First Defiance Financial Corp.
2017 **Annual Report**

FIRST DEFIANCE
FINANCIAL CORP.

Better together.

SUCCESS THROUGH FOCUS

SUCCESS THROUGH FOCUS

Donald P. Hileman
President & CEO

As the fifth consecutive year with record earnings, 2017 was a year filled with both financial and strategic achievements for First Defiance Financial Corp. by balancing high performance with strong principles, shareholder value with client needs, and clear focus on the details with a vision of the future. We served our customers as a high-performing community bank and witnessed continued improvement of our key metrics and strategic initiatives.

GROWTH

Our strong sales and service model allowed us to achieve balance sheet growth in the face of competitive market pressures, particularly in pricing. We successfully integrated Commercial Savings Bank in the first quarter of 2017 and Corporate One Benefits in the second quarter of 2017, marking our first bank acquisition in nine years. We continued to expand our commitment to metro markets with the opening of a loan production office in Ann Arbor, Michigan, and a new office that houses both our bank and insurance agency in Sylvania, Ohio. Our successful growth strategy, defined as deepening client relationships, expanding our branch and insurance agency network and aligning leadership to support accelerated growth within our metro markets, contributed to our accomplishments and will carry into 2018 and beyond.

CLIENTS

Our people-focused mentality leads us to continually look for ways to enhance our client experience in person and through digital channels. A dedicated team of employees that concentrates on client experience has allowed us to introduce our clients to People Pay, a person to person digital payment solution, additional Smart ATM locations, an improved, personalized online mortgage experience and a new First Insurance Group app. In addition, we realigned our Treasury Management team to improve processes and provide in-depth customer service. We will continue to provide smart solutions as more and more people choose to bank beyond our doors.

TECHNOLOGY

A focus on technology allowed us to gain efficiencies and transform our customer service model. We view technology as a means to offer clients additional choices and more personalized solutions. Progress in our branch transformation initiatives brought our first in-lobby automated teller unit into a branch to provide clients a means to define their banking experience. A foundation was established for an enhanced data strategy with new data management software. This data-driven approach will deepen our understanding of our clients and assist in making client-focused decisions.

EMPLOYEES

We re-energized our teams; and now, more than ever, have a synergy when working to accomplish our goals. Employee and client feedback helped us bring new mission, vision and values to life, and these values are being personified and recognized throughout our company on a daily basis. This enthusiasm is echoed in our employee engagement scores and has resulted in significant progress within initiatives to attract and retain top talent. We have great confidence in those working hard to achieve our goals now and in the future.

COMMUNITIES

Our philosophy of building strong communities comes to life each time we donate dollars or volunteer hours to the communities we call home. By offering every employee paid time off to volunteer for life-changing organizations, we are truly living our motto of being Better Together. This pay-it-forward philosophy supports our annual Pay it Forward events which have now contributed to over $40,000 in funding for community-generated ideas to make the places we call home even stronger. That's a mission that will always be in our sight.

As we move into 2018, we look to build on this momentum. We will look closely to discover every opportunity to balance shareholder value with smart solutions for our clients and our communities. After all, it's that focus that makes us better together.

Donald P. Hileman | President & CEO

COMPANY PROFILE

First Defiance Financial Corp., headquartered in Defiance, Ohio, is the holding company for First Federal Bank of the Midwest and First Insurance Group. First Federal Bank operates 43 full-service branches and numerous ATM locations in northwest and central Ohio, southeast Michigan and northeast Indiana, and a loan production office in Ann Arbor, Michigan. First Insurance Group, including its division Corporate One Benefits, is a full-service insurance agency with nine offices throughout northwest Ohio.

Founded in the 1920s as Northwest Savings, First Federal Bank was chartered in 1935 as a federal mutual savings and loan company. First Federal Bank converted to a mutual holding company and issued its first stock to the public and employees in 1993. In September 1995, First Federal Bank converted to a full stock company, trading stock on the NASDAQ national market under the ticker symbol FDEF. At the same time, First Defiance Financial Corp. was founded as the holding company for First Federal Bank. In 1998, an additional business line was added with the acquisition of an insurance agency, now known as First Insurance Group. The Bank's name was changed to First Federal Bank of the Midwest in 1999, to better reflect our community banking business strategy.

Since 2003, First Defiance has completed five bank acquisitions and five insurance agency acquisitions. Most recently, 2017 marked the successful completion of acquisitions of Commercial Bancshares, Inc. based in Upper Sandusky, Ohio, and Corporate One Benefits Agency, Inc. based in Fostoria, Ohio. Both acquisitions expanded our community-based financial service offerings through office locations in new communities.

SAFE HARBOR STATEMENT

Statements contained in this Annual Report may not be based on historical facts and are "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21B of the Securities Act of 1934, as amended. Actual results could vary materially depending on risks and uncertainties inherent in general and local banking and insurance conditions, competitive factors specific to markets in which the Company and its subsidiaries operate, future interest rate levels, legislative and regulatory decisions or capital market conditions. The Company assumes no responsibility to update this information. For more details, please refer to the Company's SEC filings, including its most recent Annual Report on Form 10-K and quarterly reports on Form 10-Q.

FINANCIAL HIGHLIGHTS

(In thousands, except per share amounts)

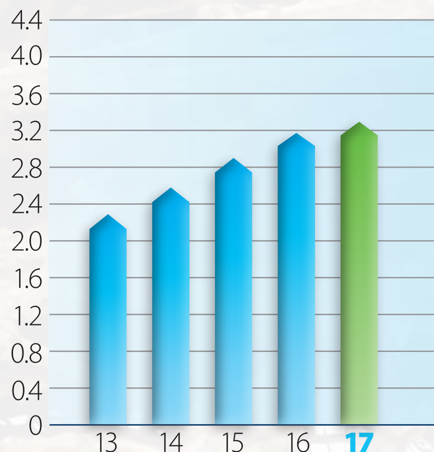
Summary of Operating Results	2017	2016	% Change
Net interest income	$96,671	$78,943	22.5%
Provision for loan losses	2,949	283	942.1%
Non-interest income (excluding securities gains)	39,497	33,521	17.8%
Securities gains	584	509	14.7%
Non-interest expense	85,351	71,093	20.1%
Net income	32,268	28,843	11.9%

Balance Sheet Data	2017	2016	% Change
Total assets	$2,993,403	$2,477,597	20.8%
Loans, net	2,322,030	1,914,603	21.3%
Deposits	2,437,656	1,981,628	23.0%
Stockholders' equity	373,286	293,018	27.4%
Allowance for loan losses	26,683	25,884	3.1%

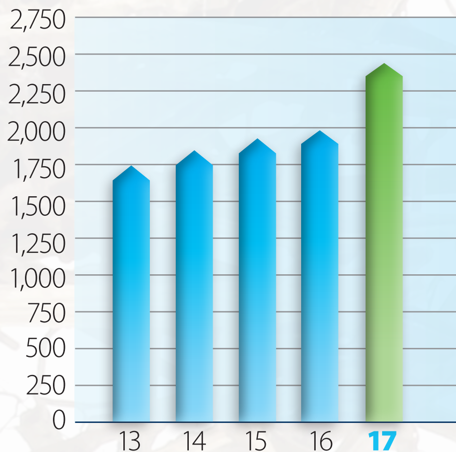
Share Information	2017	2016	% Change
Basic earnings per common share	$3.23	$3.21	0.6%
Diluted earnings per common share	3.22	3.19	0.9%
Dividends per common share	1.00	0.88	13.6%
Tangible book value per common share	26.49	25.59	3.5%
Shares outstanding at end of period	10,156	8,983	13.1%

Key Ratios	2017	2016	% Change
Average net interest margin	3.88%	3.74%	3.7%
Return on average assets	1.13%	1.20%	-5.8%
Return on average equity	9.19%	10.10%	-9.0%
Efficiency ratio	61.81%	62.20%	-0.6%

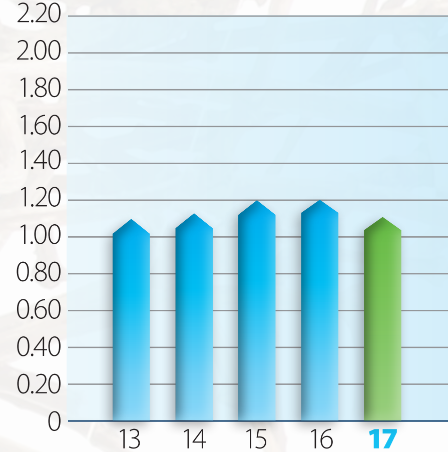
Building shareholder value while earning trust.



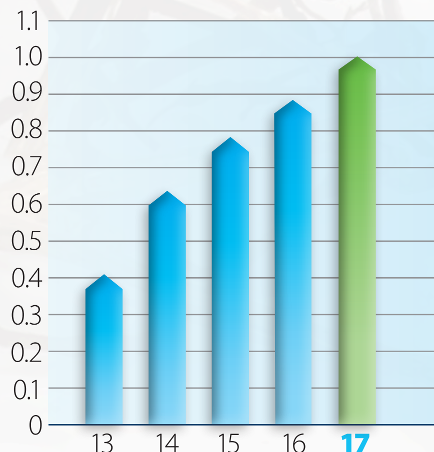
Diluted Earnings Per Share
4.4
4.0
3.6
3.2
2.8
2.4
2.0
1.6
1.2
0.8
0.4
0
13
14
15
16
17



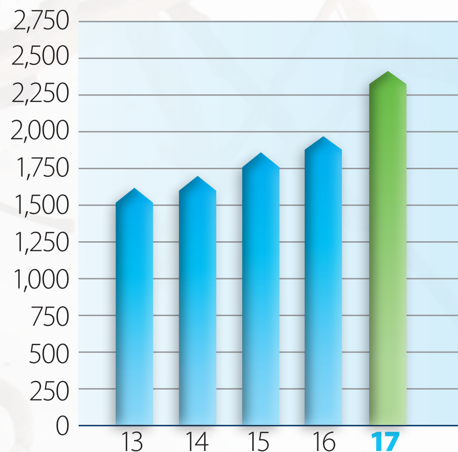
Deposits (in millions)
2,750
2,500
2,250
2,000
1,750
1,500
1,250
1,000
750
500
250
0
13
14
15
16
17



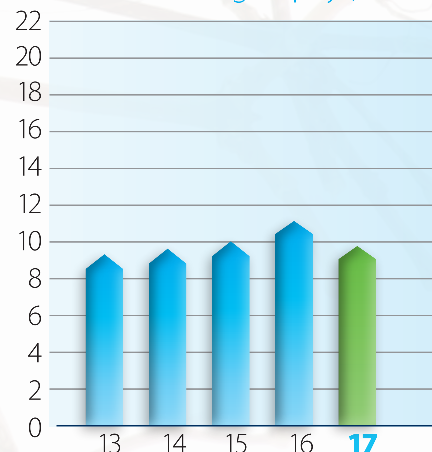
Return on Average Assets (percent)
2.20
2.00
1.80
1.60
1.40
1.20
1.00
0.80
0.60
0.40
0.20
0
13
14
15
16
17



Dividends Per Share
1.1
1.0
0.9
0.8
0.7
0.6
0.5
0.4
0.3
0.2
0.1
0
13
14
15
16
17



Loans (in millions)
2,750
2,500
2,250
2,000
1,750
1,500
1,250
1,000
750
500
250
0
13
14
15
16
17



Return on Average Equity (percent)
22
20
18
16
14
12
10
8
6
4
2
0
13
14
15
16
17

BOARD OF DIRECTORS AND CORPORATE OFFICERS

BOARD OF DIRECTORS

William J. Small
Chairman,
First Defiance Financial Corp.
1, 5, 6, 7 & 8

Donald P. Hileman
President &
Chief Executive Officer,
First Defiance Financial Corp.
1, 5, 6, 7 & 8

John L. Bookmyer
Vice Chairman & Lead Director,
First Defiance Financial Corp.,
Chief Executive Officer,
Pain Management Group
Findlay, Ohio
1, 2, 3 & 5

Robert E. Beach
Retired President & CEO,
Commercial Bancshares, Inc.
Upper Sandusky, Ohio
5, 6 & 8

Terri A. Bettinger
Former Chief Information Officer,
Franklin Data Center
Columbus, Ohio
2, 3 & 8

Douglas A. Burgei, D.V.M.
Veterinarian,
Napoleon, Ohio
3, 4, 5 & 7

Thomas K. Herman
Co-Founder & President,
Aptera
Fort Wayne, Indiana
4, 5 & 8

Jean A. Hubbard
Business Manager &
Corporate Treasurer,
The Hubbard Company
Defiance, Ohio
2, 3 & 8

Barbara A. Mitzel
Retired Director of
Public Affairs,
Consumers Energy
Adrian, Michigan
4, 5 & 6

Charles D. Niehaus
Managing Partner,
Niehaus & Associates, Ltd.
Toledo, Ohio
2, 4 & 8

Thomas A. Reineke
President and CEO,
Reineke Family Dealerships
Findlay, Ohio
4 & 6

Mark A. Robison
Chairman & President,
Brotherhood Mutual
Insurance Company
Fort Wayne, Indiana
2, 4 & 7

Samuel S. Strausbaugh
President, Chief
Executive Officer &
Chief Financial Officer,
JB & Company, Inc.
Tiffin, Ohio
2, 3 & 8

KEY FOR BOARD OF DIRECTORS:

1. Executive Committee
2. Audit Committee
3. Compensation Committee
4. Corporate Governance Committee
5. Investment Committee
6. Trust Committee
7. First Insurance Group Board
8. Risk Committee

FIRST FEDERAL BANK OF THE MIDWEST CORPORATE OFFICERS

Donald P. Hileman
President &
Chief Executive Officer

Kevin T. Thompson
Executive Vice President,
Chief Financial Officer

John R. Reisner
Executive Vice President,
Chief Risk Officer &
Legal Counsel

Sharon L. Davis
Executive Vice President,
Director of Human Resources

Dennis E. Rose, Jr.
Executive Vice President,
Director of Strategy
Management

Michael D. Mulford
Executive Vice President,
Chief Credit Administration Officer

Timothy K. Harris
Executive Vice President,
Chief Credit Officer

Marybeth Shunck
Executive Vice President,
Director of Sales

Amy L. Hackenberg
Executive Vice President,
Southern Market Area Executive

James R. Williams, III
Executive Vice President,
Northern Market
Area Executive

Gregory R. Allen
Executive Vice President,
Fort Wayne Market Area
Executive

Joel P. Jerger
Executive Vice President,
Toledo Market Area Executive

David D. Dygert
Executive Vice President,
Columbus Market Area Executive

Brent L. Beard
Senior Vice President, Controller

Amy M. Daeger
Senior Vice President,
Director of Retail Administration

Brian A. Eitniear
Senior Vice President,
Director of Corporate Services

Charles V. Hoecherl
Senior Vice President,
Treasury Management Sales

David L. Kondas
Senior Vice President,
Director of Wealth Management

Kathleen A. Miller
Senior Vice President,
Information Technology

Justin R. Rodemich
Senior Vice President,
Bank Operations

Martha J. Woelke
Senior Vice President,
Retail Lending

Ryan J. Miller
Senior Vice President,
Northern Market Area
Commercial Lending Manager

John W. Schuld
Senior Vice President,
Southern Market Area
Commercial Lending Manager

Dirk VanHeyst
Senior Vice President,
Senior Commercial Lender

Danielle R. Figley
Corporate Secretary

FIRST DEFIANCE FINANCIAL CORP. CORPORATE OFFICERS

Donald P. Hileman
President &
Chief Executive Officer

Kevin T. Thompson
Executive Vice President,
Chief Financial Officer

Sharon L. Davis
Executive Vice President,
Director of Human Resources

John R. Reisner
Executive Vice President,
Chief Risk Officer &
Legal Counsel

Danielle R. Figley
Corporate Secretary

FIRST INSURANCE GROUP, INC. CORPORATE OFFICERS

Donald P. Hileman
Chief Executive Officer

Michael R. Klein
President &
Chief Operating Officer

Ronald R. Burns
Executive Vice President,
Group Health & Life

Steven R. Dandurand
Executive Vice President,
Group Health & Life

Marvin K. Dubbs, Jr.
Executive Vice President,
Property & Casualty

Kenneth G. Keller
Executive Vice President,
Group Health & Life

John Payak, III
Executive Vice President,
Property & Casualty

Timothy S. Whetstone
Executive Vice President,
Property & Casualty

Lawrence H. Woods
Executive Vice President,
Property & Casualty

Leadership rooted in our communities.

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-K

(Mark One)

[X] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year Ended December 31, 2017

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	**34-1803915**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
601 Clinton Street, Defiance, Ohio	**43512**
(Address of principal executive offices)	(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	**The NASDAQ Stock Market**
(Title of Class)	(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 [X]

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 [X]

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate 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 [X] No [ ]

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, smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer ☐ Accelerated filer X Non-accelerated filer ☐ Smaller reporting company ☐ Emerging growth company ☐

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes [ ] No [X]

The aggregate market value of the 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, 2017, was approximately $517.0 million.

As of February 23, 2018, there were issued and outstanding 10,182,308 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 2018 Annual Meeting of the Registrant's shareholders.

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" or "the Bank"), First Insurance Group of the Midwest, Inc. ("First Insurance"), and First Defiance Risk Management Inc. (collectively, "the Subsidiaries"), focuses on traditional banking and property, casualty, life and group health insurance products.

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 premiums 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.

Effective February 24, 2017, the Company acquired Commercial Bancshares, Inc. ("Commercial Bancshares") and its subsidiary, The Commercial Savings Bank ("CSB"), pursuant to an Agreement and Plan of Merger ("merger agreement"), dated August 23, 2016. The acquisition was accomplished by the merger of Commercial Bancshares into First Defiance, immediately followed by the merger of CSB into First Defiance's banking subsidiary, First Federal. Prior to the consummation of the mergers, CSB operated 7 full-service banking offices in northwest and north central Ohio and 1 commercial loan production office in central Ohio. Commercial Bancshares' consolidated assets and equity (unaudited) as of February 24, 2017 totaled $348.4 million and $37.5 million, respectively. The Company accounted for the transaction under the acquisition method of accounting which means that the acquired assets and liabilities were recorded at fair value at the date of acquisition.

On April 13, 2017, First Defiance and Corporate One Benefits Agency, Inc. ("Corporate One") jointly announced the acquisition of Corporate One's business by First Defiance. The total purchase price paid in cash was made up of the following: $6.5 million was paid at closing, $500,000 will be due in July 2018, and approximately $2.3 million will be due at the end of a three-year earn-out based on the compound annual growth rate of net revenue over the performance period of Corporate One, for a total purchase price of $9.3 million. The recorded fair value of the $2.3 million earn-out was $1.8 million at December 31, 2017. As of December 31, 2017, total Company recorded goodwill of $7.9 million, identifiable intangible assets of $756,000 (consisting of customer relationship intangible of $564,000 and a non-compete intangible of $192,000) from the acquisition of Corporate Ones business. Corporate One was a full-service employee benefits consulting organization founded in 1996 with offices located in Archbold, Findlay, Fostoria and Tiffin, Ohio. Corporate One provided consulting services to employers regarding management and modernization of their employee benefit program. It is anticipated that the

transaction will enhance employee benefit products offered by First Insurance and expand First Insurance's presence into adjacent markets in northwest Ohio.

At December 31, 2017, the Company had consolidated assets of $3.0 billion, consolidated deposits of $2.4 billion, and consolidated stockholders' equity of $373.3 million. The Company was incorporated in Ohio in June of 1995. Its principal executive offices are located at 601 Clinton Street, Defiance, Ohio 43512, and its telephone number is (419) 782-5015.

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").

The Subsidiaries

The Company's core business operations are conducted through its subsidiaries:

First Federal Bank of the Midwest: First Federal is a federally chartered stock savings bank headquartered in Defiance, Ohio. It conducts operations through thirty-six full-service banking center offices in Allen, Defiance, Fulton, Hancock, Henry, Lucas, Marion, Ottawa, Paulding, Putnam, Seneca, Williams, Wood, and Wyandot counties in northwest and central Ohio, two full-service banking center offices in Allen County in northeast Indiana, five full-service banking center offices in Lenawee County in southeast Michigan and one commercial loan production office in Ann Arbor, Michigan that was opened late in the fourth quarter of 2017.

First Federal is primarily engaged in community banking. It attracts deposits from the general public through its offices and website, and uses those and other available sources of funds to originate residential real estate loans, commercial 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 residential 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 through offices located in the Archbold, Bowling Green, Bryan, Defiance, Findlay, Fostoria, Lima, Maumee, Oregon, and Tiffin, Ohio areas. The Maumee and Oregon offices were consolidated into a new office in Sylvania, Ohio in January 2018. First Insurance offers property and casualty insurance, life insurance and group health insurance.

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 help minimize the risk allocable to each participating insurer.

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 Mission & Vision and Core

Values initiatives. 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. In the later part of 2017, the Company recognized the need to adapt its organization structure to meet certain future strategic objectives and to continue its past success. The Company believes that fully utilizing the strengths of its leadership team and a structure that supports strategic initiatives will enhance its ability to achieve even more milestones in the future. With that being said, the Company redefined its market areas to support strategies to enhance processes and efficiencies to support overall growth. The new structure includes three metro markets; Toledo, Ohio, Fort Wayne, Indiana, and Columbus, Ohio and two legacy markets; Southern Market Area and Northern Market Area.

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, including 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. 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 and mobile banking services.

Fee Income Development - Generation of fee income and the diversification of revenue sources are accomplished through the mortgage banking operation, First Insurance 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's pricing strategy considers the whole relationship of the customer. First Federal continues 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 to 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 monitors 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. 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 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.

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, Controller, and the Chief Administration Officer can each approve transactions up to $3.0 million. Two of the three officers are required to approve transactions between $3.0 million and $5.0 million. All transactions in excess of $5.0 million must be approved by the Board of Directors.

First Defiance's investment portfolio includes 76 CMO issues totaling $93.9 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, 2017.

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, 2017, 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	
	Under 1 Year	Weighted Average Rate	1 - 5 Years	Weighted Average Rate	6-10 Years	Weighted Average Rate	Over 10 Years	Weighted Average Rate	Amount	Yield
	(Dollars in Thousands)									
Mortgage-backed securities	$ 6,334	3.12%	$ 22,269	3.08%	$17,149	3.02%	$11,817	3.33%	$ 57,569	3.12%
CMOs	12,751	3.11	43,744	3.10	31,600	3.12	6,250	3.31	94,345	3.12
U.S. government and federal agency obligations	-	-	519	2.00	-	-	-	-	519	2.00
Obligations of states and political subdivisions (1)	1,423	4.37	9,425	3.39	36,965	3.76	42,911	3.37	90,724	3.55
Corporate bonds	-	-	10,017	2.29	2,897	2.58	-	-	12,914	2.36
Total	$ 20,508		$ 85,974		$ 88,611		$ 60,978		$ 256,071	
Unamortized premiums/ (discounts)									4,303	
Unrealized gain on securities available for sale and unrecognized gain on held to maturity									924	
Total									$ 261,298	

(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%.

