% of the award was paid in December 2012, rather than 25% at the beginning of 2013 and 25% at the beginning of 2014.

Under the 2011 and 2012 LTIPs the participants may earn up to 25% to 45% of their salary for potential payout based on the achievement of certain corporate performance targets either over a two or three year period. The final amount of benefit under the 2011 LTIP was determined as of December 31, 2012 and the final amount of benefit under the 2012 LTIP will be determined as of December 31, 2014. The benefits earned under the plans will be paid out in cash and/or equity, as elected by the participant, in the first quarter following the close of the performance period. The participants are required to be employed on the day of payout in order to receive the payment.

In March 2013, the Company approved a 2013 STIP and a 2013 LTIP for selected members of management. Under the 2013 STIP the participants may earn up to 25% to 45% of their salary for potential payout based on the achievement of certain corporate performance targets during the calendar year. The final amount of awards earned under the 2013 STIP will be determined as of December 31, 2013 and will be paid out in cash in the first quarter of 2014. The participants are required to be employed on the day of payout in order to receive such payment.

Under the 2013 LTIP the participants may earn up to 25% to 45% of their salary, depending upon their position, for potential payout in the form of equity awards based on the achievement of certain corporate performance targets over a three year period. The Company granted 86,065 RSUs to the participants in this plan effective January 1, 2013, which represents the maximum target award. The amount of benefit under the 2013 LTIP will be determined individually at the 12 month period ending December 31, 2013, the 24 month period ending December 31, 2014 and the 36 month period ending December 31, 2015. The awards' vesting will be as follows: 16.7% of the target award after the end of the performance period ending December 31, 2013, 27.8% of the target award at the end of the performance period ending December 31, 2014 and 55.5% of the target award at the end of the performance period ending December 31, 2015. The RSUs shall vest between 0% and 100% of the applicable portion of the target award based on the portion of the performance targets that are achieved. RSUs settle in common shares in the first quarter following the close of the applicable performance period. The participants are required to be employed on the day of payout in order to receive the payment. Equity awards issued under these plans will reduce the amount of awards available to be issued under the 2010 Equity Plan.

The fair value of each option award is estimated on the date of grant using the Black-Scholes model. Expected volatilities are based on historical volatilities of the Company's common shares. The Company uses historical data to estimate option exercise and post-vesting termination behavior. The expected term of options granted is based on historical data and represents the period of time that options granted are expected to be outstanding, which takes into account that the options are not transferable. The risk-free interest rate for the expected term of the option is based on the U.S. Treasury yield curve in effect at the time of the grant. There were no stock options granted in 2013, 2012 or 2011.

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Following is activity under the plans during 2013:

Stock options:	Options Outstanding	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value (in 000's)
Options outstanding, January 1, 2013	312,350	\$ 20.33		
Forfeited or cancelled	(22,000)	22.31		
Exercised	(39,330)	16.55		
Granted	-	-		
Options outstanding, December 31, 2013	251,020	\$ 20.75	3.16	\$ 1,415
Vested or expected to vest at December 31, 2013	251,020	\$ 20.75	3.16	\$ 1,415
Exercisable at December 31, 2013	240,350	\$ 21.26	3.06	\$ 1,239

Information related to the stock option plans follows:

	Year Ended December 31		
	2013	2012	2011
	(in thousands, except per share amounts)		
Intrinsic value of options exercised	\$ 310	\$ 4	\$ 1
Cash received from option exercises	350	5	11
Tax benefit realized from option exercises	54	-	-
Weighted average fair value of options granted	-	-	-

As of December 31, 2013, there was \$6,000 of total unrecognized compensation costs related to unvested stock options granted under the Company's equity plans. The cost is expected to be recognized over a weighted-average period of 0.3 years.

At December 31, 2013, 106,061 RSU's were outstanding. Compensation expense is recognized over the performance period based on the achievement of established targets. Total expense of \$1.0 million, \$677,000 and \$492,000 was recorded during the years ended December 31, 2013, 2012 and 2011, respectively, and approximately \$540,000 and \$530,000 is included within other liabilities at December 31, 2013 and 2012, respectively, related to the STIPs and LTIPs.

	Restricted Stock Units		Stock Grants	
Unvested Shares	Shares	Weighted-Average Grant Date Fair Value	Shares	Weighted-Average Grant Date Fair Value
Unvested at January 1, 2013	38,871	\$ 14.74	11,260	\$ 13.28
Granted	91,187	19.42	20,639	15.77
Vested	(20,639)	15.77	(31,899)	14.89
Forfeited	(3,358)	11.97	-	-
Unvested at December 31, 2013	106,061	\$ 18.66	-	\$ -

The maximum amount of compensation expense that may be earned for the 2013 STIP and the 2012 and 2013 LTIPs at December 31, 2013 is approximately \$2.9 million. However, the estimated expense expected to be earned as of December 31, 2013 based on the performance measures in the plans, is \$1.9 million of which \$787,000 is

unrecognized at December 31, 2013 and will be recognized over the remaining performance period.

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As of December 31, 2013 and 2012, 202,405 and 290,234 shares, respectively, were available for grant under the Company's stock option plans. Options forfeited or cancelled under all plans except the 2010 plan are no longer available for grant to other participants.

21. Parent Company Statements

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Condensed parent company financial statements, which include transactions with subsidiaries, follow:

Statements of Financial Condition	December 31	
	2013	2012
	(In Thousands)	
Assets		
Cash and cash equivalents	\$ 8,228	\$ 8,884
Available for Sale Securities	-	1,002
Investment in banking subsidiary	285,813	270,444
Investment in non-bank subsidiaries	13,518	13,034
Other assets	1,774	1,766
Total assets	\$ 309,333	\$ 295,130
Liabilities and stockholders' equity:		
Subordinated debentures	\$ 36,083	\$ 36,083
Accrued liabilities	1,103	919
Stockholders' equity	272,147	258,128
Total liabilities and stockholders' equity	\$ 309,333	\$ 295,130

Statements of Income	Years Ended December 31		
	2013	2012	2011
	(In Thousands)		
Dividends from subsidiaries	\$ 4,500	\$ 37,300	\$ -
Interest on investments	18	12	8
Interest expense	(601)	(971)	(1,278)
Other income	1	-	1
Noninterest expense	(853)	(1,013)	(690)
Income (loss) before income taxes and equity in earnings of subsidiaries	3,065	35,328	(1,959)
Income tax credit	(415)	(669)	(665)
Income (loss) before equity in earnings of subsidiaries	3,480	35,997	(1,294)
Undistributed equity in (distributions in excess of) earnings of subsidiaries	18,755	(17,333)	16,828
Net income	\$ 22,235	\$ 18,664	\$ 15,534
Comprehensive income	\$ 18,506	\$ 18,941	\$ 19,873

Statements of Cash Flows	Years Ended December 31		2011
	2013	2012	
	(In Thousands)		
Operating activities:			
Net income	\$ 22,235	\$ 18,664	\$ 15,534
Adjustments to reconcile net income to net cash (used in) provided by operating activities:			
Distribution in excess of (undistributed equity in) earnings of subsidiaries	(18,755)	17,333	(16,828)
Change in other assets and liabilities	176	97	109
Net cash provided by (used in) operating activities	3,656	36,094	(1,185)
Investing activities:			
Investment in non-bank subsidiary	-	(250)	(4,785)
Purchase of available-for-sale securities	-	-	(2,000)
Sale of available-for-sale securities	1,002	1,000	-
Net cash (used in) provided by investing activities	1,002	750	(6,785)
Financing activities:			
Repurchase of common stock	(1,821)	-	-
Cash dividends paid	(3,907)	(3,086)	(2,331)
Stock Options Exercised	350	4	11
Treasury stock sales	64	14	29
Proceeds from issuance of common stock	-	-	19,859
Preferred Stock payoff	-	(36,358)	-
Net cash used in financing activities	(5,314)	(39,426)	17,568
Net increase (decrease) in cash and cash equivalents	(656)	(2,582)	9,598
Cash and cash equivalents at beginning of year	8,884	11,466	1,868
Cash and cash equivalents at end of year	\$ 8,228	\$ 8,884	\$ 11,466

22. Fair Value

FASB ASC Topic 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. A fair value measurement assumes that the transaction to sell the asset or transfer the liability occurs in the principal market for the asset or liability or, in the absence of a principal market, the most advantageous market for the asset or liability. The price in the principal (or most advantageous) market used to measure the fair value of the asset or liability shall not be adjusted for transaction costs. An orderly transaction is a transaction that assumes exposure to the market for a period prior to the measurement date to allow for marketing activities that are usual and customary for transactions involving such assets and liabilities; it is not a forced transaction. Market participants are buyers and sellers in the principal market that are (i) independent, (ii) knowledgeable, (iii) able to transact and (iv) willing to transact.

FASB ASC Topic 820 requires the use of valuation techniques that are consistent with the market approach, the income approach and/or the cost approach. The market approach uses prices and other relevant information generated

by market transactions involving identical or comparable assets and liabilities. The income approach uses valuation techniques to convert future amounts, such as cash flows or earnings, to a single present amount on a discounted basis. The cost approach is based on the amount that currently would be required to replace the service capacity of an asset (replacement cost). Valuation techniques should be consistently applied. Inputs to valuation techniques refer to the assumptions that market participants would use in pricing the asset or liability. Inputs may be observable, meaning those that reflect the assumptions market participants would use in pricing the asset or liability developed based on the best information available. In that regard, FASB ASC Topic 820 established a fair value hierarchy for valuation inputs that gives the highest priority to quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. The fair value hierarchy is as follows:

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

Level 2: Inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. These might include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability (such as interest rates, prepayment speeds, credit risks, etc.) or inputs that are derived principally from or corroborated by market data by a correlation or other means.

Level 3: Unobservable inputs for determining fair value of assets and liabilities that reflect an entity's own assumptions about the assumptions that market participants would use in pricing the assets or liabilities.

A description of the valuation methodologies used for instruments measured at fair value, as well as the general classification of such instruments pursuant to the valuation hierarchy, is set forth below.

Available for sale securities - Securities classified as available for sale are generally reported at fair value utilizing Level 2 inputs where the Company obtains fair value measurements from an independent pricing service that uses matrix pricing, which is a mathematical technique widely used in the industry to value debt securities without relying exclusively on quoted prices for the specific securities but rather by relying on the securities' relationship to other benchmark quoted securities (Level 2 inputs). The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows and the bonds' terms and conditions, among other things. Securities in Level 1 include federal agency preferred stock securities. Securities in Level 2 include U.S. Government agencies, mortgage-backed securities, corporate bonds and municipal securities. The Company classifies its pooled trust preferred collateralized debt obligations as Level 1 and Level 3. The portfolio consists of collateralized debt obligations backed by pools of trust preferred securities issued by financial institutions and insurance companies. Two collateralized debt obligations backed by insurance companies were classified as Level 1 at December 31, 2013 due to receiving a Level 1 price at which the securities were subsequently sold on January 15, 2014 as a result of these securities being disallowed under the final interim Volcker rule that was announced January 14, 2014. The two collateralized debt obligations backed by financial institutions are allowed under the final interim Volcker Rule and classified as Level 3 based on the lack of observable market data, the Company estimated fair values based on the observable data available and reasonable unobservable market data. The Company estimated fair value based on a discounted cash flow model, which used appropriately adjusted discount rates reflecting credit and liquidity risks. The Company used an independent third party, which is described further in Note 7.

Impaired loans - Fair values for impaired collateral dependent loans are generally based on appraisals obtained from licensed real estate appraisers and in certain circumstances consideration of offers obtained to purchase properties prior to foreclosure. Appraisals for commercial real estate generally use three methods to derive value: cost, sales or market comparison and income approach. The cost method bases value on the cost to replace the current property. Value of market comparison approach evaluates the sales price of similar properties in the same market area. The income approach considers net operating income generated by the property and an investors required return. Adjustments are routinely made in the appraisal process by the independent appraisers to adjust for differences between the comparable sales and income data available. Comparable sales adjustments are based on known sales prices of similar type and similar use properties and duration of time that the property has been on the market to sell. Such adjustments made in the appraisal process are typically significant and result in a Level 3 classification of the inputs for determining fair value.

Real Estate held for sale - 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 then reviewed monthly by members of the asset review committee for valuation changes and are accounted for at lower of cost or fair value less estimated costs to sell. Fair value is commonly based on recent real estate appraisals which may utilize a single valuation approach or a combination of approaches including cost, 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 may be significant and typically result in a Level 3 classification of the inputs for determining fair value.