The carrying value of investment securities is as follows:

	December 31		
	2017	2016	2015
	(In Thousands)		
Available-for-sale securities:			
Obligations of U.S. government corporations and agencies	**$ 508**	$ 3,915	$ 2,994
Obligations of state and political subdivisions	**92,828**	88,043	90,389
CMOs, REMICS and mortgage-backed securities	**154,210**	146,019	138,074
Trust preferred stock and preferred stock	**1**	2	1
Corporate bonds	**13,103**	13,013	4,977
Total	**$ 260,650**	$ 250,992	$ 236,435
Held-to-maturity securities:			
Mortgage-backed securities	**$ 68**	$ 91	$ 119
Obligations of state and political subdivisions	**580**	93	124
Total	**$ 648**	$ 184	$ 243

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 $55.0 million and $46.0 million in overnight investments at the Federal Reserve at December 31, 2017 and 2016, 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 $2.0 million and $1.8 million at December 31, 2017 and 2016, 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, 2017, First Federal serviced

14,447 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, 2017, 65.92%, 33.32% and 0.70% 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 approximating 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:

	December 31								
	2017			2016			2015		
Rate	Number of Loans	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
	(Dollars in Thousands)								
Less than 3.00%	**2,024**	**$ 189,700**	**13.69%**	2,191	$ 225,328	16.42%	1,836	$ 188,916	14.06%
3.00% -3.99%	**6,598**	**710,084**	**51.22**	6,279	682,157	49.72	5,606	603,875	44.94
4.00% -4.99%	**3,919**	**377,821**	**27.26**	3,551	332,023	24.20	3,924	379,917	28.28
5.00% - 5.99%	**1,122**	**68,423**	**4.94**	1,405	83,775	6.11	1,761	110,616	8.23
6.00% - 6.99%	**626**	**33,658**	**2.43**	749	41,055	2.99	922	50,937	3.79
7.00% and over	**158**	**6,382**	**0.46**	175	7,680	0.56	209	9,461	0.70
Total	**14,447**	**$ 1,386,068**	**100.00%**	14,350	$ 1,372,018	100.00%	14,258	$1,343,722	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.

	December 31											
	2017				2016				2015			
Maturity	**Number of Loans**	**% 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**	**% of Unpaid Principal Amount**
	(Dollars in Thousands)											
1–5 years	**444**	**3.07%**	**$ 8,346**	**0.60%**	529	3.69%	$ 7,432	0.54%	680	4.77%	$ 10,801	0.80%
6–10 years	**2,557**	**17.70**	**162,190**	**11.70**	1,784	12.43	102,132	7.44	1,563	10.97	89,364	6.65
11–15 years	**3,012**	**20.85**	**278,655**	**20.10**	3,671	25.58	343,750	25.05	3,759	26.36	349,986	26.05
16–20 years	**1,258**	**8.71**	**109,300**	**7.89**	1,526	10.63	135,540	9.88	1,635	11.47	144,249	10.74
21–25 years	**2,460**	**17.03**	**248,919**	**17.96**	1,846	12.86	169,496	12.35	1,833	12.85	169,889	12.64
More than 25 years	**4,716**	**32.64**	**578,658**	**41.75**	4,994	34.81	613,668	44.74	4,788	33.58	579,433	43.12
Total	**14,447**	**100.00%**	**$1,386,068**	**100.00%**	14,350	100.00%	$1,372,018	100.00%	14,258	100.00%	$1,343,722	100.00%

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, 2017, First Federal's limit on loans-to-one borrower was

$48.8 million and its five largest loans (including available lines of credit) or groups of loans to one borrower, including related entities, were $25.0 million, $24.8 million, $24.4 million, $23.2 million and $22.3 million. All of these loans or groups of loans were performing in accordance with their terms at December 31, 2017.

Loan Portfolio Composition – The net increase in net loans receivable over the prior year was $407.4 million (including $285.4 million acquired from CSB), $137.8 million and $154.8 million at December 31, 2017, 2016, and 2015, respectively. The loan portfolio contains no foreign loans. The Company's loan portfolio is concentrated geographically in the northwest and central 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 $838.1 million at December 31, 2017, which represents 34.9% of the Company's loan portfolio.

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

	December 31									
	2017		2016		2015		2014		2013	
	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%
	(Dollars in Thousands)									
Real estate:										
1-4 family residential	**$ 274,862**	**11.1%**	$ 207,550	10.2%	$ 205,330	11.0%	$ 206,437	12.2%	$ 195,752	12.2%
Multi-family residential	**248,092**	**10.1**	196,983	9.7	167,558	9.0	156,530	9.3	148,952	9.2
Commercial real estate	**987,129**	**40.0**	843,579	41.5	780,870	41.8	683,958	40.6	670,666	41.6
Construction	**265,476**	**10.8**	182,886	9.0	163,877	8.7	112,385	6.7	86,058	5.3
Total real estate loans	**1,775,559**	**72.0**	1,430,998	70.4	1,317,635	70.5	1,159,310	68.8	1,101,428	68.3
Other:										
Commercial	**526,142**	**21.3**	469,055	23.0	419,349	22.4	399,730	23.7	388,236	24.1
Home equity and improvement	**135,457**	**5.5**	118,429	5.8	116,962	6.2	111,813	6.6	106,930	6.6
Consumer finance	**29,109**	**1.2**	16,680	0.8	16,281	0.9	15,466	0.9	16,902	1.0
	690,708	**28.0**	604,164	29.6	552,592	29.5	527,009	31.2	512,068	31.7
Total loans	**2,466,267**	**100.0%**	2,035,162	100.0%	1,870,227	100.0%	1,686,319	100.0%	1,613,496	100.0%
Less:										
Undisbursed loan funds	**115,972**		93,355		66,902		38,653		32,290	
Net deferred loan origination fees	**1,582**		1,320		1,108		880		758	
Allowance for loan losses	**26,683**		25,884		25,382		24,766		24,950	
Net loans	**$ 2,322,030**		$ 1,914,603		$ 1,776,835		$ 1,622,020		$ 1,555,498	

In addition to the loans reported above, First Defiance had $10.4 million, $9.6 million, $5.5 million, $4.5 million, and $9.1 million in loans classified as held for sale at December 31, 2017, 2016, 2015, 2014 and 2013, 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, 2017, 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, 2017						
	Due Less than 1	Due 1-2	Due 3-5	Due 5-10	Due 10-15	Due 15+	Total
	(In Thousands)						
Real estate	$ 502,526	$ 203,035	$ 769,909	$ 146,336	$ 65,905	$ 87,848	$1,775,559
Other loans:							
Commercial	361,561	59,542	96,673	8,243	123	-	526,142
Home equity and improvement	121,475	3,108	7,768	1,678	840	588	135,457
Consumer finance	13,710	6,176	8,216	970	37	-	29,109
Total	$ 999,272	$ 271,861	$ 882,566	$ 157,227	$ 66,905	$ 88,436	$2,466,267

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, 2017, which has fixed interest rates or which have floating or adjustable interest rates.

	Fixed Rates	Floating or Adjustable Rates	Total
	(In Thousands)		
Real estate	$ 475,443	$ 797,590	$1,273,033
Commercial	120,148	44,433	164,581
Other	27,893	1,488	29,381
	$ 623,484	$ 843,511	$ 1,466,995

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, internet 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 by a commercial lender and underwritten by a commercial credit analyst. The commercial lender may approve credits within their lending limit, and another loan officer with limits sufficient to cover the exposure must approve credits exceeding an individual's lending limit. All credits which exceed $250,000 in aggregate exposure must be presented for review or approval to the Senior Loan Committee comprised of senior lending personnel. Credits which exceed $5,000,000 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 the Senior Loan Committee and, if necessary, by the Executive Loan Committee.

First Federal 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 Federal'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 9.9% of First Federal's total originations of one-to-four family residential mortgage loans in 2017 compared to 10.8% and 10.3% during 2016 and 2015, 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 Federal's total loans and loans held for sale during the periods indicated:

	Years Ended December 31		
	2017	**2016**	**2015**
	(In Thousands)		
Loan originations:			
1-4 family residential	**$ 240,921**	$ 294,307	$ 241,658
Multi-family residential	**74,342**	59,957	44,352
Commercial real estate	**181,289**	166,437	241,969
Construction	**205,088**	138,553	116,224
Commercial	**219,588**	389,037	465,543
Home equity and improvement	**68,856**	56,816	54,676
Consumer finance	**15,185**	10,426	10,235
Total loans originated	**1,005,269**	1,115,533	1,174,657
Loans acquired in acquisitions:	**285,448**	-	-
Loans purchased:	**11,476**	822	-
Loan reductions:			
Loan pay-offs	**350,971**	232,302	265,311
Loans sold	**231,073**	282,589	231,067
Periodic principal repayments	**288,215**	432,445	493,383
	870,259	947,336	989,761
Net increase in total loans and loans held for sale	**$ 431,934**	$ 169,019	$ 184,896

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, 2017, 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.

	30 to 59 Days		60 to 89 Days		90 Days and Over		Total	
	Amount	Percentage	Amount	Percentage	Amount	Percentage	Amount	Percentage
	(Dollars in Thousands)							
1-4 family residential real estate	$ 1,305	0.05%	$ 1,031	0.04%	$ 1,463	0.06%	$ 3,799	0.15%
Multi- family residential	418	0.02	-	0.00	-	0.00	418	0.02
Commercial real estate	616	0.02	277	0.01	1,964	0.07	2,857	0.10
Construction	-	0.00	-	0.00	-	0.00	-	0.00
Commercial	179	0.01	1,248	0.05	1,393	0.06	2,820	0.12
Home equity and improvement	2,465	0.10	428	0.02	206	0.01	3,099	0.13
Consumer finance	292	0.01	79	0.00	2	0.00	373	0.01
Total	$ 5,275	0.21%	$ 3,063	0.12%	$ 5,028	0.20%	$ 13,366	0.53%

Overall, the level of delinquencies at December 31, 2017, increased from the levels at December 31, 2016, when First Defiance reported that 0.32% of its outstanding loans were at least 30 days delinquent. The level of total loans 90 or more days delinquent has increased to 0.20% at December 31, 2017, from 0.17% at December 31, 2016. The level of total loans 60-89 days delinquent increased to 0.12% at December 31, 2017, from 0.07% at December 31, 2016. The level of loans that were 30 to 59 days past due increased to 0.21% at December 31, 2017, from 0.08% at December 31, 2016. 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 status 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 $56.3 million, $27.4 million and $41.9 million were considered impaired as of December 31, 2017, 2016 and 2015, respectively. The increase in impaired loans from 2016 to 2017 is due to an increase in two loan relationships totaling $11.0 million that became impaired during 2017 as well as $10.4 million of newly impaired loans from the CSB acquisition due to new financial information received. 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, except for those classified as troubled debt restructurings. There was $1.4 million of interest received and recorded in income during 2017 related to impaired loans. There was $1.7 million and $1.3 million recorded in 2016 and 2015, respectively. Unrecorded interest income based on the loan's contractual terms on these impaired loans and all non-performing loans in 2017, 2016 and 2015 was $1.1 million, $1.2 million, and $1.5 million, respectively. The average recorded investment in impaired loans during 2017, 2016 and 2015 (excluding loans accounted for under FASB ASC Topic 310 Subtopic 30) was $47.1 million, $32.8 million and $51.8 million, respectively. The total allowance for loan losses related to these loans was $0.8 million, $0.8 million, and $0.4 million at December 31, 2017, 2016 and 2015, respectively.

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 2017, First Defiance recognized $20,000 of expense related to write-downs in value of real estate acquired by foreclosure. The balance of real estate owned at December 31, 2017 was $1.5 million.

As of December 31, 2017, First Defiance's total non-performing loans amounted to $30.7 million or 1.31% of total loans (net of undisbursed loan funds and deferred fees and costs), compared to $14.3 million or 0.74% of total loans, at December 31, 2016. Non-performing loans are loans which are more than 90 days past due or on nonaccrual. The nonperforming loan balance for 2017 includes $25.5 million of loans that were originated by First Federal and also considered impaired, compared to $11.3 million for 2016.

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				
	2017	**2016**	**2015**	**2014**	**2013**
	(Dollars in Thousands)				
Nonperforming loans:					
1-4 family residential real estate	**$ 3,037**	$ 2,928	$ 2,610	$ 3,332	$ 3,273
Multi-family residential real estate	**128**	2,639	2,419	2,539	581
Commercial real estate	**18,091**	6,953	7,429	12,635	15,253
Commercial	**8,841**	1,007	3,078	4,993	8,327
Home equity and improvement	**590**	730	689	619	413
Consumer finance	**28**	91	36	12	-
Total nonperforming loans	**30,715**	14,348	16,261	24,130	27,847
Real estate owned	**1,532**	455	1,321	6,181	5,859
Total repossessed assets	**1,532**	455	1,321	6,181	5,859
Total nonperforming assets	**$ 32,247**	$ 14,803	$ 17,582	$ 30,311	$ 33,706
Restructured loans, accruing	**$ 13,770**	$ 10,544	$ 11,178	$ 24,686	$ 27,630
Total nonperforming assets as a percentage of total assets	**1.08%**	0.60%	0.77%	1.39%	1.58%
Total nonperforming loans as a percentage of total loans*	**1.31%**	0.74%	0.90%	1.47%	1.76%
Total nonperforming assets as a percentage of total loans plus REO*	**1.37%**	0.76%	0.97%	1.83%	2.12%
Allowance for loan losses as a percent of total nonperforming assets	**82.75%**	174.86%	144.36%	81.71%	74.02%

* 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.

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. See **"Item 7 - Management's Discussion and Analysis of Financial Condition and Results of Operations – Allowance for Loan Losses"** for further discussion on management's evaluation of the allowance for loan losses.

Loans 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 along with a static loan environment. To the extent that the portfolio grows at a rapid rate or overall quality or the loan environment deteriorates, the provision generally will exceed charge-offs. However, in certain circumstances 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 or the loan environment 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, 2017, First Defiance's allowance for loan losses totaled $26.7 million compared to $25.9 million at December 31, 2016. The following table sets forth the activity in First Defiance's allowance for loan losses during the periods indicated.

	Years Ended December 31				
	2017	**2016**	**2015**	**2014**	**2013**
	(Dollars in Thousands)				
Allowance at beginning of year	**$ 25,884**	$ 25,382	$ 24,766	$ 24,950	$ 26,711
Provision for credit losses	**2,949**	283	136	1,117	1,824
Charge-offs:					
1-4 family residential real estate	**(279)**	(350)	(282)	(426)	(643)
Commercial real estate and multi-family	**(429)**	(92)	(468)	(1,018)	(2,475)
Commercial	**(2,301)**	(615)	(68)	(2,982)	(1,230)
Consumer finance	**(139)**	(94)	(53)	(41)	(94)
Home equity and improvement	**(301)**	(268)	(350)	(392)	(757)
Total charge-offs	**(3,449)**	(1,419)	(1,221)	(4,859)	(5,199)
Recoveries	**1,299**	1,638	1,701	3,558	1,614
Net (charge-offs) recoveries	**(2,150)**	219	480	(1,301)	(3,585)
Ending allowance	**$ 26,683**	$ 25,884	$ 25,382	$ 24,766	$ 24,950
Allowance for loan losses to total non-performing loans at end of year	**86.87%**	180.40%	156.09%	102.64%	89.60%
Allowance for loan losses to total loans at end of year*	**1.14%**	1.33%	1.41%	1.50%	1.58%
Net charge-offs (recoveries) for the year to average loans	**0.10%**	-0.01%	-0.03%	0.08%	0.23%

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

The provision for credit losses increased significantly in 2017 from previous years due to growth of the loan portfolio as well as an increase in net charge offs. The decrease in the allowance for loan loss as a percentage of total loans at December 31, 2017 vs December 31, 2016 is primarily attributable to the CSB acquisition. The CSB loans acquired were recorded at fair value with purchase accounting adjustments discounting the loan balance instead of an allowance for loan losses. For the CSB loans acquired, the discount recorded totaled $3.9 million, or 1.9% of acquired CSB loans at December 31, 2017. Management feels that the level of the allowance for loan losses at December 31, 2017, 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"** Below.

	December 31									
	2017		2016		2015		2014		2013	
	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)									
1-4 family residential	**$ 2,532**	**11.1%**	$ 2,627	10.2%	$ 3,212	11.0%	$ 2,494	12.2%	$ 2,847	12.2%
Multi-family residential real estate	**2,702**	**10.1**	2,228	9.7	2,151	9.0	2,453	9.3	2,508	9.2
Commercial real estate	**10,354**	**40.0**	10,625	41.5	11,772	41.8	11,268	40.6	12,000	41.6
Construction	**647**	**10.8**	450	9.0	517	8.7	221	6.7	134	5.3
Commercial loans	**7,965**	**21.3**	7,361	23.0	5,192	22.4	6,509	23.7	5,678	24.1
Home equity and improvement loans	**2,255**	**5.5**	2,386	5.8	2,270	6.2	1,704	6.6	1,635	6.6
Consumer loans	**228**	**1.2**	207	0.8	171	0.9	117	0.9	148	1.0
	$ 26,683	**100.0%**	$ 25,884	100.0%	$25,382	100.0%	$ 24,766	100.0%	$ 24,950	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 has the ability to utilize the national market for certificates of deposit. First Defiance has used these deposits in the past and could in the future if necessary.

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

	Years Ended December 31					
	2017		2016		2015	
	Amount	Rate	Amount	Rate	Amount	Rate
	(Dollars in Thousands)					
Non-interest-bearing demand deposits	**$ 528,926**	**-**	$ 441,731	-	$ 388,257	-
Interest bearing demand deposits	**955,248**	**0.18%**	798,266	0.17%	742,856	0.16%
Savings deposits	**284,814**	**0.04**	235,137	0.04	215,253	0.04
Time deposits	**530,414**	**1.33**	430,487	1.12	441,510	0.92
Totals	**$ 2,299,402**	**0.38%**	$ 1,905,621	0.33%	$ 1,787,876	0.30%

The following table sets forth the maturities of First Defiance's retail certificates of deposit having principal amounts $250,000 or greater at December 31, 2017 (In Thousands):

Retail certificates of deposit maturing in quarter ending:	
March 31, 2018	$ 4,813
June 30, 2018	9,358
September 30, 2018	8,172
December 31, 2018	3,428
After December 31, 2018	28,072
Total retail certificates of deposit with balances $250,000 or greater	$ 53,843

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

	2017	2016
	(In Thousands)	
Interest bearing demand deposits and money market accounts	**$ 29**	$ 23
Certificates of deposit	**68**	19
	$ 97	$ 42

For additional information regarding First Defiance's deposits see Note 11 to the Consolidated Financial Statements.

Borrowings— First Defiance may obtain advances from the FHLB of Cincinnati by pledging certain of its residential mortgage loans, commercial real estate 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.

	Years Ended December 31		
	2017	**2016**	**2015**
	(Dollars in Thousands)		
Long-term:			
FHLB advances	**$ 84,279**	$ 103,943	$ 59,902
Weighted average interest rate	**1.55%**	1.42%	1.62%
Short-term:			
Securities sold under agreement to repurchase	**$ 26,019**	$ 31,816	$ 57,188
Weighted average interest rate	**0.20%**	0.22%	0.27%

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		
	2017	**2016**	**2015**
	(Dollars in Thousands)		
Long-term:			
FHLB advances:			
Maximum balance	**$ 105,214**	$ 103,943	$ 59,902
Average balance	**102,115**	84,944	38,185
Weighted average interest rate	**1.44%**	1.42%	1.62%

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		
	2017	**2016**	**2015**
	(Dollars in Thousands)		
Short-term:			
FHLB advances:			
Maximum balance	**$ -**	$ 30,000	$ -
Average balance	**44**	861	41
Weighted average interest rate	**0.80%**	0.39%	0.18%
Securities sold under agreement to repurchase:			
Maximum balance	**$ 26,019**	$ 57,984	$ 60,272
Average balance	**23,337**	52,821	54,632
Weighted average interest rate	**0.23%**	0.26%	0.28%

First Defiance borrows funds under a variety of programs at the FHLB. As of December 31, 2017, there was $84.3 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, 2017 and 2016, no outstanding balances existed under First Defiance's short-term Cash Management Advance Line of Credit or REPO line of credit. The total available under the Cash Management Advance 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, 2017, other than amounts available on the REPO and Cash Management line, First Federal had additional borrowing capacity with the FHLB of $567.4 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 was in compliance with the minimum requirement with an investment in stock of the FHLB of Cincinnati of $16.0 million at December 31, 2017, and $13.8 million at December 31, 2016. First Federal holds stock of the FHLB of Indianapolis of $5,000 at December 31, 2017, and December 31, 2016.

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 Consolidated Financial Statements.

Subordinated Debentures - In March 2007, the Company sponsored an affiliated trust, First Defiance Statutory Trust II ("Trust Affiliate II") that issued $15.0 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 3.09% and 2.46% as of December 31, 2017 and 2016 respectively.

The Trust Preferred Securities are subject to mandatory redemption, in whole or in part, upon repayment of the Subordinated Debentures. The Company 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 can be redeemed at the Company's option at any time now.

In October 2005, the Company formed an affiliated trust, First Defiance Statutory Trust I ("Trust Affiliate I") that issued $20.0 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 2.97% and 2.34% as of December 31, 2017 and 2016 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 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 December 15, 2035, but can be redeemed by the Company at any time now.

Employees

First Defiance had 674 employees at December 31, 2017. 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 commercial real estate 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, except for central Ohio.

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 is subject to regulation examination and oversight by the Federal Reserve Board ("Federal Reserve"). First Federal is subject to regulation, examination and oversight by the Office of the Comptroller of the Currency ("OCC"). Because the FDIC insures First Federal's deposits, First Federal is also subject to examination and regulation by the FDIC. In addition, First Federal is subject to regulations of the Consumer Financial Protection Bureau (the "CFPB") which was established by the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act") and has broad powers to adopt and enforce consumer protection regulations. 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, the 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 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.

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.

Regulatory Capital Requirements and Prompt Corrective Action – The federal banking regulators have adopted risk-based capital guidelines for financial institutions and their holding companies, designed to absorb losses. The guidelines provide a systematic analytical framework, which makes regulatory capital requirements sensitive to differences in risk profiles among banking organizations, takes off-balance sheet exposures expressly into account in evaluating capital adequacy and minimizes disincentives to holding liquid, low-risk assets. Capital levels as measured by these standards are also used to categorize financial institutions for purposes of certain prompt corrective action regulatory provisions.

In July 2013, the United States banking regulators issued final new capital rules applicable to smaller banking organizations which also implement certain provisions of the Dodd-Frank Act. The new minimum capital requirements became effective on January 1, 2015, whereas a new capital conservation buffer and deductions from common equity capital phase in from January 1, 2016, through January 1, 2019, and most deductions from common equity tier 1 capital are being phased in from January 1, 2015, through January 1, 2019.

The rules include (a) a minimum common equity tier 1 ("CET1") capital ratio of 4.5%, (b) a minimum Tier 1 capital ratio of 6.0%, (c) a minimum total capital ratio of 8.0%, and (d) a minimum leverage ratio of 4%.

Common equity for the common equity tier 1 capital ratio includes common stock (plus related surplus) and retained earnings, plus limited amounts of minority interests in the form of common stock, less the majority of certain regulatory deductions.

Tier 1 capital includes common equity as defined for the common equity tier 1 capital ratio, plus certain non-cumulative preferred stock and related surplus, cumulative preferred stock and related surplus and trust preferred securities that have been grandfathered (but which are not permitted going forward), and limited amounts of minority interests in the form of additional Tier 1 capital instruments, less certain deductions.

Tier 2 capital, which can be included in the total capital ratio, includes certain capital instruments (such as subordinated debt) and limited amounts of the allowance for loan and lease losses, subject to new eligibility criteria, less applicable deductions.

The deductions from common equity tier 1 capital include goodwill and other intangibles, certain deferred tax assets, mortgage-servicing assets above certain levels, gains on sale in connection with a securitization, investments in a banking organization's own capital instruments and investments in the capital of unconsolidated financial institutions (above certain levels).

Under the guidelines, capital is compared to the relative risk related to the balance sheet. To derive the risk included in the balance sheet, one of several risk weights is applied to different balance sheet and off-balance sheet assets, primarily based on the relative credit risk of the counterparty. The

capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings and other factors.