Appraisals for both collateral-dependent impaired loans and other real estate owned are performed by certified general appraisers (for commercial properties) or certified residential appraisers (for residential properties) whose qualifications and licenses have been reviewed and verified by the Company. Once received, a member of the Company's asset quality or collections department reviews the assumptions and approaches utilized in the appraisal. Appraisal values are discounted from 0% to 20% to account for other factors that may impact the value of collateral. In determining the value of impaired collateral dependent loans and other real estate owned, significant unobservable inputs may be used, which include: physical condition of comparable properties sold, net operating income generated by the property and investor rates of return.

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

Mortgage banking derivative - The fair value of mortgage banking derivatives are evaluated monthly based on derivative valuation models using quoted prices for similar assets adjusted for specific attributes of the commitments and other observable market data at the valuation date (Level 2).

The following table summarizes the financial assets measured at fair value on a recurring basis segregated by the level of the valuation inputs within the fair value hierarchy utilized to measure fair value:

Assets and Liabilities Measured on a Recurring Basis

December 31, 2013	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total Fair Value
(In Thousands)				
Available for sale securities:				
Obligations of U.S. Government corporations and agencies	\$ -	\$ 4,921	\$ -	\$ 4,921
Mortgage-backed - residential	-	41,292	-	41,292
Collateralized mortgage obligations	-	59,841	-	59,841
Trust preferred stock	1,654	-	582	2,236
Preferred stock	718	-	-	718
Corporate bonds	-	8,942	-	8,942
Obligations of state and political subdivisions	-	80,220	-	80,220
Mortgage banking derivative - asset	-	295	-	295
Mortgage banking derivative - liability	-	-	-	-
December 31, 2012	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total Fair Value
(In Thousands)				
Available for sale securities:				
Obligations of U.S. Government corporations and agencies	\$ -	\$ 11,069	\$ -	\$ 11,069
U.S. treasury bonds	-	1,002	-	1,002
Mortgage-backed - residential	-	31,461	-	31,461
Collateralized mortgage obligations	-	57,466	-	57,466
Trust preferred stock	-	-	1,474	1,474
Preferred stock	134	-	-	134
Corporate bonds	-	8,884	-	8,884
Obligations of state and political subdivisions	-	82,611	-	82,611
Mortgage banking derivative - asset	-	950	-	950
Mortgage banking derivative - liability	-	(94)	-	(94)

Trust preferred stock in the amount of \$1,654,000 was transferred from level 3 to level 1 in 2013 due to two securities being disallowed under the final interim Volcker Rule resulting in the company selling these two securities on January 15, 2014 after obtaining a Level 1 price. The selling price (Level 1) was used to determine the fair value at December 31, 2013. There were no transfers between Levels during the period ended December 31, 2012.

The table below presents a reconciliation and income classification of gains and losses for all assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the years ended December 31, 2013 and 2012:

Fair Value Measurements Using Significant
Unobservable Inputs (Level 3)

(In Thousands)

	2013	2012
Beginning balance	\$ 1,474	\$ 1,342
Total gains or losses (realized/unrealized)		
Included in earnings (realized)	(337)	76
Included in other comprehensive income (presented gross of taxes)	1,099	322
Amortization	-	-
Redemption	-	(266)
Transfers in and/or out of Level 3	(1,654)	-
Ending balance	\$ 582	\$ 1,474

Changes in Unrealized Gains/Losses Recorded in Earnings
For the Year Relating to Level 3 Assets Still Held at Reporting
Date for the Year Ended December 31
(In Thousands)

Trust Preferred Stock

	2013	2012	2011
Interest income on securities	\$ 83	\$ 160	\$ 71
Other changes in fair value	(420)	(84)	(73)
Total	\$ (337)	\$ 76	\$ (2)

The following table summarizes the financial assets measured at fair value on a non-recurring basis segregated by the level of the valuation inputs within the fair value hierarchy utilized to measure fair value:

Assets and Liabilities Measured on a Non-Recurring Basis

December 31, 2013	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total Fair Value
(In Thousands)				
Impaired loans				
1-4 Family Residential Real Estate	\$ -	\$ -	\$ 259	\$ 259
Multi Family Residential	-	-	338	338
Commercial Real Estate	-	-	9,590	9,590
Home Equity and Improvement	-	-	531	531
Total impaired loans	-	-	10,718	10,718
Mortgage servicing rights	-	1,370	-	1,370
Real estate held for sale				
Residential	-	-	112	112
CRE	-	-	1,278	1,278
Total Real Estate held for sale	-	-	1,390	1,390
December 31, 2012	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total Fair Value
(In Thousands)				
Impaired loans				
1-4 Family Residential Real Estate	\$ -	\$ -	\$ 599	\$ 599
Multi Family Residential	-	-	407	407
Commercial Real Estate	-	-	12,126	12,126
Commercial	-	-	771	771
Home Equity and Improvement	-	-	168	168
Total Impaired loans	-	-	14,071	14,071
Mortgage servicing rights	-	7,833	-	7,833
Real estate held for sale				
Residential	-	-	61	61
CRE	-	-	385	385
Total Real Estate held for sale	-	-	446	446

For Level 3 assets and liabilities measured at fair value on a recurring or nonrecurring basis as of December 31, 2013, the significant unobservable inputs used in the fair value measurements were as follows:

	Fair Value	Valuation Technique	Unobservable Inputs	Range of Inputs		Weighted Average	
(Dollars in Thousands)							
Trust preferred stock	\$ 582	Discounted cash flow	Constant prepayment rate	2-40	%	40	%
			Expected asset default	0-30	%	15	%
			Expected recoveries	10-15	%	10	%
Impaired Loans- Applies to all loan classes	\$ 10,718	Appraisals which utilize sales comparison, net income and cost approach	Discounts for collection issues and changes in market conditions	0-10	%	10	%
Real estate held for sale Applies to all classes	\$ 1,390	Appraisals which utilize sales comparison, net income and cost approach	Discounts for changes in market conditions	0-20	%	20	%

For Level 3 assets and liabilities measured at fair value on a recurring or nonrecurring basis as of December 31, 2012, the significant unobservable inputs used in the fair value measurements were as follows:

	Fair Value	Valuation Technique	Unobservable Inputs	Range of Inputs		Weighted Average	
(Dollars in Thousands)							
Trust preferred stock	\$ 1,474	Discounted cash flow	Constant prepayment rate	2-40	%	40	%
			Expected asset default	0-30	%	15	%
			Expected recoveries	10-15	%	10	%
Impaired Loans- Applies to all loan classes	\$ 14,071	Appraisals which utilize sales comparison, net income and cost approach	Discounts for collection issues and changes in market conditions	0-10	%	10	%
Real estate held for sale Applies to all classes	\$ 446	Appraisals which utilize sales comparison, net	Discounts for changes in market conditions	0-20	%	20	%

income and cost
approach

Impaired loans, which are measured for impairment using the fair value of the collateral for collateral dependent loans, had a fair value of \$10.7 million, with no valuation allowance and a fair value of \$14.1 million with no valuation allowance at December 31, 2013 and 2012. A provision expense of \$3.2 million and \$6.3 million for the years ended December 31, 2013 and 2012 related to these impaired loans was included in earnings.

Mortgage servicing rights, which are carried at the lower of cost or fair value, had a fair value of \$1.4 million with a valuation allowance of \$1.0 million and a fair value of \$7.8 million with a valuation allowance of \$2.3 million at December 31, 2013 and 2012, respectively. A recovery of \$1.3 million and a charge of \$759,000 for the years ended December 31, 2013 and 2012 was included in earnings.

Real estate held for sale is determined using Level 3 inputs which include appraisals and are adjusted for changes in market conditions. The change in fair value of real estate held for sale was \$740,000 and \$416,000 for the years ended December 31, 2013 and 2012 which was recorded directly as an adjustment to current earnings through non-interest expense.

In accordance with FASB ASC Topic 825, the Fair Value Measurements tables are a comparative condensed consolidated statement of financial condition based on carrying amount and estimated fair values of financial instruments as of December 31, 2013 and December 31, 2012. Accordingly, the aggregate fair value amounts presented do not represent the underlying value of First Defiance.

Much of the information used to arrive at “fair value” is highly subjective and judgmental in nature and therefore the results may not be precise. Subjective factors include, among other things, estimated cash flows, risk characteristics and interest rates, all of which are subject to change. With the exception of investment securities, the Company’s financial instruments are not readily marketable and market prices do not exist. Since negotiated prices for the instruments, which are not readily marketable, depend greatly on the motivation of the buyer and seller, the amounts that will actually be realized or paid per settlement or maturity of these instruments could be significantly different.

The carrying amount of cash and cash equivalents, term notes payable and advance payments by borrowers for taxes and insurance, as a result of their short-term nature, is considered to be equal to fair value and are classified as Level 1.

It was not practicable to determine the fair value of Federal Home Loan Bank (“FHLB”) stock due to restrictions placed on its transferability.

The fair value of loans that reprice within 90 days is equal to their carrying amount. For other loans, the estimated fair value is calculated based on discounted cash flow analysis, using interest rates currently being offered for loans with similar terms, resulting in a Level 3 classification. Impaired loans are valued at the lower of cost or fair value as previously described. The allowance for loan losses is considered to be a reasonable adjustment for credit risk. The methods utilized to estimate the fair value of loans do not necessarily represent an exit price. The fair value of loans held for sale is estimated based on binding contracts and quotes from third party investors resulting in a Level 2 classification.

The fair value of accrued interest receivable is equal to the carrying amounts resulting in a Level 2 or Level 3 classification, which is consistent with its underlying value.

The fair value of non-interest bearing deposits are considered equal to the amount payable on demand at the reporting date (i.e., carrying value) and are classified as Level 1. The fair value of savings, NOW and certain money market accounts are equal to their carrying amounts and are a Level 2 classification. Fair values of fixed rate certificates of deposit are estimated using a discounted cash flow calculation that applies interest rates currently being offered on certificates to a schedule of aggregated expected monthly maturities on time deposits resulting in a Level 2 classification.

The fair values of securities sold under repurchase agreements are equal to their carrying amounts resulting in a Level 2 classification. The carrying value of subordinated debentures and deposits with fixed maturities is estimated based on discounted cash flow analyses based on interest rates currently being offered on instruments with similar characteristics and maturities resulting in a Level 3 classification.

FHLB advances with maturities greater than 90 days are valued based on discounted cash flow analysis, using interest rates currently being quoted for similar characteristics and maturities resulting in a Level 2 classification. The cost or value of any call or put options is based on the estimated cost to settle the option at December 31, 2013.

Fair Value Measurements at December 31, 2013
(In Thousands)

	Carrying Value	Total	Level 1	Level 2	Level 3
Financial Assets:					
Cash and cash equivalents	\$ 179,318	\$ 179,318	\$ 179,318	\$ -	\$ -
Investment securities	198,557	198,563	2,372	195,609	582
Federal Home Loan Bank Stock	19,350	N/A	N/A	N/A	N/A
Loans, net, including loans held for sale	1,564,618	1,568,929	-	9,140	1,559,789
Accrued interest receivable	5,778	5,778	4	696	5,078
Financial Liabilities:					
Deposits	\$ 1,735,792	\$ 1,738,216	\$ 348,943	\$ 1,389,273	\$ -
Advances from Federal Home Loan Bank	22,520	22,713	-	22,713	-
Securities sold under repurchase agreements	51,919	51,919	-	51,919	-
Subordinated debentures	36,083	35,237	-	-	35,237

Fair Value Measurements at December 31, 2012
(In Thousands)

	Carrying Value	Total	Level 1	Level 2	Level 3
Financial Assets:					
Cash and cash equivalents	\$ 136,832	\$ 136,832	\$ 136,832	\$ -	\$ -
Investment securities	194,609	194,617	134	193,009	1,474
Federal Home Loan Bank Stock	20,655	N/A	N/A	N/A	N/A
Loans, net, including loans held for sale	1,520,610	1,543,438	-	22,577	1,520,861
Accrued interest receivable	5,594	5,594	-	757	4,837
Financial Liabilities:					
Deposits	\$ 1,667,472	\$ 1,671,713	\$ 315,132	\$ 1,356,581	\$ -
Advances from Federal Home Loan Bank	12,796	13,466	-	13,466	-
Securities sold under repurchase	51,702	51,702	-	51,702	-

agreements					
Subordinated					
debentures	36,083	35,766	-	-	35,766

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23. Derivative Financial Instruments

Commitments to fund certain mortgage loans (interest rate locks) to be sold into the secondary market and forward commitments for the future delivery of mortgage loans to third party investors are considered derivatives. It is the Company's practice to enter into forward commitments for the future delivery of residential mortgage loans when interest rate lock commitments are entered into in order to economically hedge the effect of changes in interest rates resulting from its commitments to fund the loans. These mortgage banking derivatives are not designated in hedge relationships. First Federal had approximately \$7.5 million and \$34.0 million of interest rate lock commitments at December 31, 2013 and 2012, respectively. There were \$12.1 million and \$53.6 million of forward commitments for the future delivery of residential mortgage loans at December 31, 2013 and 2012, respectively.