The rules also place restrictions on the payment of capital distributions, including dividends, and certain discretionary bonus payments to executive officers if the company does not hold a capital conservation buffer of greater than 2.5% composed of common equity tier 1 capital above its minimum risk-based capital requirements, or if its eligible retained income is negative in that quarter and its capital conservation buffer ratio was less than 2.5% at the beginning of the quarter. The capital conservation buffer phases in through January 1, 2019 and is currently 1.875%.

The federal banking agencies have established a system of “prompt corrective action” to resolve certain problems of undercapitalized banks. This system is based on five capital level categories for insured depository institutions: "well capitalized," "adequately capitalized," "undercapitalized," "significantly undercapitalized" and "critically undercapitalized." The federal banking agencies may (or in some cases must) take certain supervisory actions depending upon a bank's capital level. For example, the banking agencies must appoint a receiver or conservator for a bank within 90 days after it becomes "critically undercapitalized" unless the bank's primary regulator determines, with the concurrence of the FDIC, that other action would better achieve regulatory purposes. Banking operations otherwise may be significantly affected depending on a bank's capital category. For example, a bank that is not "well capitalized" generally is prohibited from accepting brokered deposits and offering interest rates on deposits higher than the prevailing rate in its market, and the holding company of any undercapitalized depository institution must guarantee, in part, specific aspects of the bank's capital plan for the plan to be acceptable.

Effective January 1, 2015, in order to be "well-capitalized," a financial institution must have a common equity tier 1 capital ratio of 6.5%, a total risk-based capital ratio of at least 10%, a Tier 1 risk-based capital of at least 8% and a leverage ratio of at least 5%, and the institution must not be subject to any written agreement, order, capital directive or prompt corrective action directive to meet and maintain a specific capital level for any capital measure. As of December 31, 2017, First Federal met the ratio requirements in effect at that date to be deemed "well-capitalized." See Note 17 of the Notes to the Consolidated Financial Statements which is incorporated herein by reference.

The following table sets forth the amounts and percentage levels of regulatory capital of First Defiance and First Federal, the minimum amounts required for each of First Defiance and First Federal, and the amounts required for First Federal to be deemed well capitalized under the prompt corrective action system, all as of December 21, 2017. (Dollars in Thousands):

	Actual		Minimum Required for Adequately Capitalized		Minimum Required to be Well Capitalized for Prompt Corrective Action	
	Amount	**Ratio**	**Amount**	**Ratio(1)**	**Amount**	**Ratio**
CET1 Capital (to Risk-Weighted Assets) (2)						
Consolidated	$274,832	10.43%	$118,596	4.5%	N/A	N/A
First Federal	$298,571	11.33%	$118,534	4.5%	$171,216	6.5%
Tier 1 Capital (2)						
Consolidated	$309,832	10.80%	$114,773	4.0%	N/A	N/A
First Federal	$298,571	10.43%	$114,539	4.0%	$143,173	5.0%
Tier 1 Capital (to Risk Weighted Assets) (2)						
Consolidated	$309,832	11.76%	$158,128	6.0%	N/A	N/A
First Federal	$298,571	11.33%	$158,046	6.0%	$220,728	8.0%
Total Capital (to Risk Weighted Assets) (2)						
Consolidated	$336,515	12.77%	$210,838	8.0%	N/A	N/A
First Federal	$332,254	12.35%	$210,728	8.0%	$263,410	10.0%

(1) Excludes capital conservation buffer of 1.25% as of December 31, 2017.
(2) Core capital is computed as a percentage of adjusted total assets of $2.87 billion for consolidated and $2.86 billion for the Bank. Risk-based capital is computed as a percentage of total risk-weighted assets of $2.64 billion for consolidated and $2.63 billion for the Bank.

In September 2017, the Federal Reserve Board, along with other bank regulatory agencies, proposed amendments to its capital requirements to simplify various aspects of the capital rules and thereby reduce regulatory burden for "non-advanced approaches" banking organizations. The Bank is a non-advanced approach bank because it has total consolidated assets of less than $250 billion and balance sheet foreign exposures of less than the maximum amount for a non-advanced approach bank. Because the amendments were proposed with a request for comments and have not been finalized, we do not yet know what effect the final rules will have on the Bank's capital calculations. In November 2017, the federal banking agencies extended, for such non-advanced approaches banks, the existing capital requirements for certain items that were scheduled to change effective January 1, 2018, in light of the simplification amendments being considered.

Dividends - Dividends paid by First Federal to First Defiance are subject to various regulatory restrictions. First Federal paid $13.0 million in dividends to First Defiance in 2017 and $22.0 million in 2016. Generally, First Federal may not pay dividends to First Defiance in excess of its net profits (as defined by statute) for the last two fiscal years, plus any year-to-date net profits without the approval of the OCC. First Insurance paid $1.8 million in dividends to First Defiance in 2017 and $1.2 million in dividends in 2016. First Defiance Risk Management paid $1.0 million in dividends to First Defiance in each of 2017 and 2016.

First Defiance's ability to pay dividends to its shareholders is primarily dependent on its receipt of dividends from the Subsidiaries. The Federal Reserve expects First Defiance to serve as a source of strength for First Federal and may require First Defiance to retain capital for further investment in First Federal, rather than pay dividends to First Defiance shareholders. Payment of dividends by First Defiance or First Federal may be restricted at any time at the discretion of its applicable regulatory authorities if they deem such dividends to constitute an unsafe or unsound practice. These provisions could have the effect of limiting First Defiance's ability to pay dividends on its common shares.

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 comply with Sections 23A and 23B of the Federal Reserve Act ("FRA") and the Federal Reserve's 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, First Defiance Risk Management and First Insurance are affiliates of First Federal.

Deposit Insurance - The FDIC maintains the DIF, which insures the deposit accounts of First Federal to the maximum amount provided by law. The general insurance limit is $250,000 per separately insured depositor. This insurance is backed by the full faith and credit of the United States government.

The FDIC assesses deposit insurance premiums on each insured institution quarterly based on risk characteristics of the institution. The FDIC may also impose a special assessment in an emergency situation.

Pursuant to the Dodd-Frank Act, the FDIC has established 2.0% as the designated reserve ratio (DRR), which is the ratio of the DIF to insured deposits of the total industry. In March 2016, the FDIC adopted final rules designed to meet the statutory minimum DRR of 1.35% by September 30, 2020, the deadline imposed by the Dodd-Frank Act. The Dodd-Frank Act requires the FDIC to offset the effect on institutions with assets of less than $10 billion of the increase in the statutory minimum DRR to 1.35% from the former statutory minimum of 1.15%. The FDIC's rules reduced assessment rates on all banks but imposed a surcharge on banks with assets of $10 billion or more until the DRR reaches 1.35% and provide assessment credits to banks with assets of less than $10 billion for the portion of their assessments that contribute to the increase of the DRR to 1.35%. The rules also changed the method to determine risk-based assessment rates for established banks with less than $10 billion in assets to better ensure that banks taking on greater risks pay more for deposit insurance than less risky banks.

In addition, all institutions with deposits insured by the FDIC are required to pay assessments to fund interest payments on bonds issued by the Financing Corporation, a mixed-ownership government corporation established to recapitalize a predecessor to the DIF. These assessments will continue until the Financing Corporation bonds mature in 2019.

As insurer, the FDIC is authorized to conduct examinations of, and to require reporting by, federally-insured institutions. It also may prohibit any federally-insured institution from engaging in any activity the FDIC determines by regulation or order to pose a serious threat to the Deposit Insurance Fund. The FDIC also has the authority to take enforcement actions against insured institutions. Insurance of deposits may be terminated by the FDIC upon a finding that the institution has engaged or is engaging in unsafe and 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 or written agreement entered into with the FDIC.

Consumer Protection Laws and Regulations - Banks are subject to regular examination to ensure compliance with federal statutes and regulations applicable to their business, including consumer protection statutes and implementing regulations. Potential penalties under these laws include, but are not limited to, fines. The Dodd-Frank Act established the CFPB, which has extensive regulatory and enforcement powers over consumer financial products and services. The CFPB has adopted numerous rules with respect to consumer protection laws, amending some existing regulations and adopting new ones, and has commenced enforcement actions. The following are just some of the consumer protection laws applicable to First Federal:

- Community Reinvestment Act of 1977: imposes a continuing and affirmative obligation to fulfill the credit needs of its entire community, including low- and moderate-income neighborhoods.

- Equal Credit Opportunity Act: prohibits discrimination in any credit transaction on the basis of any of various criteria.

- Truth in Lending Act: requires that credit terms are disclosed in a manner that permits a consumer to understand and compare credit terms more readily and knowledgeably.

- Fair Housing Act: makes it unlawful for a lender to discriminate in its housing-related lending activities against any person on the basis of any of certain criteria.

- Home Mortgage Disclosure Act: requires financial institutions to collect data that enables regulatory agencies to determine whether the financial institutions are serving the housing credit needs of the communities in which they are located.

- Real Estate Settlement Procedures Act: requires that lenders provide borrowers with disclosures regarding the nature and cost of real estate settlements and prohibits abusive practices that increase borrowers' costs.

- Privacy provisions of the Gramm-Leach-Bliley Act: requires financial institutions to establish policies and procedures to restrict the sharing of non-public customer data with non-affiliated parties and to protect customer information from unauthorized access.

The banking regulators also use their authority under the Federal Trade Commission Act to take supervisory or enforcement action with respect to unfair or deceptive acts or practices by banks that may not necessarily fall within the scope of specific banking or consumer finance law.

Community Reinvestment Act - Under the Community Reinvestment Act ("CRA"), every FDIC-insured institution is obligated, consistent with safe and sound banking practices, to help meet the credit needs of its entire community, including low and moderate income neighborhoods. The CRA requires the appropriate federal banking regulator, in connection with the examination of an insured institution, to assess the institution's record of meeting the credit needs of its community and to consider this record in its evaluation of certain applications to banking regulators, such as an application for approval of a merger or the establishment of a branch. An unsatisfactory rating may be used as the basis for the denial of an application to acquire another financial institution or open a new branch. As of its last examination, First Federal received a CRA rating of "satisfactory."

Executive and Incentive Compensation - In June 2010, the Federal Reserve Board, the OCC and the FDIC issued joint interagency guidance on incentive compensation policies (the Joint Guidance) intended to ensure that the incentive compensation policies of banking organizations do not undermine the safety and soundness of such organizations by encouraging excessive risk-taking. This principles-based guidance, which covers all employees that have the ability to materially affect the risk profile of an organization, either individually or as part of a group, is based upon the key principles that a banking organization's incentive compensation arrangements should: (i) provide incentives that do not encourage risk-taking beyond the organization's ability to effectively identify and manage risks; (ii) be compatible with effective internal controls and risk management; and (iii) be supported by strong corporate governance, including active and effective oversight by the organization's board of directors. The Joint Guidance made incentive compensation part of the regulatory agencies' examination process, with the findings of the supervisory initiatives included in reports of examination and enforcement actions possible.

In May 2016, the federal bank regulatory agencies approved a joint notice of proposed rules (the Proposed Joint Rules) designed to prohibit incentive-based compensation arrangements that encourage inappropriate risks at financial institutions. The Proposed Joint Rules would apply to covered financial institutions with total assets of $1 billion or more. For all covered institutions, including Level 3 institutions like us, the proposed rule would:

- prohibit incentive-based compensation arrangements that are "excessive" or "could lead to material financial loss;"

- require incentive based compensation that is consistent with a balance of risk and reward, effective management and control of risk, and effective governance; and

- require board oversight, recordkeeping and disclosure to the appropriate regulatory agency.

Further, as stock exchanges impose additional listing requirements under the Dodd-Frank Act, public companies will be required to implement "clawback" procedures for incentive compensation payments and to disclose the details of the procedures, which allow recovery of incentive compensation that was paid on the basis of erroneous financial information necessitating a restatement due to material noncompliance with financial reporting requirements. This clawback policy is intended to apply to compensation paid within a three-year look-back window of the restatement and would cover all executives who received incentive awards.

Patriot Act - In response to the terrorist events of September 11, 2001, the Uniting and Strengthening of America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (the Patriot Act) was signed into law in October 2001. The Patriot Act gives the United States government powers to address terrorist threats through enhanced domestic security measures, expanded surveillance powers, increased information sharing and broadened anti-money laundering requirements. Title III of the Patriot Act takes measures intended to encourage information sharing among bank regulatory agencies and law enforcement bodies. Further, certain provisions of Title III impose affirmative obligations on a broad range of financial institutions. Among other requirements, Title III and related regulations require regulated financial institutions to establish a program specifying procedures for obtaining identifying information from customers seeking to open new accounts and establish enhanced due diligence policies, procedures and controls designed to detect and report suspicious activity. First Federal has established policies and procedures that it considers to be in compliance with the requirements of the Patriot Act.

Volcker Rule – The Volcker Rule under the Dodd-Frank Act prohibits banks and their affiliates from engaging in proprietary trading and investing in and sponsoring hedge funds and private equity funds. The Volcker Rule, which became effective in July 2015, does not significantly impact the operations of First Defiance or its subsidiaries, as the Company does not engage in the businesses prohibited by the Volcker Rule.

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

First Defiance's financial performance generally, and in particular the ability of borrowers to pay interest on and repay principal of outstanding loans and the value of collateral securing those loans, as well as demand for loans and other products and services First Defiance offers, is highly dependent upon the business environment in the markets where the Company operates, mainly in the State of Ohio and in the Great Lake Region. A favorable business environment is generally characterized by, among other factors, economic growth, efficient capital markets, low inflation, low unemployment, high business and investor confidence, and strong business earnings. Unfavorable or uncertain economic and market conditions can be caused by declines in economic growth, business activity or investor or business confidence; limitations on the availability or increases in the cost of credit and capital; increases in inflation or interest rates; high unemployment, natural disasters; or a combination of these or other factors. Conditions such as inflation, recession, unemployment, changes in interest rates, fiscal and monetary policy and other factors beyond First Defiance's control may adversely affect its deposit levels and composition, demand for loans, the ability of its borrowers to repay their loans and the value of the collateral securing the loans it makes. Because First Defiance has a significant amount of real estate loans, decreases in real estate values could adversely affect the value of property used as collateral and

First Defiance's ability to sell the collateral upon foreclosure.

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, 2017, First Federal's portfolio of commercial real estate loans totaled $1.2 billion, or approximately 50.1% 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, 2017, First Federal's portfolio of commercial loans totaled $526.1 million, or approximately 21.3% 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.

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 cash flows are largely dependent upon its net interest income. Net interest income is the difference between interest income earned on interest-earning assets such as loans and securities, and interest expense paid on interest-bearing liabilities such as deposits and borrowed funds. Interest rates are highly sensitive to many factors that are beyond First Defiance's control, including general economic conditions and policies of various governmental and regulatory agencies and, in particular, the Federal Open Market Committee. Changes in monetary policy, including changes in interest rates, could influence not only the interest First Defiance receives on loans and securities and the amount of interest it pays on deposits and borrowings, but such changes could also affect (i) First

Defiance's ability to originate loans and obtain deposits, (ii) the fair value of First Defiance's financial assets and liabilities, and (iii) the average duration of certain assets and liabilities. If the interest rates paid on deposits and other borrowings increase at a faster rate than the interest rates received on loans and other investments, First Defiance's net interest income, and therefore earnings, could be adversely affected. Earnings could also be adversely affected if the interest rates received on loans and other investments fall more quickly than the interest rates paid on deposits and other borrowings. Any substantial, unexpected, prolonged change in market interest rates could have a material adverse effect on First Defiance's results of operations and financial condition.

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, the OCC, the FDIC and the CFPB. 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 of First Defiance's depositors and borrowers and the deposit insurance fund, rather than First Defiance's shareholders.

Comprehensive revisions to the regulatory capital framework were finalized by the Federal Reserve, the OCC, and the FDIC in 2013. The revised regulations change 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. 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.

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

Potential misuse of funds or information by First Defiance's employees or by third parties could result in damage to First Defiance's customers for which First Defiance could be held liable, subject First Defiance to regulatory sanctions and otherwise adversely affect First Defiance's financial condition and results of operations.

First Defiance's employees handle a significant amount of funds, as well as financial and personal information. First Defiance also depends upon third-party vendors who have access to funds and

personal information about customers. Cybersecurity breaches of other companies, such as the breach of the systems of a credit bureau, may result in criminals using personal information obtained from such other source to impersonate a customer of First Defiance and obtain funds from customer accounts. Further, First Defiance may be affected by data breaches at retailers and other third parties who participate in data interchanges with First Defiance's customers that involve the theft of customer credit and debit card data, which may include the theft of debit card PIN numbers and commercial card information used to make purchases at such retailers and other third parties. Such data breaches could result in First Defiance incurring significant expenses to reissue debit cards and cover losses, which could result in a material adverse effect on First Defiance's results of operations.

Although First Defiance has implemented systems to minimize the risk of fraudulent taking or misuse of funds or information, there can be no assurance that such systems will be adequate or that a taking or misuse of funds or information by employees, by third parties who have authorized access to funds or information, or by third parties who are able to access funds or information without authorization will never occur. First Defiance could be held liable for such an event and could also be subject to regulatory sanctions. First Defiance could also incur the expense of developing additional controls and investing in additional equipment or contracts to prevent future such occurrences. Although First Defiance has insurance to cover such potential losses, First Defiance cannot provide assurance that such insurance will be adequate to meet any liability, and insurance premiums may rise substantially if First Defiance suffers such an event. In addition, any loss of trust or confidence placed in First Defiance by our clients could result in a loss of business, which could adversely affect our financial condition and results of operations, or result in a loss of investor confidence, hurting First Defiance's stock price and ability to acquire capital in the future. First Defiance could also lose revenue by the wrongful appropriation of confidential information about its business operations by competitors who use the information to compete with First Defiance.

First Defiance could suffer a material adverse impact from interruptions in the effective operation of, or security breaches affecting, First Defiance's computer systems.

First Defiance relies heavily on its own information systems and those of vendors to conduct our business and to process, record, and monitor transactions. Risks to the system could result from a variety of factors, including the potential for bad acts on the part of hackers, criminals, employees and others. As one example, some banks have experienced denial of service attacks in which individuals or organizations flood the bank's website with extraordinarily high volumes of traffic, with the goal and effect of disrupting the ability of the bank to process transactions. Other businesses have been victims of a ransomware attack in which a business becomes unable to access its own information and is presented with a demand to pay a ransom in order to once again have access to its information. First Defiance is also at risk for the impact of natural disasters, terrorism and international hostilities on its systems or for the effects of outages or other failures involving power or communications systems operated by others. These risks also arise from the same types of threats to businesses with which First Defiance deals.

Potential adverse consequences of attacks on First Defiance's computer systems or other threats include damage to First Defiance's reputation, loss of customer business, costs of incentives to customers or business partners in order to maintain their relationships, loss of investor confidence and a reduction in First Defiance's stock price, litigation, increased regulatory scrutiny and potential enforcement actions, repairs of system damage, increased investments in cybersecurity (such as obtaining additional technology, making organizational changes, deploying additional personnel, training personnel and engaging consultants), and increased insurance premiums, all of which could result in financial loss and material adverse effects on First Defiance's results of operations and financial condition.

If First Defiance forecloses on collateral property resulting in First Defiance's ownership of the underlying real estate, First Defiance may be subject to the increased costs associated with the ownership of real property, resulting in reduced income.

A significant portion of First Defiance's loan portfolio is secured by real property. During the ordinary course of business, First Defiance may foreclose on and take title to properties securing certain loans. In doing so, there is a risk that hazardous or toxic substances could be found on these properties.

If hazardous or toxic substances are found, First Defiance may be liable for remediation costs, as well as for personal injury and property damage.

In addition, when First Defiance forecloses on real property, the amount First Defiance realizes after a default is dependent upon factors outside of First Defiance's control, including, but not limited to, economic conditions, neighborhood real estate values, interest rates, real estate taxes, operating expenses of the mortgaged properties, zoning laws, governmental rules, regulations and fiscal policies, and acts of God. Certain expenditures associated with the ownership of real estate, principally real estate taxes and maintenance costs, may adversely affect the income from the real estate. Therefore, the cost of operating real property may exceed the rental income earned from such property, and First Defiance may have to sell the property at a loss. The foregoing expenditures could adversely affect First Defiance's financial condition and results of operations.

First Defiance's business strategy includes planned growth, with a focus on strategic acquisitions. First Defiance's financial condition and results of operations could be negatively affected if First Defiance fails to grow or fails to manage its growth effectively.

First Defiance's ability to grow successfully will depend on a variety of factors, including the continued availability of desirable business opportunities, its ability to integrate mergers and other acquisitions and manage growth and First Defiance's ability to raise capital. There can be no assurance that growth opportunities will be available.

First Defiance may acquire other financial institutions or parts of institutions in the future, open new branches, and consider new lines of business and new products or services. Expansions of its business would involve a number of expenses and risks, including:

- the time and costs associated with identifying and evaluating potential acquisitions or expansions into new markets;
- the potential inaccuracy of estimates and judgments used to evaluate the business and risks with respect to target institutions;
- the time and costs of hiring local management and opening new offices;
- the delay between commencing making acquisitions or engaging in new activities and the generation of profits from the expansion;
- First Defiance's ability to finance an expansion and the possible dilution to existing shareholders;
- the diversion of management's attention to the expansion;
- management's lack of familiarity with new market areas;
- the integration of new products and services and new personnel into First Defiance's existing business;
- the incurrence and possible impairment of goodwill associated with an acquisition and effects on First Defiance's results of operations; and
- the risk of loss of key employees and customers.

If First Defiance's growth involves the acquisition of companies through mergers or other acquisitions, the success of such acquisitions will depend on, among other things, First Defiance's ability to combine the businesses in a manner that permits growth opportunities and cost efficiencies, and does not cause inconsistencies in standards, controls, procedures and policies that adversely affect the ability of First Defiance to maintain relationships with customers and employees or to achieve the anticipated benefits of the acquisitions.

Failure to manage First Defiance's growth effectively could have a material adverse effect on its business, future prospects, financial condition or results of operations and could adversely affect First Defiance's ability to successfully implement its business strategy.

First Defiance's ability to pay dividends is subject to regulatory limitations which, to the extent First Defiance requires such dividends in the future, may affect its ability to pay dividends or repurchase its stock.

As a savings and loan holding company, First Defiance is a separate legal entity from First Federal and does not have significant operations of its own. Dividends from First Federal provide a significant source of capital for First Defiance. The availability of dividends from First Federal is limited by various statutes and regulations. The federal banking regulators require that insured financial institutions and their holding companies should generally only pay dividends out of current operating earnings. It is possible, depending upon the financial condition of First Federal and other factors, that the OCC, as First Federal's primary regulator, could assert that the payment of dividends or other payments by First Federal are an unsafe or unsound practice. In the event First Federal is unable to pay dividends to First Defiance, First Defiance may not be able to pay its obligations as they become due, repurchase its stock, or pay dividends on its common stock. Consequently, the potential inability to receive dividends from First Defiance could adversely affect First Defiance's business, financial condition, results of operations or prospects.

Failure to integrate or adopt new technology may undermine First Defiance's ability to meet customer demands, leading to adverse effects on First Defiance's financial condition and results of operations.