The fair value of these mortgage banking derivatives are reflected by a derivative asset or a derivative liability. The table below provides data about the carrying values of these derivative instruments:

	December 31, 2013			December 31, 2012		
	Assets	(Liabilities)	Derivative	Assets	(Liabilities)	Derivative
	Carrying	Carrying	Net Carrying	Carrying	Carrying	Net Carrying
	Value	Value	Value	Value	Value	Value
	(In Thousands)					
Derivatives not designated as hedging instruments						
Mortgage Banking Derivatives	\$ 295	\$ -	\$ 295	\$ 950	\$ (94)	\$ 856

The table below provides data about the amount of gains and losses recognized in income on derivative instruments not designated as hedging instruments:

	Twelve Months Ended December 31,		
	2013	2012	2011
	(In Thousands)		
Derivatives not designated as hedging instruments			
Mortgage Banking Derivatives	Gain (Loss)	\$ (526)	\$ 249
			\$ 252

The above amounts are included in mortgage banking income with gain on sale of mortgage loans. During 2013 and 2011, management determined that a group of loans, previously classified as held for sale, were no longer sellable and were transferred back into the portfolio. As a result, a \$34,000 and \$90,000 loss related to a fair value adjustment on those loans was recorded in 2013 and 2011, respectively. No such adjustments were made in 2012.

24. Quarterly Consolidated Results of Operations (Unaudited)

The following is a summary of the quarterly consolidated results of operations:

	Three Months Ended			
	March 31	June 30	September 30	December 31
(In Thousands, Except Per Share Amounts)				
2013				
Interest income	\$ 18,476	\$ 18,732	\$ 18,836	\$ 18,737
Interest expense	1,949	1,814	1,680	1,727
Net interest income	16,527	16,918	17,156	17,010
Provision for loan losses	425	448	476	475
Net interest income after provision for loan losses	16,102	16,470	16,680	16,535
Gain on sale, call or write-down of securities	53	44	-	(337)
Noninterest income	8,909	7,804	7,289	6,808
Noninterest expense	17,199	15,674	16,045	15,926
Income before income taxes	7,865	8,644	7,924	7,080
Income taxes	2,306	2,535	2,445	1,992
Net income	\$ 5,559	\$ 6,109	\$ 5,479	\$ 5,088
Dividends declared on Preferred Shares	-	-	-	-
Accretion on Preferred Shares	-	-	-	-
Net income applicable to common shares	\$ 5,559	\$ 6,109	\$ 5,479	\$ 5,088
Earnings per common share:				
Basic	\$ 0.57	\$ 0.63	\$ 0.56	\$ 0.52
Diluted	\$ 0.55	\$ 0.60	\$ 0.54	\$ 0.50
Average shares outstanding:				
Basic	9,736	9,774	9,780	9,766
Diluted	10,105	10,156	10,212	10,198

	Three Months Ended			
	March 31	June 30	September 30	December 31
	(In Thousands, Except Per Share Amounts)			
2012				
Interest income	\$ 20,754	\$ 20,519	\$ 20,098	\$ 19,572
Interest expense	3,555	3,273	2,923	2,186
Net interest income	17,199	17,246	17,175	17,386
Provision for loan losses	3,503	4,097	705	2,619
Net interest income after provision for loan losses	13,696	13,149	16,470	14,767
Gain on sale, call or write-down of securities	43	382	103	1,606
Noninterest income	8,376	7,612	7,677	8,575
Noninterest expense	16,259	15,532	16,450	17,539
Income before income taxes	5,856	5,611	7,800	7,409
Income taxes	1,703	1,690	2,366	2,253
Net income	\$ 4,153	\$ 3,921	\$ 5,434	\$ 5,156
Dividends declared on Preferred Shares	(462)	(435)	(3)	-
Accretion on Preferred Shares	(46)	(305)	(8)	-
Redemption of Preferred Shares	-	642	-	-
Net income applicable to common shares	\$ 3,645	\$ 3,823	\$ 5,423	\$ 5,156
Earnings per common share:				
Basic	\$ 0.37	\$ 0.39	\$ 0.56	\$ 0.53
Diluted	\$ 0.37	\$ 0.38	\$ 0.54	\$ 0.52
Average shares outstanding:				
Basic	9,726	9,729	9,729	9,729
Diluted	9,970	9,985	10,000	10,012

25. Preferred Stock

On December 5, 2008, as part of the Capital Purchase Program (“CPP”), the Company entered into a Letter Agreement and Securities Purchase Agreement (collectively, the “Purchase Agreement”) with the U.S. Treasury, pursuant to which the Company sold \$37.0 million shares of newly authorized Fixed Rate Cumulative Perpetual Preferred Stock, par value \$0.01 per share and liquidation value \$1,000 per share (“Senior Preferred Shares”) and also issued warrants (the “Warrants”) to the U.S. Treasury to acquire an additional 550,595 of common shares having an exercise price of \$10.08 per share. The Warrants have a term of 10 years.

The Senior Preferred Shares qualified as Tier 1 capital and paid cumulative dividends at a rate of 5% per annum for the first five years, and 9% per annum thereafter. The Senior Preferred Shares could be redeemed by the Company after three years. The Senior Preferred Shares were not subject to any contractual restrictions on transfer, except that the U.S. Treasury or any its transferees may affect any transfer that, as a result of such transfer, would require the Company to become subject to the periodic reporting requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934.

Pursuant to the terms of the Purchase Agreement, the ability of the Company to declare or pay dividends or distributions on, or purchase, redeem or otherwise acquire for consideration, its common shares was subject to restrictions, including a restriction against increasing dividends from the last quarterly cash dividend per share of \$0.26 declared on the common stock prior to October 14, 2008. The redemption, purchase or other acquisition of trust

preferred securities of the Company or its affiliates also was restricted.

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The Purchase Agreement also subjected the Company to certain of the executive compensation limitations included in the Emergency Economic Stabilization Act of 2008 (the “EESA”). As a condition to the closing of the transaction, the Company’s Senior Executive Officers (as defined in the Purchase Agreement) (the “Senior Executive Officers”), (i) voluntarily waived any claim against the U.S. Treasury or the Company for any changes to such officer’s compensation or benefits that are required to comply with the regulation issued by the U.S. Treasury under the CPP and acknowledged that the regulation may require modification of the compensation, bonus, incentive and other benefit plans, arrangements and policies and agreements as they relate to the period the U.S. Treasury owns the Senior Preferred Shares of the Company; and (ii) entered into a letter agreement with the Company amending the Benefit Plans with respect to such Senior Executive Officers as may be necessary, during the period that the U.S. Treasury owns the Senior Preferred Shares, as necessary to comply with Section 111(b) of the EESA.

In June 2012, the U.S. Treasury sold its preferred shares of the Company through a public offering structured as a modified Dutch auction. The Company bid on its preferred shares in the auction after receiving approval from its regulators. The clearing price per preferred share was \$962.66 (compared to a par value of \$1,000.00 per share) and the Company was successful in repurchasing 16,560 of the 37,000 preferred shares outstanding through the auction process. The Company also acquired an additional 19,440 preferred shares in the secondary market prior to the end of the second quarter of 2012. The remaining 1,000 outstanding preferred shares were purchased at par value on July 18, 2012. The clearing prices per preferred share purchased in the secondary market were as follows: 1,100 shares at \$997.50, 2,500 shares at \$1,000.00 and 16,840 shares at \$998.75.

The net balance sheet impact was a reduction to stockholders’ equity of \$36.4 million which is comprised of a decrease in preferred stock of \$37.0 million and a \$642,000 increase to retained earnings related to the discount on the shares repurchased, which is also included in net income applicable to common shares for purposes of calculating earnings per share.

Included in the 2012 operating results is \$181,000 of costs incurred by the Company related to the U.S. Treasury’s offering. All these costs were incurred in the second quarter of 2012. These costs are not tax-deductible.

26. Balance Sheet Restructure

In October 2012, the Company executed a balance sheet restructuring strategy to enhance the Company’s current and future profitability while increasing its capital ratios and protecting the balance sheet against rising rates. The strategy required taking an after tax loss of approximately \$260,000 through selling \$60.0 million in securities for a gain of \$1.6 million and paying off \$62.0 million in FHLB advances with a prepayment penalty of \$2.0 million.

27. Other Comprehensive Income (Loss)

The before and after tax amounts allocated to each component of other comprehensive income (loss) are presented in the table below. Reclassification adjustments related to securities available for sale are included in gains on sale or call of securities and OTTI losses on investment securities in the accompanying consolidated condensed statements of income.

	Before Tax Amount	Tax Expense (Benefit)	Net of Tax Amount
Twelve months ended December 31, 2013:	(In Thousands)		
Securities available for sale and transferred securities:			
Change in net unrealized gain/loss during the period	\$ (6,309)	\$ (2,216)	\$ (4,093)
Reclassification adjustment for net (gains) losses included in net income	240	92	148
Change in postretirement benefit obligation	333	117	216
Total other comprehensive income (loss)	\$ (5,736)	\$ (2,007)	\$ (3,729)
	Before Tax Amount	Tax Expense (Benefit)	Net of Tax Amount
Twelve months ended December 31, 2012:	(In Thousands)		
Securities available for sale and transferred securities:			
Change in net unrealized gain/loss during the period	\$ 2,360	\$ 846	\$ 1,514
Reclassification adjustment for net (gains) losses included in net income	(2,134)	(767)	(1,367)
Change in postretirement benefit obligation	199	69	130
Total other comprehensive income (loss)	\$ 425	\$ 148	\$ 277

Activity in accumulated other comprehensive income (loss), net of tax, was as follows:

	Securities Available For Sale (In Thousands)	Post- retirement Benefit	Accumulated Other Comprehensive Income
Balance January 1, 2013	\$ 4,851	\$ (577)	\$ 4,274
Other comprehensive loss before reclassifications	(4,093)	216	(3,877)
Amounts reclassified from accumulated other comprehensive loss	148	-	148
Net other comprehensive loss during period	(3,945)	216	(3,729)
Balance December 31, 2013	\$ 906	\$ (361)	\$ 545
Balance January 1, 2012	\$ 4,704	\$ (707)	\$ 3,997
Other comprehensive loss before reclassifications	1,514	130	1,644
Amounts reclassified from accumulated other	(1,367)	-	(1,367)

comprehensive loss

Net other comprehensive loss during period	147	130	277
Balance December 31, 2012	\$ 4,851	\$ (577)	\$ 4,274

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28. Subsequent Event

On February 18, 2014, the Company announced the signing of a definitive agreement to acquire First Community Bank (FCB"). Under the merger agreement First Federal will acquire FCB in a cash transaction in which FCB will merge with and into First Federal. FCB operates four branches in the Columbus, Ohio market and at December 31, 2013, had assets of \$101.4 million (unaudited), loans of \$65.4 million (unaudited), deposits of \$90.5 million (unaudited) and common equity of \$10.6 million (unaudited). Under the terms of the merger agreement, First Federal will pay \$12.9 million in cash for all outstanding shares of FCB, subject to certain adjustment factors. The transaction is expected to close by the end of the third quarter of 2014.

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Item 9. Changes In and Disagreements With Accountants on Accounting and Financial Disclosure

None.

Item 9A. Controls and Procedures

First Defiance's management carried out an evaluation, under the supervision and with the participation of the chief executive officer and the chief financial officer, of the effectiveness of First Defiance's disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of December 31, 2013. Based upon that evaluation, the chief executive officer along with the chief financial officer concluded that First Defiance's disclosure controls and procedures as of December 31, 2013, are effective.

The information set forth under "Management's Report on Internal Control Over Financial Reporting" and "Report of Independent Registered Public Accounting Firm" included in Item 8 above is incorporated herein by reference.

There were no changes in First Defiance's internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the last fiscal quarter ended December 31, 2013 that have materially affected, or are reasonably likely to materially affect First Defiance's internal control over financial reporting.

Item 9B. Other Information

None

PART III

Item 10. Directors, Executive Officers and Corporate Governance

The information required herein is incorporated by reference from the sections captioned: "Proposal 1 - Election of Directors", "Executive Officers", and "Section 16(a) Beneficial Ownership Reporting Compliance" of the definitive proxy statement to be filed on or about March 24, 2014 (the "Proxy Statement").

First Defiance has adopted a Code of Ethics applicable to all officers, directors and employees that complies with SEC requirements, and is available on its Internet site at www.fdef.com under Governance Documents.