The financial services industry is continually undergoing rapid technological change with frequent introductions of new technology-driven products and services. The effective use of technology increases efficiency and enables financial institutions to better serve customers and to reduce costs. First Defiance's future success depends, in part, upon its ability to address the needs of its customers by using technology to provide products and services that will satisfy customer demands, as well as to create additional efficiencies it is operations. First Defiance may not be able to effectively implement or have the resources to implement new technology-driven products and services or be successful in marketing these products and services to its customers. Failure to successfully keep pace with technological change affecting the financial services industry could adversely affect First Defiance's business, financial condition, or results of operations.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

At December 31, 2017, First Federal conducted its business from its main office at 601 Clinton Street, Defiance, Ohio, and forty-two other full-service banking centers in northwest and central Ohio, northeast Indiana and southeast Michigan as well as a loan production office in southeast Michigan. First Insurance conducted its business from nine offices in northwest Ohio.

In January 2017, First Federal opened a branch located at 1707 Cherry St., Toledo, Ohio. This office is leased.

In February 2017, First Federal acquired seven branches in the Commercial Savings Bank acquisition: 118 S. Sandusky Ave., Upper Sandusky, Ohio; 112 E. Liberty St., Arlington, Ohio; 128 S. Vance St., Carey, Ohio; 1660 Tiffin Ave., Findlay, Ohio; 17480 Cherokee St., Harpster, Ohio; 279 Jamesway Dr., Marion, Ohio; 195 Barks Rd. West, Marion, Ohio. These offices are owned. The branch located at 1660 Tiffin Ave., Findlay, Ohio was closed on June 30, 2017.

In April 2017, First Insurance acquired four insurance offices in the Corporate One acquisition: 107 Ditto St., Suite 400, Archbold, Ohio; 101 W. Sandusky St., Suite 306, Findlay, Ohio; 1650 N. Countyline St., Suite 200, Fostoria, Ohio and 643 Miami St., Suite 5, Tiffin, Ohio. These offices are leased.

In November 2017, First Defiance entered into a lease agreement for the office located at 5520 Monroe St., Sylvania, Ohio. This office opened as a branch for First Federal and an insurance office for First Insurance in January 2018. Two First Insurance offices moved into this location: 1755 Indian Wood Cir., Maumee, Ohio and 4350 Navarre Ave., Oregon, Ohio. These leases were terminated in January 2018.

In December 2017, First Federal entered into a lease agreement for the office located at 1995 Highland Dr., Ann Arbor, Michigan. This office opened in December as a loan production office.

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 Rd., Defiance, Ohio.

The following table sets forth certain information with respect to the offices and other properties of the Company at December 31, 2017. See Note 9 to the Consolidated Financial Statements.

Description/address	Leased/ Owned	Net Book Value of Property	Deposits
		(In Thousands)	
First Federal			
Main Office			
601 Clinton St., Defiance, OH	Owned	$ 3,120	$ 223,102
Operations Center			
25600 Elliott Rd., Defiance, OH	Owned	4,641	N/A
Branch Offices, First Federal			
204 E. High St., Bryan, OH	Owned	531	161,290
211 S. Fulton St., Wauseon, OH	Owned	315	80,641
625 Scott St., Napoleon, OH	Owned	828	80,346
1050 E. Main St., Montpelier, OH	Owned	229	47,772
1800 Scott St., Napoleon, OH	Owned	1,078	35,850
1177 N. Clinton St., Defiance, OH	Owned, Land Lease	682	43,910
905 N. Williams St., Paulding, OH	Owned	623	85,825
201 E. High St., Hicksville, OH	Owned	269	35,894
3900 N. Main St., Findlay, OH	Owned	772	60,326
1694 N. Countyline St., Fostoria, OH	Owned	536	68,386
1226 W. Wooster St., Bowling Green, OH	Owned	843	123,336
301 S. Main St., Findlay, OH	Owned	728	104,224
405 E. Main St., Ottawa, OH	Owned	265	96,342
124 E. Main St., McComb, OH	Owned	151	20,127
7591 Patriot Dr., Findlay, OH	Owned	1,000	47,873
417 W. Dussel Dr., Maumee, OH	Owned, Land Lease	665	84,692
230 E. Second St., Delphos, OH	Owned	819	104,705
105 S. Greenlawn Ave., Elida, OH	Owned	289	42,760
2600 Allentown Rd., Lima, OH	Owned	906	48,769
22020 W. State Rt. 51, Genoa, OH	Owned	705	37,096
3426 Navarre Ave., Oregon, OH	Owned	777	41,017
1077 Louisiana Ave., Perrysburg, OH	Owned	498	44,634
2565 Shawnee Rd., Lima, OH	Owned	1,202	37,592
1595 W. Dupont Rd., Fort Wayne, IN	Leased	-	25,008
135 S. Main St., Glandorf, OH	Leased	-	16,970
300 N. Main St., Adrian, MI	Owned	583	83,999
1701 W. Maumee St., Adrian, MI	Owned	184	48,827
211 W. Main St., Morenci, MI	Owned	157	34,582
539 S. Meridian Hwy., Hudson, MI	Owned	473	49,149
1449 W. Chicago Blvd., Tecumseh, MI	Owned	1,355	65,506
1200 N. Main St., Bowling Green OH	Owned	1,529	10,903
9909 Illinois Rd, Fort Wayne, IN	Owned	1,895	47,819
4501 Cemetery Rd, Hilliard, OH	Owned	947	6,558
2920 W. Central Ave., Toledo, OH	Owned	161	1,288
118 S. Sandusky Ave., Upper Sandusky, OH	Owned	1,144	121,402

112 E. Liberty St., Arlington, OH	Owned	85	21,849
128 S. Vance St., Carey, OH	Owned	171	54,650
17480 Cherokee St., Harpster, OH	Owned	136	12,517
279 Jamesway Dr., Marion, OH	Owned	705	33,678
195 Barks Rd. West, Marion, OH	Owned	633	43,745
1707 Cherry St., Toledo, OH	Owned	72	2,447
1995 Highland Dr., Suite A, Ann Arbor, MI	Leased	-	-
5520 Monroe St., Sylvania, OH	Leased	-	250
First Insurance Group			
511 Fifth St., Defiance, OH	Leased	436	N/A
209 W. Poe Rd., Bowling Green, OH	Leased	-	N/A
204 E. High St., Bryan, OH	Leased	-	N/A
1755 Indian Wood Cir., Maumee, OH	Leased	-	N/A
4350 Navarre Ave., Oregon, OH	Leased	-	N/A
2600 Allentown Rd., Lima, OH	Leased	-	N/A
107 Ditto St., Suite 400, Archbold, OH	Leased	-	N/A
101 W. Sandusky St., Suite 306, Findlay, OH	Leased	-	N/A
1650 N. Countyline St., Suite 200, Fostoria, OH	Leased	-	N/A
643 Miami St., Suite 5, Tiffin, OH	Leased	-	N/A
5520 Monroe St., Suite A, Sylvania, OH	Leased	-	N/A
		$ 33,138	$ 2,437,656

Item 3. Legal Proceedings

First Defiance is involved in routine legal proceedings that are incidental to and occur 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

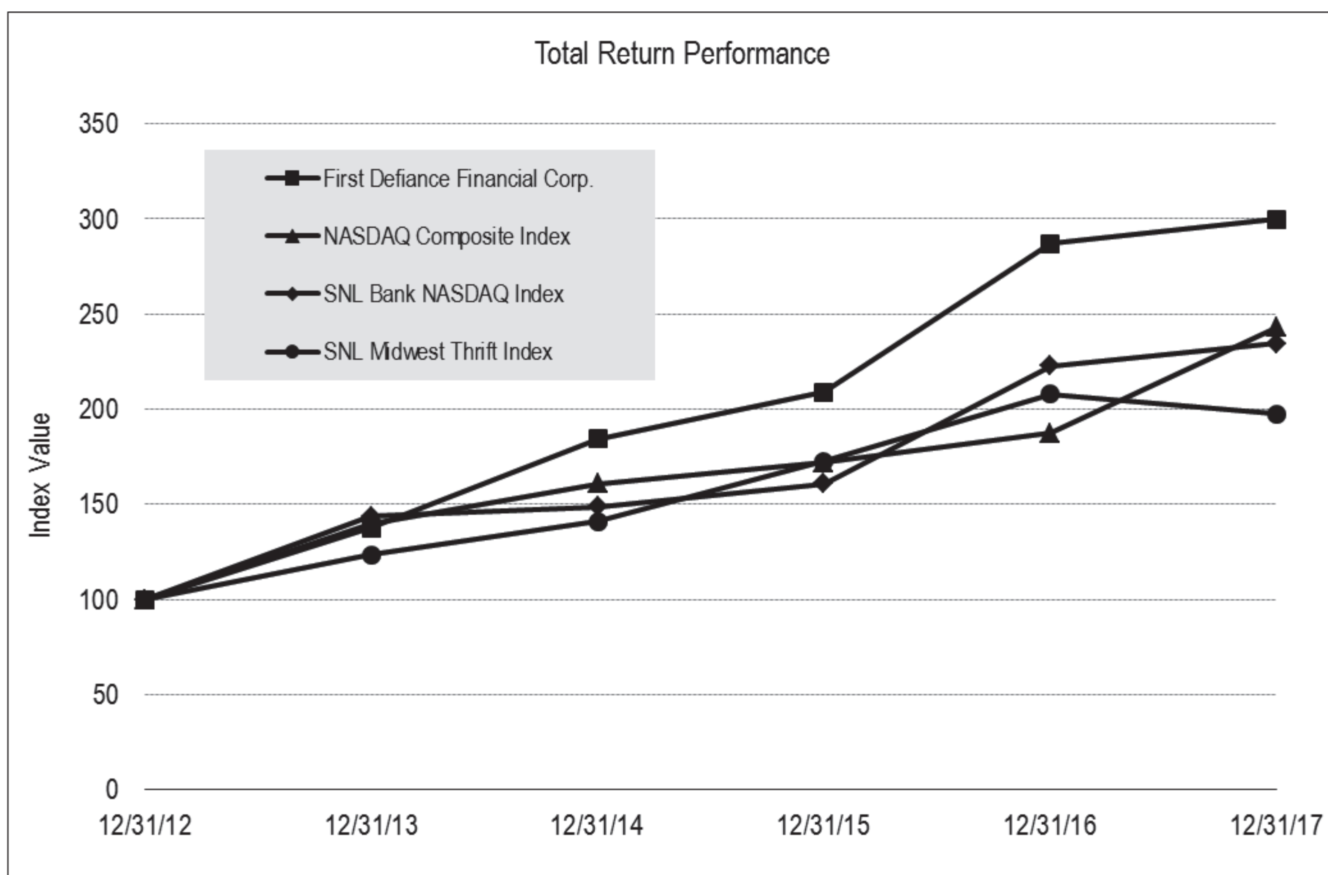
The Company's common shares trade on The NASDAQ Global Select Market under the symbol "FDEF." As of February 23, 2018, the Company had approximately 2,407 shareholders of record.

The Company's ability to pay dividends to its shareholders is subject to regulatory limitations due to the Company's dependence on First Federal as a source of capital for the payment of the dividends. The Federal Reserve expects First Defiance to serve as a source of strength for First Federal and may require First Defiance to retain capital for further investment in First Federal, rather than pay dividends to First Defiance shareholders. If federal banking regulators deem the payment of dividends to be an unsafe or unsound banking practice, the regulators, within their discretion, may restrict the Company's payment of dividends to its shareholders. 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 2017 and 2016.

	Year Ending					
	December 31, 2017			December 31, 2016		
	High	**Low**	**Dividend**	**High**	**Low**	**Dividend**
Quarter ended:						
March 31	**$ 51.15**	**$ 46.27**	**$ 0.25**	$ 40.98	$ 34.80	$ 0.22
June 30	**56.90**	**48.78**	**0.25**	41.21	37.53	0.22
September 30	**53.99**	**47.01**	**0.25**	46.83	35.90	0.22
December 31	**56.91**	**50.28**	**0.25**	52.31	36.91	0.22

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, 2012, 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.

	Period Ending					
Index	**12/31/12**	**12/31/13**	**12/31/14**	**12/31/15**	**12/31/16**	**12/31/17**
First Defiance Financial Corp.	100.00	137.61	184.50	209.03	286.93	299.75
NASDAQ Composite	100.00	140.12	160.78	171.97	187.22	242.71
SNL Bank NASDAQ	100.00	143.73	148.86	160.70	222.81	234.58
SNL Midwest Thrift	100.00	123.32	140.94	172.58	207.82	197.64



The following table provides information regarding First Defiance's purchases of its common shares during the fourth quarter period ended December 31, 2017:

Period	**Total Number of Shares Purchased**	**Average Price Paid Per Share**	**Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs**	**Maximum Number of Shares (or Approximate Dollar Value) that May Yet Be Purchased Under the Plans or Programs (1)**
October 1 – October 31, 2017	-	$ -	-	377,500
November 1 – November 30, 2017	-	-	-	377,500
December 1 – December 31, 2017	-	-	-	377,500
Total	-	$ -	-	377,500

(1) On January 29, 2016, the Company announced that its Board of Directors authorized another program for the repurchase of up to 5% of the outstanding common shares or 450,000 shares. There is no expiration date for the new repurchase program.

The information set forth under the caption **"Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters – Equity Compensation Plans"** of this Form 10-K is incorporated herein by reference.

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, 2017. 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 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				
	2017	**2016**	**2015**	**2014**	**2013**
	(Dollars in Thousands, Except Per Share Data)				
Financial Condition:					
Total assets	**$ 2,993,403**	$ 2,477,597	$ 2,297,676	$ 2,178,952	$ 2,137,148
Investment securities	**261,298**	251,176	236,678	239,634	198,557
Loans receivable, net	**2,322,030**	1,914,603	1,776,835	1,622,020	1,555,498
Allowance for loan losses	**26,683**	25,884	25,382	24,766	24,950
Nonperforming assets (1)	**32,247**	14,803	17,582	30,311	33,706
Deposits and borrowers' escrow balances	**2,440,581**	1,984,278	1,838,811	1,763,122	1,737,311
FHLB advances	**84,279**	103,943	59,902	21,544	22,520
Stockholders' equity	**373,286**	293,018	280,197	279,505	272,147
Share Information:					
Basic earnings per share	**3.23**	3.21	2.87	2.55	2.28
Diluted earnings per share	**3.22**	3.19	2.82	2.44	2.19
Book value per common share	**36.76**	32.62	30.78	30.17	27.91
Tangible book value per common share (2)	**26.49**	25.59	23.79	23.25	21.22
Cash dividends per common share	**1.00**	0.88	0.775	0.625	0.40
Dividend payout ratio	**30.96%**	27.41%	27.00%	24.51%	17.45%
Weighted average diluted shares outstanding	**10,034**	9,035	9,371	9,969	10,171
Shares outstanding end of period	**10,156**	8,983	9,102	9,235	9,720
Operations:					
Interest income	**$ 108,102**	$ 87,383	$ 80,836	$ 76,248	$ 74,781
Interest expense	**11,431**	8,440	6,781	6,559	7,170
Net interest income	**96,671**	78,943	74,055	69,689	67,611
Provision for loan losses	**2,949**	283	136	1,117	1,824
Non-interest income	**40,081**	34,030	31,803	31,641	30,778
Non-interest expense	**85,351**	71,093	67,889	66,758	65,052
Income before tax	**48,452**	41,597	37,833	33,455	31,513
Federal income tax	**16,184**	12,754	11,410	9,163	9,278
Net Income	**32,268**	28,843	26,423	24,292	22,235
Performance Ratios:					
Return on average assets	**1.13%**	1.20%	1.19%	1.12%	1.08%
Return on average equity	**9.19%**	10.10%	9.52%	8.78%	8.39%
Interest rate spread (2)	**3.74%**	3.61%	3.71%	3.57%	3.65%
Net interest margin (2)	**3.88%**	3.74%	3.81%	3.68%	3.76%
Ratio of operating expense to average total assets	**2.99%**	2.97%	3.05%	3.09%	3.16%
Efficiency ratio (2)	**61.81%**	62.20%	63.01%	65.32%	64.81%
Other Ratios:					
Equity to total assets at end of period	**12.47%**	11.83%	12.19%	12.83%	12.73%
Average equity to average assets	**12.32%**	11.91%	12.49%	12.79%	12.92%
Asset Quality Ratios:					
Nonperforming assets to total assets at end of period (1)	**1.08%**	0.60%	0.77%	1.39%	1.58%
Allowance for loan losses to total loans*	**1.14%**	1.33%	1.41%	1.50%	1.58%
Net charge-offs (recoveries) to average loans	**0.10%**	-0.01%	-0.03%	0.08%	0.23%

(1) Nonperforming assets include 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) Refer to Non-GAAP Financial Measures in Item 7- Management's Discussion and Analysis of Financial Condition and Results of Operations.

** 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 intended 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.
- 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 its subsidiaries must comply.

- 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.

This Item 7 presents information to assess the financial condition and results of operations of First Defiance. This item 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.

Non-GAAP Financial Measures

This Annual Report on Form 10-K contains GAAP financial measures and certain non-GAAP financial measures. Management believes that these measures are helpful in understanding the Company's results of operations or financial position. Fully taxable-equivalent ("FTE") is an adjustment to net interest income to reflect tax-exempt income on an equivalent before-tax basis. The following tables present a reconciliation of non-GAAP measures to their respective GAAP measures at December 31, 2017 and 2016.

Non-GAAP Financial Measures – Net Interest Income on an FTE basis, Net Interest Margin and Efficiency Ratio

($ in Thousands)		**December 31, 2017**		December 31, 2016
Net interest income (GAAP)	**$**	**96,671**	$	78,943
Add: FTE adjustment		1,914		1,830
Net interest income on a FTE basis (1)	**$**	**98,585**	$	80,773
Noninterest income – less securities gains/losses (2)	**$**	**39,497**	$	33,521
Noninterest expense (3)		**85,351**		71,093
Average interest-earning assets less average unrealized gains/losses on securities(4)		**2,542,129**		2,160,561
Average interest-earning assets		**2,545,261**		2,168,046
Average unrealized gains/losses on securities		**3,132**		7,485
Ratios:				
Net interest margin (1) / (4)		**3.88%**		3.74%
Efficiency ratio (3) / (1) + (2)		**61.81%**		62.20%

Non-GAAP Financial Measures – Tangible Book Value

($ in Thousands, except per share data)		**December 31, 2017**		December 31, 2016
Total Shareholders' Equity (GAAP)	**$**	**373,286**	$	293,018
Less: Goodwill		**(98,569)**		(61,798)
Intangible assets		**(5,703)**		(1,336)
Tangible common equity (1)	**$**	**269,014**	$	229,884
Common shares outstanding (2)		**10,156**		8,983
Tangible book value per share (1) / (2)	**$**	**26.49**	$	25.59

Overview

First Defiance is a unitary thrift holding company that conducts business through its wholly-owned 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 43 full service banking centers in fourteen northwest and central Ohio counties, one northeast Indiana county, and one southeastern Michigan county. First Federal operates one loan production office in Ann Arbor, Michigan which is located in Washtenaw 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 Archbold, Bowling Green, Bryan, Defiance, Findlay, Fostoria, Lima, Maumee, Oregon, and Tiffin, Ohio areas. The Maumee and Oregon offices were consolidated into a new office in Sylvania, Ohio in January 2018.

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, 2017, totaled $2.99 billion compared to $2.48 billion at December 31, 2016, an increase of $515.8 million or 20.8%. Cash and cash equivalents increased $14.7 million to $113.7 million at December 31, 2017 from $99.0 million at December 31, 2016. The increase in assets was due to an increase in loans receivable, net of undisbursed loan funds and deferred fees and costs, of $407.4 million, an increase in goodwill of $36.8 million and an increase in securities of $10.1 million. These increases were funded by increases in total deposits of $456.0 million. These increases were primarily due to the acquisition of CSB, which increased total assets by $367.1 million, loans by $285.4 million, goodwill and intangible assets by $33.8 million and deposits by $308.0 million. See Note 3 – Business Combinations to the Consolidated Financial Statements for further details regarding the CSB acquisition and the impact to the individual categories.

Securities

The securities portfolio increased $10.1 million to $261.3 million at December 31, 2017. The 2017 activity in the portfolio included $73.5 million of purchases, $4.3 million acquired from CSB, $1.4 million of amortization, $32.8 million of principal pay-downs and maturities, and $33.7 million of securities being sold. There was a net increase of $148,000 in the market value of available-for-sale securities. For additional information regarding First Defiance's investment securities see Note 5 to the Consolidated Financial Statements.

Loans

Loans receivable, net of undisbursed loan funds and deferred fees and costs, increased $408.2 million to $2.35 billion at December 31, 2017. For more details on the loan balances, see Note 7 – Loans Receivable to the Consolidated Financial Statements.

The majority of First Defiance's commercial real estate and commercial loans are to small and mid-sized businesses. The combined commercial, commercial real estate and multi-family real estate loan portfolios totaled $1.76 billion and $1.51 billion at December 31, 2017 and 2016, respectively, and accounted for approximately 71.4% and 74.2% of First Defiance's loan portfolio at the end of those respective periods. The net commercial and commercial real estate loan amounts acquired from CSB at the acquisition date were $194.6 million. 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 1-4 family residential portfolio totaled $274.9 million at December 31, 2017, compared with $207.6 million at the end of 2016. At the end of 2017, those loans comprised 11.1% of the total loan portfolio, up from 10.2% at December 31, 2016. The net 1-4 family residential loans acquired from CSB at the acquisition date were $58.6 million.

Construction loans, which include one-to-four family and commercial real estate properties, increased to $265.5 million at December 31, 2017, compared to $182.9 million at December 31, 2016. These loans accounted for approximately 10.8% and 9.0% of the total loan portfolio at December 31, 2017 and 2016, respectively. The net construction loans acquired from CSB at the acquisition date were $5.6 million.

Home equity and home improvement loans increased to $135.5 million at December 31, 2017, from $118.4 million at the end of 2016. At the end of 2017, those loans comprised 5.5% of the total loan portfolio, down slightly from 5.8% at December 31, 2016. The net home equity and home improvement loans acquired from CSB at the acquisition date was $15.7 million.

Consumer finance and mobile home loans were $29.1 million at December 31, 2017 up from $16.7 million at the end of 2016. These loans accounted for approximately 1.2% and 0.8% of the total loan portfolio at December 31, 2017 and 2016, respectively. The net consumer loans acquired from CSB at the acquisition date were $10.9 million.

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 a determination of value.

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 appropriate, based on First Federal's assessment of the appraisal, such as age, market, etc. First Federal will discount the appraisal 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.

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. 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.

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 ("TDR") 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 TDRs, 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 specific 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, 2017 and December 31, 2016, First Federal had $13.8 million and $10.5 million, respectively, of loans that were still performing and which were classified as TDRs.

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 commercial loan and commercial real estate loan relationships. The goal is to have approximately 55% to 60% of the portfolio reviewed annually. This includes all relationships over $5.0 million with new exposure greater than $2.0 million and a sample of other relationships greater than $5.0 million; loan relationships between $1.0 million and $5.0 million with new exposure greater than $750,000 and a sample of other relationships between $1.0 million and $5.0 million; and a sample of relationships less than $1.0 million. 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 allowance for loan loss is made up of two basic components. The first component of the allowance for loan loss is the specific reserve in which the Company sets aside reserves based on the

analysis of individual impaired credits. 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 impaired and 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 impaired and 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. The specific reserve was $758,000 at December 31, 2017, and $809,000 at December 31, 2016.

The second component 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. For purposes of the general reserve analysis, the loan portfolio is stratified into nine different loan pools based on loan type to allocate historic loss experience. The loss experience factor is then applied to the non-impaired loan portfolio. The Company utilizes loss migration measurement for each loan portfolio segment with differentiation between loan risk grades in calculating the general reserve component for non-impaired loans. Beginning December 31, 2016 the historical loss calculation was changed from using a an average of four (4) four-year loss migration periods to using an average of all four-year loss migration periods to the present beginning with data from the second quarter 2011. Management believes this enhancement is consistent with the rationale of the previous measurement but provides a more precise calculation of historical losses by incorporating more data points for the average loss ratio and including periods that provide a more complete coverage of the full business cycle. Management believes that capturing the risk grade changes and cumulative losses over the life cycle of a loan more accurately depicts management's estimate of historical losses as well as being more reflective of the ongoing risks in the loan portfolio.

The quantitative general allowance decreased $2.7 million to $6.0 million at December 31, 2017 from $8.7 million at December 31, 2016 primarily due to a decrease in the historical loss rates from the migration analysis.

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, 2017, indicated a general reserve of $20.0 million compared with $16.4 million at December 31, 2016, an increase of $3.6 million. Management reviews

the overall economic, environmental and risk factors quarterly and determines appropriate adjustments to these sub-factors based on that review.

The economic factors for all loan segments were decreased in 2017 due to economic conditions showing continued strength and sustainability, as well as strong employment data.

The environmental factors decreased slightly in 2017 in all loan segments. This is due to there being no major changes to loan policy or underwriting guidelines, the stability of the characteristics and terms of the loan portfolio and the continued favorable results of loan review, audits and examinations.

The decrease in the economic and environmental facts was offset by an increase in risk factors in all loan segments, but primarily in commercial and commercial real estate. This is due to unfavorable trends in the levels of non-performing loans and classified assets.

First Defiance's general reserve percentages for main loan segments not otherwise classified ranged from 0.44% for construction loans to 1.59% for home equity and improvement 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 2017 was $2.9 million compared to $283,000 for 2016. The allowance for loan losses was $26.7 million at December 31, 2017, and $25.9 million at December 31, 2016, and represented 1.14% and 1.33% of loans, net of undisbursed loan funds and deferred fees and costs, respectively. The decrease in the allowance for loan loss as a percentage of total loans versus a year ago was primarily attributable to the CSB acquisition. The CSB loans acquired were recorded at fair value with purchase accounting adjustments discounting the loan balance instead of an allowance for loan losses. The recorded investment and purchase accounting adjustment of loans acquired from CSB totaled $208.4 million and $3.9 million, respectively, at December 31, 2017. The provision was offset by charge offs of $3.4 million and recoveries of $1.3 million resulting in an increase to the overall allowance for loan loss of $800,000. In management's opinion, the overall allowance for loan losses of $26.7 million as of December 31, 2017, is adequate.

Management also assesses the value of OREO 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 2017, First Defiance recorded OREO write-downs that totaled $20,000. These amounts were included in other non-interest expense. Management believes that the values recorded at December 31, 2017, for OREO and repossessed assets represent the realizable value of such assets.

Total classified loans increased to $59.4 million at December 31, 2017, compared to $27.5 million at December 31, 2016, an increase of $31.9 million. There were two loan relationships totaling $11.0 million that were downgraded and resulted in an increase in net charge offs in the second quarter of 2017. In addition, there were $17.4 million of newly classified loans from the CSB acquisition due to new financial information received.

First Defiance's ratio of allowance for loan losses to non-performing loans was 86.9% at December 31, 2017, compared with 180.4% at December 31, 2016. 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, 2017, are appropriate.

At December 31, 2017, First Defiance had total non-performing assets of $32.2 million, compared to $14.8 million at December 31, 2016. 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 assets between December 31, 2017, and December 31, 2016, is in commercial loans and commercial real estate loans. The balance of commercial non-performing loans was $7.8 million higher at December 31, 2017, compared to December 31, 2016. The balance of commercial real estate loans was $8.6 million higher at December 31, 2017, compared to December 31, 2016.

Non-performing loans in the single-family residential, commercial real estate and commercial loan categories represent 1.10%, 1.47% and 1.68% of the total loans in those categories respectively at December 31, 2017, compared to 1.41%, 0.92% and 0.21% respectively for the same categories at December 31, 2016. Management believes that the current allowance for loan losses is appropriate and that the provision for loan losses recorded in 2017 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.

The net charge-offs and nonaccrual loan balances as a percentage of total are presented in the table below at December 31, 2017 and 2016.

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

	For the Twelve Months Ended December 31, 2017		**As of December 31, 2017**	
	Net Charge-offs (Recoveries)	**% of Total Net Charge-offs (Recoveries)**	**Nonaccrual Loans**	**% of Total Non-Accrual Loans**
	(In Thousands)		(In Thousands)	
Residential	**$ 164**	**7.63%**	**$ 3,037**	**9.89%**
Construction	**-**	**0.00%**	**-**	**0.00%**
Commercial real estate	**(260)**	**(12.09)%**	**18,219**	**59.32%**
Commercial	**2,058**	**95.77%**	**8,841**	**28.78%**
Consumer finance	**54**	**2.46%**	**28**	**0.09%**
Home equity and improvement	**134**	**6.23%**	**590**	**1.92%**
Total	**$ 2,150**	**100.00%**	**$ 30,715**	**100.00%**

	For the Twelve Months Ended December 31, 2016		As of December 31, 2016	
	Net Charge-offs	% of Total Net Charge-offs	Nonaccrual Loans	% of Total Non-Accrual Loans
	(In Thousands)		(In Thousands)	
Residential	$ 184	84.02%	$ 2,928	20.41%
Construction	-	0.00%	-	0.00%
Commercial real estate	(831)	(379.45)%	9,592	66.85%
Commercial	280	127.85%	1,007	7.02%
Consumer finance	30	13.70%	91	0.63%
Home equity and improvement	118	53.88%	730	5.09%
Total	$ (219)	(100.00)%	$ 14,348	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, 2017 and 2016.

Table 2 – Allowance for Loan Loss Allocation by Loan Category

	December 31, 2017		December 31, 2016	
	Amount	Percent of total loans by category	Amount	Percent of total loans by category
	(Dollars in Thousands)			
1-4 family residential	**$ 2,532**	**11.1%**	$ 2,627	10.2%
Multi-family residential real estate	**2,702**	**10.1**	2,228	9.7
Commercial real estate	**10,354**	**40.0**	10,625	41.5
Construction	**647**	**10.8**	450	9.0
Commercial loans	**7,965**	**21.3**	7,361	23.0
Home equity and improvement loans	**2,255**	**5.5**	2,386	5.8
Consumer loans	**228**	**1.2**	207	0.8
	$ 26,683	**100.0%**	$ 25,884	100.0%

Loans Acquired with Impairment

The Company has purchased loans, for which there was, at acquisition, evidence of deterioration of credit quality since origination and it was probable, at acquisition, that all contractually required payments would not be collected.

As of December 31, 2017, the total contractual receivable for those loans was $4.8 million and the recorded value was $3.8 million.

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, 2017, totaled $50.8 million, compared to $42.8 million at December 31, 2016. 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 $98.6 million at December 31, 2017, compared to $61.8 million at December 31, 2016. The acquisition of CSB increased goodwill by $28.9 million and the acquisition of Corporate One increased goodwill by $7.9 million. Core deposit intangibles and other intangible assets increased $4.4 million to $5.7 million at December 31, 2017, compared to $1.3 million at December 31, 2016. The acquisition of CSB and Corporate One increased core deposit and other intangibles by $4.9 million and $756,000, respectively. In addition there was $1.3 million of amortization expense for core deposit and other intangibles in 2017. No impairment of goodwill was recorded in 2017 or 2016.

Deposits

Total deposits at December 31, 2017 were $2.44 billion compared to $1.98 billion at December 31, 2016, an increase of $456.0 million or 23.0%. Non-interest bearing checking accounts grew by $83.7 million, interest bearing checking accounts and money markets grew by $188.9 million, savings grew by $58.7 million and retail certificates of deposit grew by $124.8 million. The net deposit amounts acquired from CSB at the acquisition date resulted in a $56.1 million increase in non-interest bearing demand deposits, $122.0 million increase in interest bearing demand and money market deposits, $31.6 million increase in savings deposits and $98.2 million increase in retail time deposits. Management can utilize the national market for certificates of deposit to supplement its funding needs if necessary. For more details on the deposit balances in general see Note 11 – Deposits to the Consolidated Financial Statements.

Borrowings

FHLB advances totaled $84.3 million at December 31, 2017 compared to $103.9 million at December 31, 2016. The balance at the end of 2017 includes $5.0 million of convertible advances with a rate of 2.35%. This advance is callable by the FHLB, at which point it would convert to a three-month LIBOR advance if not paid off. This advance has a final maturity date in March 2018. In addition, First Defiance has fifteen fixed-rate advances totaling $72.0 million with rates ranging from 1.09% to 2.16% and two amortizing advances totaling $7.3 million with rates ranging from 1.78% to 2.14%.

At December 31, 2017, First Defiance also had $26.0 million of securities that were sold with agreements to repurchase, compared to $31.8 million at December 31, 2016.

Equity

Total stockholders' equity increased $80.3 million to $373.3 million at December 31, 2017, compared to $293.0 million at December 31, 2016. The increase in stockholders' equity was the result of recording net income of $32.3 million and an increase of $56.5 million due to the acquisition of CSB as a result of issuing 1.1 million shares of common stock. These amounts were partially offset by $9.9 million of common stock dividends paid in 2017.

Results of Operations

Summary

First Defiance reported net income of $32.3 million for the year ended December 31, 2017, compared to $28.8 million and $26.4 million for the years ended December 31, 2016 and 2015, respectively. On a diluted per common share basis, First Defiance earned $3.22 in 2017, $3.19 in 2016 and $2.82 in 2015.

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.

Net interest income was $96.7 million for the year ended December 31, 2017, compared to $78.9 million and $74.1 million for the years ended December 31, 2016 and 2015, respectively. The tax-equivalent net interest margin was 3.88%, 3.74% and 3.81% for the years ended December 31, 2017, 2016 and 2015, respectively. The margin increased 14 basis points between 2016 and 2017. The increase in margin in 2017 was primarily due to CSB's earning asset mix as well an increase in interest rates. Interest-earning asset yields increased 20 basis points (to 4.33% in 2017 from 4.13% in 2016) and the cost of interest bearing liabilities between the two periods increased 7 basis points (to 0.59% in 2017 from 0.52% in 2016).

Total interest income increased by $20.7 million or 23.7% to $108.1 million for the year ended December 31, 2017, from $87.4 million for the year ended December 31, 2016. This is due to continued loan growth, the CSB acquisition, the increase in interest rates and a more profitable earning asset mix. Interest income from loans increased to $99.5 million for 2017 compared to $80.2 million in 2016, which represents an increase of 24.1%. The average balance of loans receivable increased $345.2 million to $2.2 billion at December 31, 2017, from $1.9 billion at December 31, 2016, due primarily to the CSB acquisition.

During the same period, the average balance of investment securities increased to $258.8 million in 2017 from $233.4 million for the year ended December 31, 2016. Interest income from investment securities increased to $6.9 million in 2017 compared to $6.2 million in 2016, which represents an increase of 11.1%. The overall duration of investments increased to 3.40 years at December 31, 2017, from 3.38 years at December 31, 2016.

Interest expense increased by $3.0 million in 2017 compared to 2016, to $11.4 million from $8.4 million. This increase was mainly due to a seven basis point increase in the average cost of interest-bearing liabilities in 2017 and a $297.3 million increase in the average balance of interest-bearing liabilities. The average balance of interest bearing deposits increased $305.9 million to $1.77 billion at December 31, 2017, from $1.46 billion at December 31, 2016, primarily due to the CSB acquisition. Interest expense related to interest-bearing deposits was $8.8 million in 2017 compared to $6.3 million in 2016.

Interest expenses on FHLB advances and other interest-bearing funding sources were $1.5 million and $208,000 respectively, in 2017 and $1.3 million and $138,000 respectively in 2016. The increase in FHLB advance expense was due to rising interest rates and a $16.3 million increase in the average balance of FHLB advances to $102.2 million at December 31, 2017, compared to $85.9 million at December 31, 2016. Interest expense recognized by the Company related to subordinated debentures was $935,000 in 2017 and $753,000 in 2016 due to rising rates.

Total interest income increased by $6.6 million or 8.1% to $87.4 million for the year ended December 31, 2016, from $80.8 million for the year ended December 31, 2015. The increase in interest income was due to the significant increase in loan volume. The average balance of loans receivable increased $166.0 million to $1.85 billion at December 31, 2016, from $1.69 billion at December 31, 2015. Interest income from loans increased to $80.2 million for 2016 compared to $73.3 million in 2015, which represents an increase of 9.4%.

During the same period, the average balance of investment securities decreased to $233.4 million for 2016 from $239.9 million for the year ended December 31, 2015. Interest income from investment securities decreased to $6.2 million in 2016 compared to $6.8 million in 2015, which represents a decrease of 7.7%. The overall duration of investments decreased to 3.6 years at December 31, 2016, from 4.2 years at December 31, 2015.

Interest expense increased by $1.6 million in 2016 compared to 2015, to $8.4 million from $6.8 million. This increase was mainly due to an eight basis point increase in the average cost of interest-bearing liabilities in 2016 and a $110.2 million increase in the average balance of interest-bearing liabilities. The average balance of interest bearing deposits increased $64.3 million to $1.46 billion at December 31, 2016, from $1.40 billion at December 31, 2015. Interest expense related to interest-bearing deposits was $6.3 million in 2016 compared to $5.3 million in 2015.

Interest expenses on FHLB advances and other interest-bearing funding sources were $1.3 million and $138,000 respectively, in 2016 and $675,000 and $152,000 respectively in 2015. The increase in FHLB advance expense was due to a $47.7 million increase in the average balance of FHLB advances to $85.9 million at December 31, 2016, compared to $38.1 million at December 31, 2015. Interest expense recognized by the Company related to subordinated debentures was $753,000 in 2016 and $613,000 in 2015 due to rising rates.

The following table shows an analysis of net interest margin on a tax equivalent basis for the years ended December 31, 2017, 2016 and 2015:

Table 3 – Net Interest Margin

	Year Ended December 31 (In Thousands)								
	2017			2016			2015		
	Average Balance	Interest (1)	Yield/ Rate (2)	Average Balance	Interest (1)	Yield/ Rate	Average Balance	Interest (1)	Yield/ Rate
Interest-Earning Assets:									
Loans receivable (5)	$ 2,198,639	$ 99,742	4.54%	$ 1,853,419	$80,423	4.34%	$ 1,687,413	$73,544	4.36%
Securities (6)	258,775	8,654	3.39%	233,407	7,871	3.48%	239,852	8,476	3.64%
Interest-earning deposits	72,215	836	1.16%	67,420	367	0.54%	59,410	169	0.27%
FHLB stock	15,632	784	5.02%	13,800	552	4.00%	13,802	552	4.00%
Total interest-earning assets	2,545,261	110,016	4.33%	2,168,046	89,213	4.13%	2,000,477	82,741	4.15%
Non-interest-earning assets	306,270			229,393			222,389		
Total Assets	$2,851,531			$2,397,439			$2,222,866		
Interest-Bearing Liabilities:									
Interest-bearing deposits	$ 1,769,786	$8,818	0.50%	$ 1,463,890	$6,261	0.43%	$ 1,399,619	$5,341	0.38%
FHLB advances	102,155	1,470	1.44%	85,856	1,288	1.50%	38,134	675	1.77%
Subordinated debentures	36,156	935	2.58%	36,141	753	2.09%	36,129	613	1.70%
Other borrowings	27,929	208	0.74%	52,826	138	0.26%	54,619	152	0.28%
Total interest-bearing liabilities	1,936,026	11,431	0.59%	1,638,713	8,440	0.52%	1,528,501	6,781	0.44%
Non-interest bearing demand deposits	528,926	–		441,731	–		388,257	–	
Total including non-interest- bearing demand deposits	2,464,952	11,431	0.46%	2,080,444	8,440	0.41%	1,916,758	6,781	0.35%
Other non-interest liabilities	35,343			31,361			28,463		
Total Liabilities	2,500,295			2,111,805			1,945,221		
Stockholders' equity	351,236			285,634			277,645		
Total liabilities and stockholders' equity	$ 2,851,531			$ 2,397,439			$ 2,222,866		
Net interest income; interest rate spread (3)		$98,585	3.74%		$80,773	3.61%		$75,960	3.71%
Net interest margin (4)			3.88%			3.74%			3.81%
Average interest-earning assets to average interest-bearing liabilities			131.5%			132.3%			130.9%

(1) Interest on certain tax exempt loans (amounting to $375,000, $383,000 and $368,000 in 2017, 2016 and 2015 respectively) and tax-exempt securities ($3.2 million, $3.0 million and $3.2 million in 2017, 2016, and 2015) is not taxable for Federal income tax purposes. The average balance of such loans was $11.5 million, $11.8 million and $10.7 million in 2017, 2016, and 2015 while the average balance of such securities was $91.2 million, $83.4 million and $86.0 million in 2017, 2016, and 2015, 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, 2017, the yields earned and rates paid were as follows: loans receivable, 4.45%; securities, 3.12%; FHLB stock, 5.50%; total interest-earning assets, 4.32%; deposits, 0.30%; FHLB advances, 1.51%; other borrowings, 0.19%, subordinated debentures, 3.02%; total including non- interest-bearing liabilities, 0.39%; and interest rate spread, 3.93%.

(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 excluding average unrealized gains/losses. See Non-GAAP Financial Measure discussion for further details.

(5) For the purpose of the computation for loans, non-accrual loans are included in the average loans outstanding.

(6) Securities yield = annualized interest income divided by the average balance of securities, excluding average unrealized gains/losses. See Non-GAAP Financial Measure discussion for further details.

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 (1)

	Year Ended December 31 (In Thousands)					
	2017 vs. 2016			**2016 vs. 2015**		
	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	**$ 3,792**	**$ 15,527**	**$ 19,319**	$ (326)	$ 7,205	$ 6,879
Securities	**(66)**	**849**	**783**	(381)	(224)	(605)
Interest-earning deposits	**441**	**28**	**469**	173	25	198
FHLB stock	**152**	**80**	**232**	-	-	-
Total interest-earning assets	**$ 4,319**	**$ 16,484**	**$ 20,803**	$ (534)	$ 7,006	$ 6,472
Interest-Bearing Liabilities						
Deposits	**$ 1,128**	**$ 1,429**	**$ 2,557**	$ 667	$ 253	$ 920
FHLB advances	**(54)**	**236**	**182**	(117)	730	613
Subordinated Debentures	**182**	**-**	**182**	140	-	140
Notes Payable	**159**	**(89)**	**70**	(9)	(5)	(14)
Total interest- bearing liabilities	**$ 1,415**	**$ 1,576**	**$ 2,991**	$ 681	$ 978	$ 1,659
Increase (decrease) in net interest income			**$ 17,812**			**$ 4,813**

(1) The change in interest rates due to both rate and volume has been allocated between the factors in proportion to the relationship of the absolute dollar amounts of the change in each.

Provision for Loan Losses – First Defiance's provision for loan losses was $2.9 million for the year ended December 31, 2017, compared to $283,000 for December 31, 2016, and $136,000 for December 31, 2015.

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 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 this Management's Discussion and Analysis and Note 7 to the Consolidated Financial Statements.

Noninterest Income – Noninterest income increased by $6.1 million or 17.8% in 2017 to $40.1 million from $34.0 million for the year ended December 31, 2016. That followed an increase of $2.2 million or 7.0% in 2016 from $31.8 million in 2015.

Service fees and other charges increased to $12.1 million for the year ended December 31, 2017, from $10.9 million for 2016 and increased from $10.8 million for 2015. The increase in noninterest income in 2017 from 2016 and 2015 is due to increased number of deposit accounts primarily from the CSB acquisition.

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, 2017 and 2016 related to the overdraft privilege product, net of adjustments to the allowance for uncollectible overdrafts, were $2.8 million and $2.4 million, respectively. Accounts charged off are included in noninterest expense. The allowance for uncollectible overdrafts was $24,000 at December 31, 2017, and $14,000 at December 31, 2016.

Noninterest income also includes gains, losses and impairment on investment securities. In 2017, First Defiance realized a $584,000 gain on sale of securities. In 2016, a $509,000 gain was recognized compared to a $22,000 gain in 2015.

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 $7.0 million, $7.3 million and $6.7 million in 2017, 2016 and 2015, respectively. The $266,000 decrease in 2017 from 2016 is attributable to a $647,000 decrease in the gain on sale of loans, along with a $33,000 negative change in the valuation adjustments on mortgage servicing rights. These were partially offset by a decrease of $260,000 in mortgage servicing rights amortization expense along with a $154,000 increase in servicing revenue. First Defiance originated $213.5 million of residential mortgages for sale into the secondary market in 2017 compared with $263.7 million in 2016. The balance of the mortgage servicing right valuation allowance stands at $432,000 at the end of 2017. The $557,000 increase in 2016 from 2015 is attributable to a $747,000 increase in the gain on sale of loans, along with a $57,000 positive change in servicing revenue. These were partially offset by an increase of $104,000 in mortgage servicing rights amortization expense along with a $143,000 negative change in the valuation adjustments on mortgage servicing rights. First Defiance originated $263.7 million of residential mortgages for sale into the secondary market in 2016 compared with $213.4 million in 2015. The balance of the mortgage servicing right valuation allowance stands at $522,000 at the end of 2016. See Note 8 to the Consolidated Financial Statements.

Gains on the sale of non-mortgage loans, which include SBA and FSA loans, totaled $217,000 in 2017 compared to $753,000 in 2016 and $824,000 in 2015. The volume of eligible small business administration loans has decreased in 2017 from levels in 2016 and 2015.

Insurance commission income increased $2.4 million or 23.2% to $12.9 million in 2017 from $10.4 million in 2016 mainly due to the acquisition of Corporate One and an increase in general production in the property and casualty and group employee benefits lines of business. Insurance commission income increased $365,000 or 3.6% to $10.4 million in 2016 from $10.1 million in 2015.

Income from bank owned life insurance increased $2.1 million in 2017 to $3.1 million from $909,000 in 2016. In 2017, the Company surrendered an underperforming BOLI policy and recorded a tax penalty of $1.7 million (recorded in income tax expense) and purchased a new BOLI policy receiving a $1.5 million enhancement value gain. There was a slight increase in income in 2016 to $909,000 from $895,000 in 2015.

Trust income increased $631,000 to $2.3 million in 2017 from $1.7 million in 2016 and $1.5 million. The increase in 2017 included a $428,000 positive adjustment to accrual basis accounting.

Other income increased $316,000 to $1.9 million in 2017 compared to $1.5 million in 2016 and $1.1 million in 2015. The $316,000 increase in 2017 is due mainly to group benefit referral fees. The $479,000 increase in 2016 from 2015 is due to a $231,000 increase in the value of the assets of the Company's deferred compensation plan as well as a $139,000 increase in the gain on sale of other real estate owned.

Noninterest Expense – Total noninterest expense for 2017 was $85.4 million compared to $71.1 million for the year ended December 31, 2016, and $67.9 million for the year ended December 31, 2015.

Compensation and benefits increased $9.7 million or 24.0% to $49.8 million from $40.2 million in 2016. The increase is mainly related to personnel expenses both from certain benefit payouts associated with the CSB merger as well as operating the new CSB and Corporate One locations, merit increases and other new staff for growth strategies. Other non-interest expenses increased $2.8 million or 17.5% to $18.8 million in 2017 from $16.0 million in 2016. This is due mainly to $2.1 million increase in expenses associated with the acquisition of CSB and Corporate One, as well as an increase in the amortization of intangibles of $754,000. Occupancy expense increased $289,000, to $7.7 million in 2017 compared to $7.4 million in 2016 and data processing expense increased $1.4 million to $7.7 million in 2017 from $6.4 million in 2016.