Item 11. Executive Compensation

Information required by this item is set forth under the captions "Compensation Discussions and Analysis," "Executive Compensation," "Director Compensation," "Compensation Committee Report" and "Compensation Committee Interlocks and Insider Participation" of the Proxy Statement.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

The information set forth under the caption "Beneficial Ownership" of the Proxy Statement is incorporated herein by reference.

Equity Compensation Plans

The following table provides information as of December 31, 2013 with respect to the shares of First Defiance common stock that may be issued under First Defiance's existing equity compensation plans.

Plan Category	Number of securities to be Issued Upon Exercise of Outstanding Options, Warrants and Rights (a)	Weighted Average Exercise Price of Outstanding Options, Warrants and Rights (b)	Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans (Excluding Securities Reflected in Column (a)) (c)
Equity Compensation Plans Approved by Security Holders	251,020	\$ 20.75	202,405

Item 13. Certain Relationships and Related Transactions, and Director Independence

The information set forth under the captions "Composition of the Board" and "Related Person Transactions" of the Proxy Statement is incorporated herein by reference.

Item 14. Principal Accountant Fees and Services

The information set forth under the caption "Independent Registered Public Accounting Firm" of the Proxy Statement is incorporated herein by reference.

PART IV

Item 15. Exhibits, Financial Statement Schedules

(a) Financial Statements

(1) The following documents are filed as Item 8 of this Form 10-K.

(A) Report of Independent Registered Public Accounting Firm (Crowe Horwath LLP)

(B) Consolidated Statements of Financial Condition as of December 31, 2013 and 2012

(C) Consolidated Statements of Income for the years ended December 31, 2013, 2012 and 2011

(D) Consolidated Statements of Comprehensive Income for the years ended December 31, 2013, 2012 and 2011

(E) Consolidated Statements of Stockholders' Equity for the years ended December 31, 2013, 2012 and 2011

(F) Consolidated Statements of Cash Flows for the years ended December 31, 2013, 2012 and 2011

(G) Notes to Consolidated Financial Statements

Separate financial statement schedules are not being filed because of the absence of conditions under which they (2) are required or because the required information is included in the consolidated financial statements or the related notes.

The exhibits required by this item are listed in the Exhibit Index of this Form 10-K. The management contracts (3) and compensation plans or arrangements required to be filed with this Form 10-K are listed as Exhibits 10.1 through 10.35.

SIGNATURES

Pursuant to the requirements of Sections 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

FIRST DEFIANCE FINANCIAL CORP.

February 28, 2014 By: /s/ Kevin T. Thompson
Kevin T. Thompson, Chief Financial Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities indicated on February 28, 2014.

Signature	Title
/s/ William J. Small William J. Small	Chairman of the Board
/s/ Donald P. Hileman Donald P. Hileman	Executive Vice President and Chief Executive Officer
/s/ Kevin T. Thompson Kevin T. Thompson	Executive Vice President and Chief Financial Officer (principal accounting officer)
/s/ James L. Rohrs James L. Rohrs	Director, Executive Vice President
/s/ Stephen L. Boomer Stephen L. Boomer	Director, Vice Chairman
/s/ John L. Bookmyer John L. Bookmyer	Director
/s/ Dr. Douglas A. Burgei Dr. Douglas A. Burgei	Director
/s/ Peter A. Diehl Peter A. Diehl	Director
/s/ Barb A. Mitzel Barb A. Mitzel	Director
/s/ Jean A. Hubbard Jean A. Hubbard	Director
/s/ Samuel S. Strausbaugh Samuel S. Strausbaugh	Director
/s/ Thomas A. Voigt Thomas A. Voigt	Director

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Exhibit Index

This report incorporates by reference the documents listed below that we have previously filed with the SEC. The SEC allows us to incorporate by reference information in this document. The information incorporated by reference is considered to be part of this document.

This information may be read and copied at the Public Reference Room of the SEC at 100 F Street, N.E., Washington D.C. 20549. The SEC also maintains an internet web site that contains reports, proxy statements, and other information about issuers, like First Defiance, who file electronically with the SEC. The address of the site is <http://www.sec.gov>. The reports and other information filed by First Defiance with the SEC are also available at the First Defiance Financial Corp. web site. The address of the site is <http://www.fdef.com>. Except as specifically incorporated by reference into this Annual Report on Form 10-K, information on those web sites is not part of this report.

Exhibit Number	Description	
3.1	Articles of Incorporation	(1)
3.2	Code of Regulations	(1)
3.3	Amendment to Articles of Incorporation	(11)
4.1	Agreement to furnish instruments and agreements defining rights of holders of long-term debt	(17)
4.2	Form of Warrant for Purchase of Shares of Common Stock	(15)
10.1	1996 Stock Option Plan	(2)
10.2	Form of Incentive Stock Option Award Agreement under 2001 Plan	(3)
10.3	Form of Nonqualified Stock Option Award Agreement under 1996 Plan	(3)
10.4	1996 Management Recognition Plan and Trust	(8)
10.5	2001 Stock Option and Incentive Plan	(5)
10.6	Employment Agreement with William J. Small	(6)
10.7	Employment Agreement with James L. Rohrs	(7)
10.8	Employment Agreement with Donald P. Hileman	(18)
10.9	Employment Agreement with Gregory R. Allen	(9)
10.10	2005 Stock Option and Incentive Plan	(10)
10.11	Letter Agreement, dated December 5, 2008, between First Defiance and the U.S. Treasury	(12)
10.12	2008 Long Term Incentive Compensation Plan (LTIP)	(13)
10.13	Form of Contingent Award Agreement under LTIP	(14)
10.14	Form of Stock Option Award Agreement under 2005 Plan	(4)
10.15	Amendment to all Employment Agreements for CPP	(4)
10.16	Form of Agreement for CPP Compensation Standards	(21)
10.17	Form of Option Award Agreement with EESA restriction under 2005 Plan	(21)
10.18	First Federal Executive Group Life Plan Post Separation	(19)
10.19	2010 Equity Incentive Plan	(20)
10.20	Underwriting Agreement dated March 23, 2011	(27)
10.21	First Defiance Deferred Compensation Plan	(33)
10.22	Form of Restricted Stock Award Agreement	(22)
10.23	2010 Equity Plan Form of Long-Term Incentive Plan Award Agreement	(23)
10.24	2010 Equity Plan Form of Short-Term Incentive Plan Award Agreement	(24)
10.25	2010 Equity Plan Form of Long-Term Incentive Plan Award Agreement (with TARP Restrictions)	(25)
10.26	2010 Equity Plan Form of Short-Term Incentive Plan Award Agreement (with TARP Restrictions)	(26)
10.27	First Amendment to First Defiance Financial Corp. 2010 Equity Incentive Plan	(28)
10.28	First Defiance Financial Corp. and Affiliates Incentive Compensation Plan	(29)