Compensation and benefits increased $2.4 million or 6.4% to $40.2 million from $37.8 million in 2015. The increase is mainly related to merit increases and new staff for growth strategies, higher incentive compensation accruals and higher medical insurance costs. Other non-interest expenses increased $436,000 or 2.8% to $16.0 million in 2016 from $15.5 million in 2015 mainly due to acquisition related costs for the pending acquisition of CSB and $300,000 for a termination of a lease partially offset by a decrease in the amortization of intangibles of $164,000. Occupancy expense increased by $221,000 to $7.4 million in 2016 compared to $7.2 million in 2015 and data processing expense increased by $284,000 to $6.4 million in 2016 from $6.1 million in 2015. These increases were partially offset by decreases in FDIC insurance premiums of $155,000.

Income Taxes – Income taxes totaled $16.2 million in 2017 compared to $12.8 million in 2016 and $11.4 million in 2015. The effective tax rates for those years were 33.4%, 30.7%, and 30.2%, respectively. The tax rate is lower than the statutory 35% tax rate for the Company mainly because of investments in tax-exempt securities. The increase in the effective tax rate in 2017 primarily relates to the surrender of a bank-owned life insurance policy which added $1.7 million to income tax expense. The earnings on tax-exempt securities are not subject to federal income tax. See Note 18 – Income Taxes to the Consolidated 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, central Ohio 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 $838.1 million at December 31, 2017, which represents 34.9% 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 0.19% at December 31, 2017. 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 $36.0 million, $27.0 million and $30.7 million in 2017, 2016 and 2015, 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. In 2017 and 2016, the Company purchased $11.5 million and $822,000, respectively, in portfolio residential home loans. There were no purchases in 2015.

In considering the more typical investing activities, during 2017, $32.7 million and $34.2 million was generated from the combination of maturity or pay-downs and the sale or call of available-for-sale investment securities, respectively, and $133.4 million was used by an increase in loans while $73.0 million was used to purchase available-for-sale investment securities. During 2016, $36.4 million and $14.9 million was generated from the combination of maturity or pay-downs and the sale or call of available-for-sale investment securities, respectively, and $158.1 million was used by an increase in loans while $71.3 million was used to purchase available-for-sale investment securities. During 2015, $31.2 million and $426,000 was generated from the combination of maturity or pay-downs and the sale or call of available-for-sale investment securities, respectively, and $177.0 million was used by an increase in loans while $30.5 million was used to purchase available-for-sale investment securities.

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. In 2017, total deposits increased by $148.1 million. Securities sold under repurchase arrangements decreased by $5.8 million in 2017. Also in 2017, the Company paid $9.9 million in common stock dividends. In 2016, total deposits increased by $145.5 million. Securities sold under repurchase arrangements decreased by $25.4 million in 2016. Also in 2016, the Company paid $7.9 million in common stock dividends coupled with paying $6.3 million in common stock repurchases. In 2015, total deposits increased by $75.7 million. Securities sold under repurchase arrangements increased by $2.4 million in 2015. Also in 2015, the Company paid $7.2 million in common stock dividends coupled with paying $8.4 million in common stock repurchases. 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, 2017, First Defiance had the following commitments to fund deposit, advance, borrowing obligations and post-retirement benefits:

Table 5 – Contractual Obligations

Contractual Obligations	Total	Less than 1 year	1-3 years	4-5 years	After 5 years
	Maturity Dates by Period at December 31, 2017				
			(In Thousands)		
Certificates of deposit	$558,755	$252,895	$233,192	$72,532	136
FHLB fixed advances including interest (1)	86,574	35,018	37,227	10,451	3,878
Subordinated debentures	36,083	-	-	-	36,083
Securities sold under repurchase agreements	26,019	26,019	-	-	-
Lease obligations	11,025	826	1,360	1,149	7,690
Post-retirement benefits	2,023	174	375	401	1,073
Total contractual obligations	$720,479	$314,932	$272,154	$84,533	$48,860

(1) Includes principal payments of $84,306 and interest payments of $2,268.

At December 31, 2017, First Defiance had the following commitments to fund loan or line of credit obligations:

Table 6 - Commitments

Commitments	Total Amounts Committed	Less than 1 year	1-3 years	4-5 years	After 5 years
		Amount of Commitment Expiration by Period			
			(In Thousands)		
Fixed commitments to make loans	$42,458	$19,434	$969	$1,791	$20,264
Variable commitments to make loans	161,778	14,029	1,308	10,306	136,135
Fixed unused lines of credit	6,245	2,405	1,940	1,900	-
Variable unused lines of credit	408,831	264,025	14,923	6,152	123,731
Total loan commitments	619,312	299,893	19,140	20,149	280,130
Standby letters of credit	7,605	7,170	420	15	-
Total Commitments	$626,917	$307,063	$19,560	$20,164	$280,130

In addition to the above commitments, at December 31, 2017, First Defiance had commitments to sell $14.9 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, and brokered certificates of deposit. At December 31, 2017, First Defiance had $567.4 million in capacity under its agreements with the FHLB.

First Federal is subject to various capital requirements of the OCC. At December 31, 2017, 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 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 Consolidated 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.

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.

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 Allowance for Loan Losses in this Management's Discussion and Analysis 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 in this Management's Discussion and Analysis and Note 2 - Statement of Accounting Policies and Note 8 - Mortgage Banking to the Consolidated Financial Statements, for a further description of First Defiance's valuation process, methodology and assumptions along with sensitivity analyses.

Goodwill - First Defiance has two reporting units: First Federal and First Insurance. At December 31, 2017, First Defiance had goodwill of $98.6 million, including $80.0 million in First Federal, representing 81% of total goodwill and $18.6 million in First Insurance, representing 19% 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, 2017 and 2016.

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, 2017, 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 2.62% 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 commercial real estate and commercial loan areas. In addition to carrying higher credit risk than residential mortgage lending, such loans tend to be more rate sensitive than residential mortgage loans. The balance of First Federal's commercial real estate and multi-family real estate loan portfolio was $1.24 billion, which was split between $156.7 million of fixed-rate loans and $1.08 billion of adjustable-rate loans, at December 31, 2017. The commercial loan portfolio increased to $526.1 million, which was split between $176.9 million of fixed-rate loans and $349.2 million of adjustable-rate loans, at December 31, 2017. 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 ($135.5 million at December 31, 2017) of which $118.4 million fluctuate with changes in the prime lending rate and $17.1 million of home equity and improvement loans have fixed rates. First Federal also has consumer loans ($29.1 million at December 31, 2017) 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.

The table below presents, for the twelve months subsequent to December 31, 2017, and December 31, 2016, an estimate of the change in net interest income that would result from a gradual (ramp) and immediate (shock) change in interest rates, moving in a parallel fashion over the entire yield curve, relative to the measured base case scenario. Based on our net interest income simulation as of December 31, 2017, net interest income sensitivity to changes in interest rates for the twelve months subsequent to December 31, 2017 was slightly more liability sensitive for the ramp and shock compared to the sensitivity profile for the twelve months subsequent to December 31, 2016.

Table 7 – Net Interest Income Sensitivity Profile

(dollars in thousands)	Impact on Future Annual Net Interest Income December 31, 2017		December 31, 2016	
Gradual Change in Interest Rates				
+200	$ 2,354	2.18%	$ 1,970	2.32%
+100	1,200	1.11%	972	1.14%
-100	(3,033)	-2.81%	(2,201)	-2.59%
Immediate Change in Interest Rates				
+200	$ 4,821	4.47%	$ 4,236	4.99%
+100	2,463	2.28%	2,131	2.51%
-100	(6,223)	-5.77%	(4,132)	-4.87%

To analyze the impact of changes in interest rates in a more realistic manner, non-parallel interest rate scenarios are also simulated. These non-parallel interest rate scenarios indicate that net interest income may decrease from the base case scenario should the yield curve flatten or become inverted. Conversely, if the yield curve should steepen, net interest income may increase.

The results of all the simulation scenarios are within the Board mandated guidelines as of December 31, 2017, except for the down 100 basis points over the first twelve months in a static and dynamic-shock balance sheet as well as in the down 100 basis points for a cumulative twenty-four months in a static and dynamic ramp balance sheet. Management is reviewing the Board policy limits in all scenarios to determine if they are adequate and if so, any measures to be taken to bring the current results back into alignment with Board mandated guidelines.

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, 2017, was considered to be unlikely 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.

Table 8 – Economic Value of Equity Analysis

December 31, 2017

	Economic Value of Equity			Economic Value of Equity as % of Present Value of Assets	
Change in Rates	**$ Amount**	**$ Change**	**% Change**	**Ratio**	**Change**
		(Dollars in Thousands)			
+ 400 bp	**700,563**	**80,544**	**12.99%**	**25.63%**	**462 bp**
+ 300 bp	**685,883**	**65,864**	**10.62%**	**24.63%**	**362 bp**
+ 200 bp	**668,127**	**48,108**	**7.76%**	**23.53%**	**252 bp**
+ 100 bp	**647,439**	**27,420**	**4.42%**	**22.36%**	**135 bp**
0 bp	**620,019**	**-**	**-**	**21.01%**	**–**
- 100 bp	**585,967**	**(34,052)**	**(5.49)%**	**19.52%**	**(149) bp**

December 31, 2016

	Economic Value of Equity			Economic Value of Equity as % of Present Value of Assets	
Change in Rates	**$ Amount**	**$ Change**	**% Change**	**Ratio**	**Change**
		(Dollars in Thousands)			
+ 400 bp	569,397	85,791	17.74%	24.99%	522 bp
+ 300 bp	553,285	69,679	14.41%	23.86%	408 bp
+ 200 bp	534,478	50,873	10.52%	22.63%	286 bp
+ 100 bp	512,132	28,526	5.90%	21.30%	153 bp
0 bp	483,606	-	-	19.77%	–
- 100 bp	429,266	(34,339)	(7.10)%	17.29%	(249) bp

Based on the above analysis, in the event of a 200 basis point increase in interest rates as of December 31, 2017, First Federal would experience a 7.76% 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, 2017, was 1.86 years while the average duration of its liabilities was 3.65 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.

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. Internal control over financial reporting is defined in Rule 13a-15(f) promulgated under the Securities Exchange Act of 1934 as a process designed by, or under the supervision of our principal executive and principal financial officers and effected by the Board of Directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with U.S. generally accepted accounting principles and 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 our assets;

2. Provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with U.S. generally accepted accounting principles, and that our receipts and expenditures are being made only in accordance with authorizations of our management and directors; and

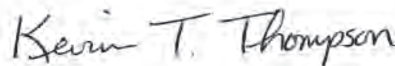
3. Provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of our assets that could have a material effect on the financial statements.

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 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 2013 Internal Control – Integrated Framework, management concluded that our internal control over financial reporting was effective as of December 31, 2017.

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, 2017. The report, which expresses an unqualified opinion on the effectiveness of the Company's internal control over financial reporting as of December 31, 2017, is included in this Item 8.

Donald P. Hileman
President and
Chief Executive Officer



Kevin T. Thompson
Executive Vice President and
Chief Financial Officer

Report of Independent Registered Public Accounting Firm

Stockholders and the Board of Directors of
First Defiance Financial Corp.
Defiance, Ohio

Opinions on the Financial Statements and Internal Control over Financial Reporting

We have audited the accompanying consolidated statements of financial condition of First Defiance Financial Corp. (the "Company") as of December 31, 2017 and 2016, the related consolidated statements of income, comprehensive income, changes in stockholders' equity, and cash flows for each of the years in the three-year period ended December 31, 2017, and the related notes (collectively referred to as the "financial statements"). We also have audited the Company's internal control over financial reporting as of December 31, 2017, based on criteria established in Internal Control – Integrated Framework: (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO)".

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2017 and 2016, and the results of its operations and its cash flows for each of the years in the three-year period ended December 31, 2017 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2017, based on criteria established in Internal Control – Integrated Framework: (2013) issued by COSO."

Basis for Opinions

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 the Company's financial statements and an opinion on the Company's internal control over financial reporting based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) ("PCAOB") and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud, and whether effective internal control over financial reporting was maintained in all material respects.

Our audits of the financial statements included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. 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.

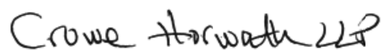
Definition and Limitations of Internal Control Over Financial Reporting

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.

We have served as the Company's auditor since 2005.



Crowe Horwath LLP
South Bend, Indiana
February 28, 2018

First Defiance Financial Corp.

Consolidated Statements of Financial Condition

Dollars in Thousands, except per share data

	December 31	
	2017	2016
Assets		
Cash and cash equivalents:		
Cash and amounts due from depository institutions	**$ 58,693**	$ 53,003
Federal funds sold	**55,000**	46,000
	113,693	99,003
Securities available-for-sale, carried at fair value	**260,650**	250,992
Securities held-to-maturity, carried at amortized cost (fair value $649 and $187 at December 31, 2017 and 2016 respectively)	**648**	184
	261,298	251,176
Loans held for sale	**10,435**	9,607
Loans receivable, net of allowance of $26,683 and $25,884 at December 31, 2017 and 2016, respectively	**2,322,030**	1,914,603
Mortgage servicing rights	**9,808**	9,595
Accrued interest receivable	**8,706**	6,760
Federal Home Loan Bank (FHLB) stock	**15,992**	13,798
Bank owned life insurance	**66,230**	52,817
Premises and equipment	**40,217**	36,958
Real estate and other assets held for sale (REO)	**1,532**	455
Goodwill	**98,569**	61,798
Core deposit and other intangibles	**5,703**	1,336
Deferred taxes	**231**	2,212
Other assets	**38,959**	17,479
Total assets	**$ 2,993,403**	$ 2,477,597

continued

First Defiance Financial Corp

Consolidated Statements of Financial Condition (continued)

Dollars in Thousands, except per share data

	December 31	
	2017	**2016**
Liabilities and stockholders' equity		
Liabilities:		
Deposits:		
Noninterest-bearing	**$ 571,360**	$ 487,663
Interest-bearing	**1,866,296**	1,493,965
Total	**2,437,656**	1,981,628
Advances from the Federal Home Loan Bank	**84,279**	103,943
Securities sold under agreements to repurchase	**26,019**	31,816
Subordinated debentures	**36,083**	36,083
Advance payments by borrowers	**2,925**	2,650
Other liabilities	**33,155**	28,459
Total liabilities	**2,620,117**	2,184,579
Commitments and Contingent Liabilities (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; 12,712,841 and 12,720,347 shares issued and 10,156,041 and 8,983,206 shares outstanding, respectively	**127**	127
Additional paid-in capital	**160,940**	126,390
Accumulated other comprehensive income, net of tax of $117 and $117, respectively	**217**	215
Retained earnings	**262,900**	240,592
Treasury stock, at cost, 2,556,800 and 3,737,141 shares respectively	**(50,898)**	(74,306)
Total stockholders' equity	**373,286**	293,018
Total liabilities and stockholders' equity	**$ 2,993,403**	$ 2,477,597

See accompanying notes

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

	Years Ended December 31		
	2017	**2016**	**2015**
Interest Income			
Loans	**$ 99,540**	$ 80,217	$ 73,346
Investment securities:			
Taxable	**3,762**	3,231	3,598
Tax-exempt	**3,180**	3,016	3,171
Interest-bearing deposits	**836**	367	169
FHLB stock dividends	**784**	552	552
Total interest income	**108,102**	87,383	80,836
Interest Expense			
Deposits	**8,818**	6,261	5,341
Federal Home Loan Bank advances and other	**1,470**	1,288	675
Subordinated debentures	**935**	753	613
Securities sold under agreement to repurchase	**208**	138	152
Total interest expense	**11,431**	8,440	6,781
Net interest income	**96,671**	78,943	74,055
Provision for loan losses	**2,949**	283	136
Net interest income after provision for loan losses	**93,722**	78,660	73,919
Noninterest Income			
Service fees and other charges	**12,139**	10,909	10,752
Mortgage banking income	**7,004**	7,270	6,713
Insurance commissions	**12,866**	10,441	10,076
Gain on sale of non-mortgage loans	**217**	753	824
Gain on sale or call of securities	**584**	509	22
Trust income	**2,332**	1,701	1,462
Income from bank owned life insurance	**3,085**	909	895
Other noninterest income	**1,854**	1,538	1,059
Total noninterest income	**40,081**	34,030	31,803
Noninterest Expense			
Compensation and benefits	**49,847**	40,187	37,769
Occupancy	**7,707**	7,418	7,197
FDIC insurance	**1,250**	1,169	1,324
Data processing	**7,737**	6,367	6,083
Other noninterest expense	**18,810**	15,952	15,516
Total noninterest expense	**85,351**	71,093	67,889
Income before income taxes	**48,452**	41,597	37,833
Federal income taxes	**16,184**	12,754	11,410
Net Income	**$ 32,268**	$ 28,843	$ 26,423
Earnings per common share (Note 4)			
Basic	**$ 3.23**	$ 3.21	$ 2.87
Diluted	**$ 3.22**	$ 3.19	$ 2.82
Dividends declared per common share	**$ 1.000**	$ 0.880	$ 0.775

See accompanying notes

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

	For the Years Ended December 31		
	2017	2016	2015
Net income	$32,268	$28,843	$26,423
Change in securities available-for-sale (AFS):			
Unrealized holding gains (losses) on available-for-sale securities arising during the period	732	(4,933)	(985)
Reclassification adjustment for (gains) losses realized in income	(584)	(509)	(22)
Net unrealized gains (losses)	148	(5,442)	(1,007)
Income tax effect	(51)	1,904	352
Net of tax amount	97	(3,538)	(655)
Change in unrealized gain/(loss) on postretirement benefit:			
Net gain (loss) on defined benefit postretirement medical plan realized during the period	(166)	172	204
Net amortization and deferral	20	30	47
Net gain (loss) activity during the period	(146)	202	251
Income tax effect	51	(71)	(88)
Net of tax amount	(95)	131	163
Total other comprehensive income (loss)	2	(3,407)	(492)
Comprehensive income	$32,270	$25,436	$25,931

See accompanying notes

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

	Preferred Stock	Common Stock Shares	Common Stock	Common Stock Warrant	Additional Paid-In Capital	Accumulated Other Comprehensive Income	Retained Earnings	Treasury Stock	Total Stockholder's Equity
Balance at January 1, 2015	$ -	9,234,534	$ 127	$ 878	$ 136,266	$ 4,114	$ 200,600	$ (62,480)	$ 279,505
Net income							26,423		26,423
Other comprehensive loss						(492)			(492)
Stock based compensation expenses					150				150
Warrant repurchase				(878)	(11,101)				(11,979)
Shares issued under stock option plan, net of 14,350 repurchased and retired		74,300			230		(313)	1,552	1,469
Restricted share activity under stock incentive plans		18,006			(58)		186	308	436
Excess tax benefit on stock compensation plans					216				216
Shares issued from direct stock sales		1,799			31			33	64
Shares repurchased		(225,808)						(8,436)	(8,436)
Common stock dividends declared							(7,159)		(7,159)
Balance at December 31, 2015	$ -	9,102,831	$ 127	$ -	$ 125,734	$ 3,622	$ 219,737	$ (69,023)	$ 280,197
Net income							28,843		28,843
Other comprehensive loss						(3,407)			(3,407)
Stock based compensation expenses					274				274
Shares issued under stock option plan, net of 1,612 repurchased and retired		36,358			(21)		(26)	761	714
Restricted share activity under stock incentive plans		10,405			370		(72)	219	517
Shares issued from direct stock sales		1,480			33			30	63
Shares repurchased		(167,868)						(6,293)	(6,293)
Common stock dividends declared							(7,890)		(7,890)
Balance at December 31, 2016	$ -	8,983,206	$ 127	$ -	$ 126,390	$ 215	$ 240,592	$ (74,306)	$ 293,018
Net income							**32,268**		**32,268**
Other comprehensive income						**2**			**2**
Stock based compensation expenses					**215**				**215**
Shares issued under stock option plan, net of 7,507 repurchased and retired		**4,044**			**51**		**(83)**	**231**	**199**
Capital stock issuance		**1,139,502**			**33,792**			**22,740**	**56,532**
Restricted share activity under stock incentive plans		**27,877**			**447**		**(18)**	**409**	**838**
Shares issued from direct stock sales		**1,412**			**45**			**28**	**73**
Common stock dividends declared							**(9,859)**		**(9,859)**
Balance at December 31, 2017	**$ -**	**10,156,041**	**$ 127**	**$ -**	**$ 160,940**	**$ 217**	**$ 262,900**	**$ (50,898)**	**$ 373,286**

See accompanying notes

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

	Years Ended December 31		
	2017	**2016**	**2015**
Operating Activities			
Net income	**$ 32,268**	$ 28,843	$ 26,423
Adjustments to reconcile net income to net cash provided by operating activities:			
Provision for loan losses	**2,949**	283	136
Provision for depreciation	**3,567**	3,356	3,267
Net amortization of premium and discounts on loans, securities, deposits and debt obligations	**740**	1,128	1,148
Amortization of mortgage servicing rights	**1,464**	1,724	1,620
Net impairment (recovery) of mortgage servicing rights	**(89)**	(123)	(266)
Amortization of intangibles	**1,289**	535	699
Gain on sale of loans	**(4,881)**	(6,064)	(5,388)
Loss on sale or disposals or write-downs of property, plant and equipment	**48**	-	428
(Gain) loss on sale or write-down of REO	**(56)**	(300)	150
(Gain) loss on sale or call of securities	**(584)**	(509)	(22)
Change in deferred taxes	**1,261**	(615)	(35)
Proceeds from sale of loans held for sale	**215,727**	262,958	215,402
Origination of loans held for sale	**(213,479)**	(263,679)	(213,416)
Stock based compensation expenses	**215**	274	150
Restricted stock unit expense	**838**	517	436
Excess tax benefit (expense) on stock compensation plans	**(171)**	(192)	216
Income from bank owned life insurance	**(3,085)**	(909)	(895)
Change in interest receivable and other assets	**(3,591)**	(4,121)	(1,356)
Change in accrued interest and other liabilities	**1,527**	3,878	1,955
Net cash provided by operating activities	**35,957**	26,984	30,652
Investing Activities			
Proceeds from maturities, calls and paydowns of held-to-maturity securities	**128**	59	69
Proceeds from maturities, calls and paydowns of available-for-sale securities	**32,687**	36,390	31,240
Proceeds from sale of available-for-sale securities	**34,248**	14,871	426
Proceeds from sale of REO	**554**	1,705	3,407
Proceeds from sale of office properties and equipment	**849**	1	212
Purchases of available-for-sale securities	**(73,007)**	(71,276)	(30,483)
Purchases of office properties and equipment	**(3,263)**	(2,106)	(1,843)
Investment in bank owned life insurance	**(20,000)**	-	(4,000)
Proceeds from FHLB stock redemption	**-**	3	1
Net cash received (paid) in acquisitions	**19,359**	-	(297)
Purchase of portfolio mortgage loans	**(11,476)**	(822)	-
Proceeds from sale of non-mortgage loans	**20,227**	20,816	24,027
Net increase in loans receivable	**(133,184)**	(158,121)	(177,013)
Net cash used in investing activities	**(132,878)**	(158,480)	(154,254)

Continued

FIRST DEFIANCE FINANCIAL CORP.

Consolidated Statements of Cash Flows (continued)
(Dollar Amounts in Thousands)

	Years Ended December 31		
	2017	**2016**	**2015**
Financing Activities			
Net increase in deposits and advance payments by borrowers	**148,065**	145,467	75,689
Repayment of Federal Home Loan Bank long-term advances	**(31,070)**	(959)	(8,642)
Proceeds from Federal Home Loan Bank long-term advances	**10,000**	45,000	47,000
Increase (decrease) in securities sold under repurchase agreements	**(5,797)**	(25,372)	2,429
Cash dividends paid on common stock	**(9,859)**	(7,890)	(7,159)
Net cash paid for repurchase of common stock	**-**	(6,293)	(8,436)
Repayment of warrants	**-**	-	(11,979)
Proceeds from exercise of stock options	**199**	714	1,469
Proceeds from direct treasury stock sales	**73**	63	64
Net cash provided by financing activities	**111,611**	150,730	90,435
Increase (decrease) in cash and cash equivalents	**14,690**	19,234	(33,167)
Cash and cash equivalents at beginning of period	**99,003**	79,769	112,936
Cash and cash equivalents at end of period	**$ 113,693**	$ 99,003	$ 79,769
Supplemental cash flow information:			
Interest paid	**$ 11,382**	$ 8,370	$ 6,764
Income taxes paid	**14,350**	12,700	10,000
Transfers from loans to other real estate owned and other assets held for sale	**705**	583	974
Transfer from real estate owned and other assets held for sale to loans	**-**	-	2,544
Transfer from (to) property and equipment to real estate and other assets held for sale	**(130)**	(44)	267
Sale of bank owned life insurance not yet settled	**17,840**	-	-
Securities traded but not yet settled	**548**	357	-

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 Archbold, Bowling Green, Bryan, Defiance, Findlay, Fostoria, Lima, Maumee, Oregon, and Tiffin, Ohio areas, offering property and casualty, and group health and life insurance products. The Maumee and Oregon offices were consolidated into a new office in Sylvania, Ohio in January 2018. 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. These estimates and assumptions affect the amounts reported in the financial statements and the disclosures provided, and actual results could differ.

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 includes the dilutive effect of additional potential common shares issuable under stock options, warrants, restricted stock awards and stock grants. See also Note 4.

Comprehensive Income

Comprehensive income consists of net income and other comprehensive income (loss). Other comprehensive income (loss) 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, 16 and 25 and the Consolidated 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. Cash and amounts due from depository institutions include required balances on hand or on deposit at the FHLB and Federal Reserve of approximately $1,322,000 and $1,325,000, respectively, at December 31, 2017, 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) other-than-temporary impairment ("OTTI") related to credit loss, which must be recognized in the income statement and (2) 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

First Federal is a member of the FHLB system. Members are required to own a certain amount of stock based on the level of borrowings and other factors, and may invest in additional amounts. FHLB stock is carried at cost, classified as a restricted security, and periodically evaluated for impairment based on ultimate recovery of par value. Both cash and stock dividends are reported as income. At December 31, 2017, the Company held $16.0 million at the FHLB of Cincinnati and $5,000 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, unamortized premiums and discounts, 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.

The Company may incur losses 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.

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.

Purchased Credit Impaired Loans

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. 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 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.

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.

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. An analysis of the net present value of estimated cash flows 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 Chief Credit Officer 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 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 Finance Loans: Consumer finance 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 Loans: 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 Loans: 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 Loans: 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 finance, 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 $3.7 million, $3.6 million and $3.5 million for the years ended December 31, 2017, 2016 and 2015. 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 for 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 non-controlling 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

Real estate and other assets held for sale are comprised of properties or other assets 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 shares 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, 2017, the reported revenue for First Insurance was 8.7% of total revenue for First Defiance. Total revenue includes interest income plus non-interest income. Net income for First Insurance for the year ended December 31, 2017 was 6.6% of consolidated net income. Total assets of First Insurance at December 31, 2017 were 0.8% 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. See Note 16 and 19.

Reclassifications

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

Accounting Standards Updates

In February 2018, the FASB issued Accounting Standard Update ("ASU") No. 2018-02, "Income Statement – Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income." The ASU required a reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the newly enacted federal corporate income tax rate as a result of the Tax Cuts and Jobs Act. The amount of the reclassification is the difference between the historical corporate income tax rate and the newly enacted twenty-one percent corporate income tax rate. The new guidance will be effective for the Company's year ending December 31, 2018 and early adoption is permitted. The Company chose not to early adopt the new standard for the year ending December 31, 2017, as allowed under the new standard.

In March 2017, the FASB issued ASU No. 2017-08, "Premium Amortization on Purchased Callable Debt Securities." This ASU shortens the amortization period for the premium on certain purchased callable debt securities to the earliest call date. Today, entities generally amortize the premium over the contractual life of the security. The new guidance does not change the accounting for purchased callable debt securities held at a discount; the discount continues to be amortized to maturity. ASU No. 2017-08 is effective for interim and annual reporting periods beginning after December 15, 2018; early adoption is permitted. The guidance calls for a modified retrospective transition approach under which a cumulative-effect adjustment will be made to retained earnings as of the beginning of the first reporting period in which the guidance is adopted. The Company adopted the provisions of ASU No. 2017-08 on January 1, 2018 and there was no material impact on the Company's Consolidated Financial Statements.

In January 2017, the FASB issued ASU No. 2017-04, "Simplifying the Test for Goodwill Impairment." The guidance removes Step 2 of the goodwill impairment test, which requires a hypothetical purchase price allocation. Goodwill impairment will now be the amount by which a reporting unit's carrying value exceeds its fair value, not to exceed the carrying amount of goodwill. All other goodwill impairment guidance will remain largely unchanged. ASU No. 2017-04 is effective for interim and annual reporting periods beginning after December 15, 2019, applied prospectively. Early adoption is permitted for any impairment tests performed after January 1, 2017. The Company early adopted ASU No. 2017-04 with its goodwill impairment test completed in 2017. ASU No. 2017-04 did not have a material impact on the Company's Consolidated Financial Statements.

In June 2016, the FASB issued ASU No. 2016-13, "Measurement of Credit Losses on Financial Instruments." This ASU significantly changes how entities will measure credit losses for most financial assets and certain other instruments that are not measured at fair value through net income. In issuing the standard, the FASB is responding to criticism that today's guidance delays recognition of credit losses. The standard will replace today's "incurred loss" approach with an "expected loss" model. The new model, referred to as the current expected credit loss ("CECL") model, will apply to: (1) financial assets subject to credit losses and measured at amortized cost, and (2) certain off-balance sheet credit exposures. This includes, but is not limited to, loans, leases, held-to-maturity securities, loan commitments, and financial guarantees. The CECL model does not apply to available-for-sale ("AFS") debt securities. For AFS debt securities with unrealized losses, entities will

measure credit losses in a manner similar to what they do today, except that the losses will be recognized as allowances rather than reductions in the amortized cost of the securities. As a result, entities will recognize improvements to estimated credit losses immediately in earnings rather than as interest income over time, as they do today. The ASU also simplifies the accounting model for purchased credit-impaired debt securities and loans. ASU 2016-13 also expands the disclosure requirements regarding an entity's assumptions, models, and methods for estimating the allowance for loan and lease losses. In addition, entities will need to disclose the amortized cost balance for each class of financial asset by credit quality indicator, disaggregated by the year of origination. ASU No. 2016-13 is effective for interim and annual reporting periods beginning after December 15, 2019; early adoption is permitted for interim and annual reporting periods beginning after December 15, 2018. Entities will apply the standard's provisions as a cumulative-effect adjustment to retained earnings as of the beginning of the first reporting period in which the guidance is effective (i.e., modified retrospective approach). The Company has begun its implementation efforts by establishing a Company-wide implementation committee. The committee's initial review indicates the Company has maintained sufficient historical loan data to support the requirement of this pronouncement and is currently evaluating the various loss methodologies to determine their correlations to the Company's loan segments historical performance. Early adoption is permitted, however, the Company does not currently plan to early adopt this ASU.

In February 2016, the FASB issued ASU No. 2016-02 — Leases (Topic 842). The objective of the update is to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. ASU No. 2016-02 will be effective for fiscal years beginning after December 15, 2018 and will require transition using a modified retrospective approach for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. In January 2018, FASB issued a proposal to provide an additional transition method that would allow entities to not apply the guidance in ASU No. 2016-02 in the comparative periods presented in the financial statements and instead recognize a cumulative-effect adjustment to the opening balance of retained earnings in the period of adoption. The Company has not yet selected a transition method as it is in the process of determining the effect of the ASU on its consolidated financial statements and disclosures. The Company has several lease agreements, such as branch locations, which are currently considered operating leases, and therefore, not recognized on the Company's consolidated condensed statements of financial condition. The Company expects the new guidance will require these lease agreements to now be recognized on the consolidated condensed statements of financial condition as a right-of-use asset and a corresponding lease liability. Therefore, the Company's preliminary evaluation indicates the provisions of ASU No. 2016-02 are expected to impact the Company's consolidated condensed statements of financial condition, along with our regulatory capital ratios. However, the Company continues to evaluate the extent of potential impact the new guidance will have on the Company's Consolidated Financial Statements. At December 31, 2017, the Company had contractual operating lease commitments of approximately $11.0 million, before considering renewal options that are generally present.

In January 2016, the FASB issued ASU No. 2016-01 — Financial Instruments — Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities. The amendments in this update address certain aspects of recognition, measurement, presentation, and disclosure of financial instruments. The ASU is effective for fiscal years and interim periods within those years beginning after December 15, 2017, and requires a cumulative-effect adjustment to the balance sheet as of the beginning of the fiscal year of adoption. Early adoption is not permitted. The Company is currently evaluating the impact of adopting the new guidance on the Consolidated Financial Statements. Management's preliminary finding is that the new pronouncement will not have a significant impact on its results of operations. The pronouncement will require some revision to the Company's disclosures within the Consolidated Financial Statements and is currently evaluating the impact.

In May 2014, the FASB and the International Accounting Standards Board (the "IASB") jointly issued a comprehensive new revenue recognition standard that will supersede nearly all existing revenue recognition guidance under GAAP and International Financial Reporting Standards ("IFRS"). Previous revenue recognition guidance in GAAP consisted of broad revenue recognition concepts together with numerous revenue requirements for particular industries or transactions, which sometimes resulted in different accounting for

economically similar transactions. In contrast, IFRS provided limited revenue recognition guidance and, consequently, could be difficult to apply to complex transactions. Accordingly, the FASB and the IASB initiated a joint project to clarify the principles for recognizing revenue and to develop a common revenue standard for U.S. GAAP and IFRS that would: (1) remove inconsistencies and weaknesses in revenue requirements; (2) provide a more robust framework for addressing revenue issues; (3) improve comparability of revenue recognition practices across entities, industries, jurisdictions, and capital markets; (4) provide more useful information to users of financial statements through improved disclosure requirements; and (5) simplify the preparation of financial statements by reducing the number of requirements to which an entity must refer. To meet those objectives, the FASB issued ASU No. 2014-09, "Revenue from Contracts with Customers." The standard's core principle is that a company will recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. In doing so, companies generally will be required to use more judgment and make more estimates than under current guidance. These may include identifying performance obligations in the contract, estimating the amount of variable consideration to include in the transaction price and allocating the transaction price to each separate performance obligation. The standard was initially effective for public entities for interim and annual reporting periods beginning after December 15, 2016; early adoption was not permitted. However, in August 2015, the FASB issued ASU No. 2015-14, "Revenue from Contracts with Customers - Deferral of the Effective Date" which deferred the effective date by one year (i.e., interim and annual reporting periods beginning after December 15, 2017). For financial reporting purposes, the standard allows for either full retrospective adoption, meaning the standard is applied to all of the periods presented, or modified retrospective adoption, meaning the standard is applied only to the most current period presented in the financial statements with the cumulative effect of initially applying the standard recognized at the date of initial application. In addition, the FASB has begun to issue targeted updates to clarify specific implementation issues of ASU 2014-09. These updates include ASU No. 2016-08, "Principal versus Agent Considerations (Reporting Revenue Gross versus Net)," ASU No. 2016-10, "Identifying Performance Obligations and Licensing," ASU No. 2016-12, "Narrow-Scope Improvements and Practical Expedients," and ASU No. 2016-20 "Technical Corrections and Improvements to Topic 606, Revenue from Contracts with Customers." The Company does not expect the new guidance to have a material impact on its financial statements as approximately 71% of the Company's revenue comes from net interest income and is explicitly out of scope of the guidance. Other out of scope revenue streams total approximately 10% of additional revenue. The primary contracts subject to the guidance include services charges and deposit related account fees, trust and asset management fees, insurance commissions, brokerage commissions, and interchange fees. The Company has concluded the adoption of the ASU will not have a material impact on the Company's revenue recognition patterns or financial presentation and disclosures. The new ASU is largely consistent with the existing guidance and current practices applied to the Company's revenue streams. The Company will adopt ASU No. 2014-09 in the first quarter of 2018 utilizing the modified retrospective approach and no adjustment was necessary to retained earnings.

3. Business Combinations

Effective February 24, 2017, the Company acquired Commercial Bancshares, Inc. ("Commercial Bancshares") and its subsidiary, The Commercial Savings Bank ("CSB"), pursuant to an Agreement and Plan of Merger ("merger agreement"), dated August 23, 2016. The acquisition was accomplished by the merger of Commercial Bancshares into First Defiance, immediately followed by the merger of CSB into First Defiance's banking subsidiary, First Federal. CSB operated 7 full-service banking offices in northwest and north central, Ohio and 1 commercial loan production office in central Ohio. Commercial Bancshares' consolidated assets and equity (unaudited) as of February 24, 2017 totaled $348.4 million and $37.5 million, respectively. The Company accounted for the transaction under the acquisition method of accounting which means that the acquired assets and liabilities were recorded at fair value at the date of acquisition. The fair value included in these financial statements is based on final valuations.

In accordance with ASC 805, the Company expensed approximately $3.7 million of direct acquisition costs, of which $2.8 million was to settle employment and benefit agreements and for personnel expenses related to operating

the new Commercial Bancshares locations. The Company recorded $28.9 million of goodwill and $4.9 million of intangible assets. Goodwill represents the future economic benefits arising from net assets acquired that are not individually identified and separately recognized and is attributable to synergies expected to be derived from the combination of the two entities. The acquisition was consistent with the Company's strategy to enhance and expand its presence in northwestern and north central Ohio. The acquisition offers the Company the opportunity to increase profitability by introducing existing products and services to the acquired customer base as well as add new customers in the expanded market area. The intangible assets are related to core deposits and are being amortized over 10 years on an accelerated basis. For tax purposes, goodwill totaling $28.9 million is non-deductible. Goodwill is evaluated annually for impairment. The following table summarizes the fair value of the total consideration transferred as part of the Commercial Bancshares acquisition as well as the fair value of identifiable assets and liabilities assumed as of the effective date of the transaction.

	February 24, 2017 (In Thousands)
Cash Consideration	**$ 12,340**
Equity – Dollar Value of Issued Shares	**56,532**
Fair Value of Total Consideration Transferred	**68,872**
Recognized Amounts of Identifiable Assets Acquired and Liabilities Assumed:	
Cash and Cash Equivalents	**35,411**
Federal Funds Sold	**2,769**
Securities	**4,338**
Loans	**285,448**
FHLB Stock of Cincinnati and Other Stock	**2,194**
Office Properties and Equipment	**5,256**
Intangible Assets	**4,900**
Bank-Owned Life Insurance	**8,168**
Accrued Interest Receivable and Other Assets	**3,606**
Deposits – Non-Interest Bearing	**(56,061)**
Deposits – Interest Bearing	**(251,931)**
Advances from FHLB	**(1,403)**
Accrued Interest Payable and Other Liabilities	**(2,717)**
Total Identifiable Net Assets	**39,978**
Goodwill	**$ 28,894**

Under the terms of the merger agreement, Commercial Bancshares common shareholders had the opportunity to elect to receive 1.1808 shares of common stock of the Company or cash in the amount of $51.00 for each share of Commercial Bancshares common stock, subject to adjustment as provided for in the merger agreement. Total consideration for Commercial Bancshares common shares outstanding was paid 80% in Company stock and 20% in cash. The Company issued 1,139,502 shares of its common stock and paid $12.3 million in cash to the former shareholders of Commercial Bancshares.

The following table presents unaudited pro forma information as if the acquisition had occurred on January 1, 2016 after giving effect to certain adjustments. The unaudited pro forma information for the twelve months ended December 31, 2017 and December 31, 2016 includes adjustments for interest income on loans and securities acquired, amortization of intangibles arising from the transaction, interest expense on deposits and borrowings acquired, and the related income tax effects. The unaudited pro forma financial information is not necessarily indicative of the results of operations that would have occurred had the transaction been effected on the assumed date.

	Pro Forma Twelve Months Ended December 31, 2017	Pro Forma Twelve Months Ended December 31, 2016
	(In Thousands)	
Net Interest Income	**$ 98,856**	$ 90,452
Provision for loan losses	**2,949**	753
Non-Interest Income	**40,338**	35,496
Non-Interest Expense	**82,597**	76,393
Income Before Income Taxes	**53,648**	48,802
Income Tax Expense	**17,780**	15,276
Net Income	**$ 35,868**	$ 33,526
Diluted Earnings Per Share	**$ 3.51**	$ 3.29

The above pro forma financial information includes approximately $4.6 million of net income related to the operations of Commercial Bancshares during the twelve months of 2017. The above pro forma financial information related to 2017 excludes merger related costs that totaled $3.7 million on a pre-tax basis.

On April 13, 2017, First Defiance and Corporate One Benefits Agency, Inc. ("Corporate One") jointly announced the acquisition of Corporate One's business by First Defiance. The total purchase price paid in cash was made up of the following: $6.5 million was paid at closing, $500,000 is due in July 2018, and $2.3 million at the end of a three-year earn-out based on the compound annual growth rate of net revenue over the performance period of Corporate One, for a total purchase price of $9.3 million. The recorded fair value of the $2.3 million earn-out was $1.8 million at December 31, 2017. As of December 31, 2017, total Company recorded goodwill of $7.9 million and identifiable intangible assets of $756,000 consisting of customer relationship intangible of $564,000 and a non-compete intangible of $192,000. The fair value included in these financial statements is based on final valuation. Corporate One was a full-service employee benefits consulting organization founded in 1996 with offices located in Archbold, Findlay, Fostoria and Tiffin, Ohio. Corporate One consulted employers to better manage their employee benefit programs to effectively lead them into the future. It is anticipated that the transaction will enhance employee benefit offerings and expand First Insurance's presence into adjacent markets in northwest Ohio.

4. Earnings Per Common Share

Basic earnings per share is calculated using the two-class method. The two-class method is an earnings allocation formula under which earnings per share is calculated from common stock and participating securities according to dividends declared and participation rights in undistributed earnings. Under this method, all earnings distributed and undistributed, are allocated to participating securities and common shares based on their respective rights to receive dividends. Unvested share-based payment awards that contain non-forfeitable rights to dividends are considered participating securities (i.e. unvested restricted stock), not subject to performance based measures.

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

	2017	2016	2015
	(In Thousands, Except Per Share Amounts)		
Basic Earnings Per Share:			
Net income available to common shareholders	**$ 32,268**	$ 28,843	$ 26,423
Less: Income allocated to participating securities	**5**	39	8
Net income allocated to common shareholders	**32,263**	28,804	26,415
Weighted average common shares outstanding Including participating securities	**9,975**	8,980	9,221
Less: Participating securities	**9**	11	11
Average common shares	**9,966**	8,969	9,210
Basic earnings per common share	**$ 3.23**	$ 3.21	$ 2.87
Diluted Earnings Per Share:			
Net income allocated to common shareholders	**$ 32,263**	$ 28,804	$ 26,415
Weighted average common shares outstanding for basic earnings per common share	**9,966**	8,969	9,210
Add: Dilutive effects of stock options	**62**	66	87
Add: Dilutive effects of warrants	**-**	-	75
Average shares and dilutive potential common shares	**10,028**	9,035	9,371
Diluted earnings per common share	**$3.22**	$ 3.19	$ 2.82

Shares subject to issue upon exercise of options of zero in 2017, 12,550 in 2016 and 8,750 in 2015 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 at December 31, 2017 and 2016 and the corresponding amounts of gross unrealized and unrecognized gains and losses:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(In Thousands)			
2017				
Available-for-sale				
Obligations of U.S. government corporations and agencies	**$ 518**	**$ -**	**$ (10)**	**$ 508**
Mortgage-backed securities - residential	**59,942**	**90**	**(763)**	**59,269**
REMICs	**1,072**	**-**	**(7)**	**1,065**
Collateralized mortgage obligations	**94,588**	**180**	**(892)**	**93,876**
Preferred stock	**-**	**1**	**-**	**1**
Corporate bonds	**12,914**	**189**	**-**	**13,103**
Obligations of state and political subdivisions	**90,692**	**2,426**	**(290)**	**92,828**
Total Available-for-Sale	**$ 259,726**	**$ 2,886**	**$ (1,962)**	**$ 260,650**

	Amortized Cost	**Gross Unrecognized Gains**	**Gross Unrecognized Losses**	**Fair Value**
	(In Thousands)			
Held-to-Maturity				
FHLMC certificates	**$ 10**	**$ -**	**$ -**	**$ 10**
FNMA certificates	**41**	**1**	**-**	**42**
GNMA certificates	**17**	**-**	**-**	**17**
Obligations of states and political subdivisions	**580**	**-**	**-**	**580**
Total Held-to-Maturity	**$ 648**	**$ 1**	**$ -**	**$ 649**

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(In Thousands)			
2016				
Available-for-sale				
Obligations of U.S. government corporations and agencies	$ 4,000	$ -	$ (85)	$ 3,915
Mortgage-backed securities - residential	82,619	390	(1,302)	81,707
REMICs	1,309	-	(2)	1,307
Collateralized mortgage obligations	63,204	422	(621)	63,005
Preferred stock	-	2	-	2
Corporate bonds	12,919	97	(3)	13,013
Obligations of state and political subdivisions	86,165	2,491	(613)	88,043
Total Available-for-Sale	$ 250,216	$ 3,402	$ (2,626)	$ 250,992

	Amortized Cost	Gross Unrecognized Gains	Gross Unrecognized Losses	Fair Value
	(In Thousands)			
Held-to-Maturity				
FHLMC certificates	$ 12	$ -	$ -	$ 12
FNMA certificates	56	2	-	58
GNMA certificates	23	1	-	24
Obligations of states and political subdivisions	93	-	-	93
Total Held-to-Maturity	$ 184	$ 3	$ -	$ 187

The amortized cost and fair value of the investment securities portfolio at December 31, 2017, is 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	Fair Value
	(In Thousands)	
2017		
Available-for-sale		
Due in one year or less	**$ 1,423**	**$ 1,440**
Due after one year through five years	**19,898**	**20,303**
Due after five years through ten years	**39,344**	**40,710**
Due after ten years	**43,459**	**43,987**
MBS/CMO/REMIC	**155,602**	**154,210**
Total	**$ 259,726**	**$ 260,650**
Held-to-maturity		
Due after one year through five years	**$ 62**	**$ 62**
Due after five years through ten years	**518**	**518**
MBS	**68**	**69**
Total	**$ 648**	**$ 649**

Securities pledged at year-end 2017 and 2016 had a carrying amount of $135.4 million and $143.6 million and were pledged to secure public deposits, securities sold under repurchase agreements and FHLB advances.

As of December 31, 2017, the Company's investment portfolio consisted of 413 securities, 121 of which were in an unrealized loss position. The Company did not hold any single security that was greater than 10% of the Company's equity at December 31, 2017.