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10.29	First Defiance Financial Corp. Long-Term Restricted Stock Unit Award Agreement (2012 Long Term Incentive TARP Applicable)	(30)
10.30	First Defiance Financial Corp. Long-Term Restricted Stock Unit Award Agreement (2012 Long Term Incentive)	(31)
10.31	Underwriting Agreement dated June 13, 2012	(32)
10.32	Employment Agreement with Donald P. Hileman	(34)
10.33	Employment Agreement with Kevin T. Thompson	(35)
10.34	Form of Restricted Stock Award Agreement	(36)
10.35	Consulting Agreement with William J. Small	(37)
21	List of Subsidiaries of the Company	(17)
23.1	Consent of Crowe Horwath LLP	(17)
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	(17)
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	(17)
32.1	Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	(17)
32.2	Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	(17)
101*	Interactive data files pursuant to Rule 405 of Regulation S-T: (i) the Consolidated Condensed Balance Sheet, (ii) the Consolidated Condensed Statements of Income, (iii) the Consolidated Condensed Statements of Changes in Equity, (iv) the Consolidated Condensed Statements of Cash Flows, and (v) the Notes to Consolidated Condensed Financial Statements tagged as blocks of text and in detail.	(17)

- (1) Incorporated herein by reference to the like numbered exhibit in the Registrant's Form S-1 (File No. 33-93354)
- (2) Incorporated herein by reference to like numbered exhibit in Registrant's 2001 Form 10-K (Film No. 02580719)
- (3) Incorporated herein by reference to like numbered exhibit in Registrant's 2004 Form 10-K (Film No. 0568550)
- (4) Incorporated herein by reference to like numbered exhibit in Registrant's 2008 Form 10-K (Film No. 09683948)
- (5) Incorporated herein by reference to Appendix B to the 2001 Proxy Statement (Film No. 1577137)
- (6) Incorporated herein by reference to exhibit 10.1 in Form 8-K filed October 1, 2007 (Film No. 071144951)
- (7) Incorporated herein by reference to exhibit 10.2 in Form 8-K filed October 1, 2007 (Film No. 071144951)
- (8) Incorporated herein by reference to exhibit 10.2 in Registrant's 2001 Form 10-K (Film No. 02580719)
- (9) Incorporated herein by reference to exhibit 10.4 in Form 8-K filed October 1, 2007 (Film No. 071144951)
- (10) Incorporated herein by reference to Appendix A to the 2005 Proxy Statement (Film No. 05692264)
- (11) Incorporated herein by reference to exhibit 3 in Form 8-K filed December 8, 2008 (Film No. 081236105)
- (12) Incorporated herein by reference to exhibit 10 in Form 8-K filed December 8, 2008 (Film No. 081236105)
- (13) Incorporated herein by reference to exhibit 10.1 in Form 8-K filed December 12, 2008 (Film No. 081245224)
- (14) Incorporated herein by reference to exhibit 10.2 in Form 8-K filed December 12, 2008 (Film No. 081245224)

- (15) Incorporated herein by reference to exhibit 4 in Form 8-K filed December 8, 2008 (Film No. 081236105)
- (17) Included herein
- (18) Incorporated herein by reference to exhibit 10.1 in Form 8-K filed December 16, 2009 (Film No. 091245196)
- (19) Incorporated herein by reference to exhibit 10.1 in Form 10-Q filed November 2, 2010 (Film No. 101158262)
- (20) Incorporated herein by reference to Annex A to 2010 Proxy Statement (Film No. 10693151)
- (21) Incorporated herein by reference to like numbered exhibit in Registrant's 2010 Form 10-K (Film No. 10652528)
- (22) Incorporated herein by reference to exhibit 10.1 in Form 10-Q filed May 5, 2011 (Film No. 11803357)
- (23) Incorporated herein by reference to exhibit 10.1 in Form 10-Q filed November 8, 2011 (Film No. 111188059)
- (24) Incorporated herein by reference to exhibit 10.2 in Form 10-Q filed November 8, 2011 (Film No. 111188059)
- (25) Incorporated herein by reference to exhibit 10.3 in Form 10-Q filed November 8, 2011 (Film No. 111188059)
- (26) Incorporated herein by reference to exhibit 10.4 in Form 10-Q filed November 8, 2011 (Film No. 111188059)
- (27) Incorporated herein by reference to exhibit 1 in Form 8-K filed March 29, 2011 (Film No. 11719267)
- (28) Incorporated herein by reference to exhibit 10.1 in Form 8-K filed March 15, 2012 (Film No. 12694926)
- (29) Incorporated herein by reference to exhibit 10.2 in Form 8-K filed March 15, 2012 (Film No. 12694926)
- (30) Incorporated herein by reference to exhibit 10.3 in Form 8-K filed March 15, 2012 (Film No. 12694926)
- (31) Incorporated herein by reference to exhibit 10.4 in Form 8-K filed March 15, 2012 (Film No. 12694926)
- (32) Incorporated herein by reference to exhibit 1.1 in Form 8-K filed June 15, 2012 (Film No. 12910514)
- (33) Incorporated herein by reference to exhibit 10.1 in Form 8-K filed December 23, 2005 (Film No. 051284175)
- (34) Incorporated herein by reference to exhibit 10.1 in Form 8-K filed December 30, 2013 (Film No. 131303552)
- (35) Incorporated herein by reference to exhibit 10.2 in Form 8-K filed December 30, 2013 (Film No. 131303552)
- (36) Incorporated herein by reference to exhibit 10.3 in Form 8-K filed December 30, 2013 (Film No. 131303552)
- (37) Incorporated herein by reference to exhibit 10.4 in Form 8-K filed December 30, 2013 (Film No. 131303552)

* As provided in Rule 406T of Regulation S-T, the Interactive Data Files on Exhibit 101 hereto are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, as amended, are deemed not filed for purposes of Section 18 of the Securities and Exchange Act of 1934, as amended, and otherwise are not subject to liability under those sections.