The following table summarizes First Defiance's securities that were in an unrealized loss position at December 31, 2017, and December 31, 2016:

	Duration of Unrealized Loss Position					
	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	Gross Unrealized Loss	Fair Value	Gross Unrealized Loss	Fair Value	Unrealized Loses
	(In Thousands)					
At December 31, 2017						
Available-for-sale securities:						
Obligations of U.S. government corporations and agencies	**$ -**	**$ -**	**$ 508**	**$ (10)**	**$ 508**	**$ (10)**
Mortgage-backed securities-residential	**27,881**	**(215)**	**19,038**	**(548)**	**46,919**	**(763)**
REMIC's	**1,065**	**(7)**	**-**	**-**	**1,065**	**(7)**
Collateralized mortgage obligations	**49,107**	**(320)**	**20,804**	**(572)**	**69,911**	**(892)**
Obligations of state and political subdivisions	**14,249**	**(163)**	**3,370**	**(127)**	**17,619**	**(290)**
Held to maturity securities:	**12**	**-**	**9**	**-**	**21**	**-**
Total temporarily impaired securities	**$ 92,314**	**$ (705)**	**$ 43,729**	**$ (1,257)**	**$ 136,043**	**$ (1,962)**
At December 31, 2016						
Available-for-sale securities:						
Obligations of U.S. government corporations and agencies	$ 3,915	$ (85)	$ -	$ -	$ 3,915	$ (85)
Mortgage-backed securities-residential	63,736	(1,302)	-	-	63,736	(1,302)
REMIC's	1,308	(2)	-	-	1,308	(2)
Collateralized mortgage obligations	28,882	(566)	1,227	(55)	30,110	(621)
Corporate bonds	-	-	997	(3)	997	(3)
Obligations of state and political subdivisions	19,172	(613)	-	-	19,172	(613)
Total temporarily impaired securities	$ 117,013	$ (2,568)	$ 2,224	$ (58)	$119,238	$ (2,626)

Management evaluates securities for OTTI on at least a quarterly basis, and more frequently 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.

With the exception of corporate bonds, the 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.

In 2017, 2016 and 2015, management determined there was no OTTI.

There were no credit losses relating to debt securities recognized in earnings for the years ended December 31, 2017, 2016 and 2015.

Realized gains from the sales and calls of investment securities totaled $584,000 ($380,000 after tax) in 2017 while there were realized gains of $509,000 ($331,000 after tax) and $22,000 ($15,000 after tax) in 2016 and 2015, respectively.

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

	2017	2016	2015
		(In Thousands)	
Proceeds	**$ 34,248**	$ 14,871	$ 426
Gross realized gains	**665**	509	22
Gross realized losses	**(81)**	-	-

6. Commitments and Contingent Liabilities

Loan Commitments

Loan commitments are made to accommodate the financial needs of First Federal's customers. 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):

	2017		2016	
	Fixed Rate	**Variable Rate**	Fixed Rate	Variable Rate
Commitments to make loans	**$ 42,458**	**$ 161,778**	$ 34,432	$ 106,356
Unused lines of credit	**6,245**	**408,831**	14,384	400,542
Standby letters of credit	**-**	**7,605**	-	9,668
Total	**$ 48,703**	**$ 578,214**	$ 48,816	$ 516,566

Commitments to make loans are generally made for periods of 60 days or less. The fixed rate loan commitments at December 31, 2017, had interest rates ranging from 1.99% to 18.00% and maturities ranging from less than 1 year to 30 years.

In addition to the above commitments, at December 31, 2017, First Defiance had commitments to sell $14.9 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, 2017	December 31, 2016
	(In Thousands)	
Real Estate:		
Secured by 1-4 family residential	**$ 274,862**	$ 207,550
Secured by multi-family residential	**248,092**	196,983
Secured by commercial real estate	**987,129**	843,579
Construction	**265,476**	182,886
	1,775,559	1,430,998
Other Loans:		
Commercial	**526,142**	469,055
Home equity and improvement	**135,457**	118,429
Consumer Finance	**29,109**	16,680
	690,708	604,164
Total loans	**2,466,267**	2,035,162
Deduct:		
Undisbursed loan funds	**(115,972)**	(93,355)
Net deferred loan origination fees and costs	**(1,582)**	(1,320)
Allowance for loan loss	**(26,683)**	(25,884)
Totals	**$ 2,322,030**	$ 1,914,603

The table above includes loans acquired during 2017 totaling $285.4 million as of February 24, 2017, which is net of purchase discount on the acquired loans of $5.4 million. The recorded investment of these loans as of December 31, 2017 was $208.4 million, net of the purchase discount of $3.9 million.

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

The following table discloses the year-to-date activity in the allowance for loan loss for the dates indicated by portfolio segment (In Thousands):

Year to Date December 31, 2017	1-4 Family Residential Real Estate	Multi- Family Residential Real Estate	Commercial Real Estate	Construction	Commercial	Home Equity and Improvement	Consumer Finance	Total
Beginning Allowance	$ 2,627	$ 2,228	$ 10,625	$ 450	$ 7,361	$ 2,386	$ 207	$ 25,884
Charge-Offs	(279)	-	(429)	-	(2,301)	(301)	(139)	(3,449)
Recoveries	115	32	657	-	243	167	85	1,299
Provisions	69	442	(499)	197	2,662	3	75	2,949
Ending Allowance	$ 2,532	$ 2,702	$ 10,354	$ 647	$ 7,965	$ 2,255	$ 228	$ 26,683

Year to Date December 31, 2016	1-4 Family Residential Real Estate	Multi- Family Residential Real Estate	Commercial Real Estate	Construction	Commercial	Home Equity and Improvement	Consumer Finance	Total
Beginning Allowance	$ 3,212	$ 2,151	$ 11,772	$ 517	$ 5,255	$ 2,304	$ 171	$ 25,382
Charge-Offs	(350)	-	(92)	-	(615)	(268)	(94)	(1,419)
Recoveries	166	-	923	-	335	150	64	1,638
Provisions	(401)	77	(1,978)	(67)	2,386	200	66	283
Ending Allowance	$ 2,627	$ 2,228	$ 10,625	$ 450	$ 7,361	$ 2,386	$ 207	$ 25,884

Year to Date December 31, 2015	1-4 Family Residential Real Estate	Multi- Family Residential Real Estate	Commercial Real Estate	Construction	Commercial	Home Equity and Improvement	Consumer Finance	Total
Beginning Allowance	$ 2,494	$ 2,453	$ 11,268	$ 221	$ 6,509	$ 1,704	$ 117	$ 24,766
Charge-Offs	(283)	(114)	(353)	-	(68)	(350)	(53)	(1,221)
Recoveries	214	-	915	-	331	188	53	1,701
Provisions	787	(188)	(58)	296	(1,517)	762	54	136
Ending Allowance	$ 3,212	$ 2,151	$ 11,772	$ 517	$ 5,255	$ 2,304	$ 171	$ 25,382

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, 2017: (In Thousands)

	1-4 Family Residential Real Estate	Multi Family Residential Real Estate	Commercial Real Estate	Construction	Commercial	Home Equity & Improvement	Consumer Finance	Total
Allowance for loan losses:								
Ending allowance balance attributable to loans:								
Individually evaluated for impairment	$ 167	$ 7	$ 118	$ -	$ 187	$ 279	$ -	$ 758
Collectively evaluated for impairment	2,365	2,695	10,236	647	7,778	1,976	228	25,925
Acquired with deteriorated credit quality	-	-	-	-	-	-	-	-
Total ending allowance balance	$ 2,532	$ 2,702	$ 10,354	$ 647	$ 7,965	$ 2,255	$ 228	$ 26,683
Loans:								
Loans individually evaluated for impairment	$ 6,910	$ 2,278	$ 31,821	$ -	$ 14,373	$ 1,176	$ 50	$ 56,608
Loans collectively evaluated for impairment	267,377	245,823	956,238	149,174	513,218	135,098	29,125	2,296,053
Loans acquired with deteriorated credit quality	1,069	301	2,121	-	337	-	-	3,828
Total ending loans balance	$ 275,356	$ 248,402	$ 990,180	$ 149,174	$ 527,928	$ 136,274	$ 29,175	$ 2,356,489

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, 2016: (In Thousands)

	1-4 Family Residential Real Estate	Multi Family Residential Real Estate	Commercial Real Estate	Construction	Commercial	Home Equity & Improvement	Consumer Finance	Total
Allowance for loan losses:								
Ending allowance balance attributable to loans:								
Individually evaluated for impairment	$ 202	$ 4	$ 255	$ -	$ 35	$ 313	$ -	$ 809
Collectively evaluated for impairment	2,425	2,224	10,370	450	7,326	2,073	207	25,075
Acquired with deteriorated credit quality	-	-	-	-	-	-	-	-
Total ending allowance balance	$ 2,627	$ 2,228	$ 10,625	$ 450	$ 7,361	$ 2,386	$ 207	$ 25,884
Loans:								
Loans individually evaluated for impairment	$ 6,898	$ 3,483	$ 13,570	$ -	$ 2,154	$ 1,269	$ 59	$ 27,433
Loans collectively evaluated for impairment	200,907	193,714	832,446	89,244	468,246	117,744	16,625	1,918,926
Loans acquired with deteriorated credit quality	-	-	-	-	11	-	-	11
Total ending loans balance	$ 207,805	$ 197,197	$ 846,016	$ 89,244	$ 470,411	$ 119,013	$ 16,684	$ 1,946,370

The following tables presents the average balance, interest income recognized and cash basis income recognized on impaired loans by class of loans for the years ended December 31, 2017, 2016 and 2015 (In Thousands):

	Twelve Months Ended December 31, 2017		
	Average Balance	Interest Income Recognized	Cash Basis Income Recognized
Residential Owner Occupied	$ 3,811	$ 138	$ 138
Residential Non Owner Occupied	3,038	138	138
Total 1-4 Family Residential Real Estate	**6,849**	**276**	**276**
Multi-Family Residential Real Estate	**2,471**	**58**	**58**
CRE Owner Occupied	10,592	110	109
CRE Non Owner Occupied	3,768	140	133
Agriculture Land	9,667	472	229
Other CRE	1,603	76	70
Total Commercial Real Estate	**25,630**	**798**	**541**
Construction	**-**	**-**	**-**
Commercial Working Capital	5,235	129	123
Commercial Other	5,940	109	79
Total Commercial	**11,175**	**238**	**202**
Home Equity and Home Improvement	**1,217**	**43**	**43**
Consumer Finance	**59**	**4**	**4**
Total Impaired Loans	**$ 47,401**	**$ 1,417**	**$1,124**

	Twelve Months Ended December 31, 2016		
	Average Balance	Interest Income Recognized	Cash Basis Income Recognized
Residential Owner Occupied	$ 3,954	$ 244	$ 237
Residential Non Owner Occupied	3,133	211	210
Total 1-4 Family Residential Real Estate	**7,087**	**455**	**447**
Multi-Family Residential Real Estate	**3,946**	**124**	**123**
CRE Owner Occupied	6,925	203	183
CRE Non Owner Occupied	5,351	411	407
Agriculture Land	2,283	128	68
Other CRE	1,632	71	70
Total Commercial Real Estate	**16,191**	**813**	**728**
Construction	**-**	**-**	**-**
Commercial Working Capital	1,606	109	90
Commercial Other	2,393	81	79
Total Commercial	**3,999**	**190**	**169**
Home Equity and Home Improvement	**1,543**	**85**	**83**
Consumer Finance	**67**	**8**	**8**
Total Impaired Loans	**$ 32,833**	**$ 1,675**	**$1,558**

	Twelve Months Ended December 31, 2015		
	Average Balance	Interest Income Recognized	Cash Basis Income Recognized
Residential Owner Occupied	$ 6,985	$ 246	$ 244
Residential Non Owner Occupied	5,444	152	152
Total 1-4 Family Residential Real Estate	**12,429**	**398**	**396**
Multi-Family Residential Real Estate	**3,799**	**40**	**40**
CRE Owner Occupied	9,019	168	167
CRE Non Owner Occupied	10,125	349	348
Agriculture Land	2,980	88	56
Other CRE	3,554	81	80
Total Commercial Real Estate	**25,678**	**686**	**651**
Construction	**50**	**2**	**2**
Commercial Working Capital	2,217	58	56
Commercial Other	4,773	49	49
Total Commercial	**6,990**	**107**	**115**
Home Equity and Home Improvement	**2,757**	**62**	**62**
Consumer Finance	**80**	**14**	**14**
Total Impaired Loans	**$ 51,783**	**$ 1,309**	**$1,270**

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

	December 31, 2017			December 31, 2016		
	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	$ 2,507	$ 2,364	$ -	$ 1,912	$ 1,765	$ -
Residential Non Owner Occupied	1,711	1,708	-	1,691	1,683	-
Total 1-4 Family Residential Real Estate	**4,218**	**4,072**	**-**	**3,603**	**3,448**	**-**
Multi-Family Residential Real Estate	**2,095**	**2,102**	**-**	**3,578**	**3,430**	**-**
CRE Owner Occupied	12,273	11,804	-	2,652	2,353	-
CRE Non Owner Occupied	3,085	2,925	-	4,372	4,240	-
Agriculture Land	13,029	13,185	-	1,695	1,722	-
Other CRE	981	768	-	1,225	1,115	-
Total Commercial Real Estate	**29,368**	**28,682**	**-**	**9,944**	**9,430**	**-**
Construction	**-**	-	-	-	-	-
Commercial Working Capital	5,462	5,422	-	838	786	-
Commercial Other	9,916	7,644	-	1,179	967	-
Total Commercial	**15,378**	**13,066**	**-**	**2,017**	**1,753**	**-**
Home Equity and Home Improvement	**630**	**584**	**-**	**631**	**585**	**-**
Consumer Finance	**42**	**42**	**-**	**55**	**55**	**-**
Total loans with no allowance recorded	**$ 51,731**	**$ 48,548**	**$ -**	**$ 19,828**	**$ 18,701**	**$ -**
With an allowance recorded:						
Residential Owner Occupied	$ 1,841	$ 1,814	$ 137	$ 2,348	$ 2,319	$ 157
Residential Non Owner Occupied	1,031	1,024	30	1,137	1,131	45
Total 1-4 Family Residential Real Estate	**2,872**	**2,838**	**167**	**3,485**	**3,450**	**202**
Multi-Family Residential Real Estate	**175**	**176**	**7**	**53**	**53**	**4**
CRE Owner Occupied	2,007	1,546	44	2,362	1,894	102
CRE Non Owner Occupied	651	593	28	1,618	1,479	108
Agriculture Land	293	292	14	45	45	3
Other CRE	909	708	32	1,144	722	42
Total Commercial Real Estate	**3,860**	**3,139**	**118**	**5,169**	**4,140**	**255**
Construction	**-**	-	-	-	-	-
Commercial Working Capital	447	449	77	230	231	24
Commercial Other	854	858	110	167	170	11
Total Commercial	**1,301**	**1,307**	**187**	**397**	**401**	**35**
Home Equity and Home Improvement	**596**	**592**	**279**	**688**	**684**	**313**
Consumer Finance	**8**	**8**	**-**	**4**	**4**	**-**
Total loans with an allowance recorded	**$ 8,812**	**$ 8,060**	**$ 758**	**$ 9,796**	**$ 8,732**	**$ 809**

* Presented gross of charge offs

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, 2017	December 31, 2016
	(In Thousands)	
Non-accrual loans	**$ 30,715**	$ 14,348
Loans over 90 days past due and still accruing	**-**	-
Total non-performing loans	**30,715**	14,348
Real estate and other assets held for sale	**1,532**	455
Total non-performing assets	**$ 32,247**	$ 14,803
Troubled debt restructuring, still accruing	**$ 13,770**	**$ 10,544**

The following table presents the aging of the recorded investment in past due and non-accrual loans as of December 31, 2017, by class of loans (In Thousands):

	Current	**30-59 days**	**60-89 days**	**90+ days**	**Total Past Due**	**Total Non Accrual**
Residential Owner Occupied	$ 175,139	$ 821	$ 1,033	$ 1,227	$ 3,081	$ 2,510
Residential Non Owner Occupied	96,400	495	8	233	736	520
Total 1-4 Family Residential Real Estate	**271,539**	**1,316**	**1,041**	**1,460**	**3,817**	**3,030**
Multi-Family Residential Real Estate	**247,980**	**422**	**-**	**-**	**422**	**128**
CRE Owner Occupied	393,125	195	188	1,268	1,651	10,775
CRE Non Owner Occupied	403,656	1	91	424	516	2,431
Agriculture Land	131,753	412	-	66	478	4,144
Other Commercial Real Estate	58,784	13	-	204	217	734
Total Commercial Real Estate	**987,318**	**621**	**279**	**1,962**	**2,862**	**18,084**
Construction	**149,174**	**-**	**-**	**-**	**-**	**-**
Commercial Working Capital	233,632	102	1,264	876	2,242	2,369
Commercial Other	291,455	82	-	517	599	6,474
Total Commercial	**525,087**	**184**	**1,264**	**1,393**	**2,841**	**8,843**
Home Equity and Home Improvement	**133,144**	**2,490**	**434**	**206**	**3,130**	**591**
Consumer Finance	**28,800**	**293**	**80**	**2**	**375**	**27**
Total Loans	**$ 2,343,042**	**$ 5,326**	**$ 3,098**	**$ 5,023**	**$ 13,447**	**$ 30,703**

Loans acquired with deteriorated credit quality (included in the totals above)	$3,662	$15	$40	$111	$166	$1,904
Loans acquired in current year (included in totals above)	$203,562	$1,881	$1,357	$1,569	$4,807	$5,309

The following table presents the aging of the recorded investment in past due and non-accrual loans as of December 31, 2016 by class of loans: (In Thousands)

	Current	30-59 days	60-89 days	90+ days	Total Past Due	Total Non Accrual
Residential Owner Occupied	$ 139,015	$ 56	$ 842	$ 544	$ 1,442	$ 1,931
Residential Non Owner Occupied	66,811	166	308	63	537	992
Total 1-4 Family Residential Real Estate	**205,826**	**222**	**1,150**	**607**	**1,979**	**2,923**
Multi-Family Residential Real Estate	**197,197**	**-**	**-**	**-**	**-**	**2,637**
CRE Owner Occupied	340,233	79	-	1,396	1,475	3,098
CRE Non Owner Occupied	338,724	81	16	426	523	1,808
Agriculture Land	102,397	-	-	-	-	755
Other Commercial Real Estate	62,415	-	-	249	249	1,292
Total Commercial Real Estate	**843,769**	**160**	**16**	**2,071**	**2,247**	**6,953**
Construction	**89,244**	**-**	**-**	**-**	**-**	**-**
Commercial Working Capital	202,786	-	10	38	48	435
Commercial Other	267,189	23	-	365	388	577
Total Commercial	**469,975**	**23**	**10**	**403**	**436**	**1,012**
Home Equity and Home Improvement	**117,458**	**1,125**	**176**	**254**	**1,555**	**730**
Consumer Finance	**16,452**	**85**	**69**	**78**	**232**	**91**
Total Loans	**$ 1,939,921**	**$ 1,615**	**$ 1,421**	**$ 3,413**	**$ 6,449**	**$ 14,346**

Troubled Debt Restructurings

As of December 31, 2017 and 2016, the Company had a recorded investment in troubled debt restructurings ("TDRs") of $21.7 million and $16.8 million, respectively. The Company allocated $751,000 and $809,000, of specific reserves to those loans at December 31, 2017 and 2016, and committed to lend additional amounts totaling up to $242,000 and $20,000 at December 31, 2017 and 2016.

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.

Of the loans modified in a TDR, $7.8 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 indicated (Dollars in Thousands):

	Loans Modified as a TDR for the Twelve Months Ended December 31, 2017		**Loans Modified as a TDR for the Twelve Months Ended December 31, 2016**		**Loans Modified as a TDR for the Twelve Months Ended December 31, 2015**	
TDRs	**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	24	$ 982	17	$ 778	6	$ 454
Residential Non Owner Occupied	5	193	5	494	4	59
Multi Family	-	-	2	1,885	-	-
CRE Owner Occupied	2	149	-	-	2	645
CRE Non Owner Occupied	1	262	5	974	2	244
Agriculture Land	5	1,700	1	45	3	1,443
Other CRE	2	153	1	348	-	-
Commercial Working Capital	7	1,475	1	226	2	62
Commercial Other	7	3,833	1	587	2	70
Home Equity and Home Improvement	6	152	9	281	13	324
Consumer Finance	5	14	2	14	9	62
Total	**64**	**$ 8,913**	**44**	**$ 5,632**	**43**	**$ 3,363**

The loans described above increased the allowance for loan losses ("ALLL") by $104,000 for the year ended December 31, 2017, decreased the ALLL by $413,000 for the year ended December 31, 2016, and increased the ALLL by $13,000 for the year ended December 31, 2015.

Of the 2017 modifications, 18 were made TDRs due to the fact that the borrower is in bankruptcy, 8 were made TDR due to terming out lines of credit at below market terms, 14 were made TDR due to advancing or renewing money to a watch list credit, 7 loans were placed under a forbearance agreement, and 18 were made a TDR because the current debt was refinanced due to maturity or for payment relief.

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 indicated:

TDRs That Subsequently Defaulted:	Twelve Months Ended December 31, 2017 ($ in thousands)		Twelve Months Ended December 31, 2016 ($ in thousands)		Twelve Months Ended December 31, 2015 ($ 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	-	$ -	-	$ -	-	$ -
Residential Non Owner Occupied	-	-	-	-	-	-
CRE Owner Occupied	-	-	-	-	-	-
CRE Non Owner Occupied	-	-	1	205	-	-
Agriculture Land	-	-	-	-	-	-
Other CRE	-	-	-	-	-	-
Commercial Working Capital	-	-	-	-	1	120
Commercial Other	-	-	-	-	5	1,791
Home Equity and Home Improvement	-	-	-	-	1	22
Consumer	-	-	-	-	-	-
Total	**-**	**$ -**	**1**	**$ 205**	**7**	**$ 1,933**

The TDRs that subsequently defaulted described above had no effect on the ALLL for the years ended December 31, 2017, 2016 and 2015.

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.

In order to determine whether a borrower is experiencing financial difficulty, an evaluation is performed regarding 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.

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, 2017, 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
Residential Owner Occupied	$ 7,534	$ 99	$ 2,367	$ -	$ 168,220	$ 178,220
Residential Non Owner Occupied	85,802	935	3,835	-	6,564	97,136
Total 1-4 Family Real Estate	**93,336**	**1,034**	**6,202**	**-**	**174,784**	**275,356**
Multi-Family Residential Real Estate	**242,969**	**2,503**	**2,819**	**-**	**111**	**248,402**
CRE Owner Occupied	370,613	10,432	13,575	-	156	394,776
CRE Non Owner Occupied	395,264	3,464	5,444	-	-	404,172
Agriculture Land	114,776	2,639	14,816	-	-	132,231
Other CRE	56,133	165	1,788	-	915	59,001
Total Commercial Real Estate	**936,786**	**16,700**	**35,623**	**-**	**1,071**	**990,180**
Construction	**125,519**	**1,254**	**-**	**-**	**22,401**	**149,174**
Commercial Working Capital	222,526	7,605	5,743	-	-	235,874
Commercial Other	280,013	3,443	8,598	-	-	292,054
Total Commercial	**502,539**	**11,048**	**14,341**	**-**	**-**	**527,928**
Home Equity and Home Improvement	**-**	**-**	**600**	**-**	**135,674**	**136,274**
Consumer Finance	**-**	**-**	**82**	**-**	**29,093**	**29,175**
Total Loans	**$ 1,901,149**	**$ 32,539**	**$ 59,667**	**$ -**	**$ 363,134**	**$ 2,356,489**

Loans acquired with deteriorated credit quality (included in the totals above)	$41	$-	$3,783	-	$4	$3,828
Loans acquired in current year (included in totals above)	$148,364	$3,502	$16,085	-	$40,418	$208,369

As of December 31, 2016, 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
Residential Owner Occupied	$ 5,980	$ 402	$ 1,824	$ -	$ 132,250	$ 140,456
Residential Non Owner Occupied	58,041	1,394	3,480	-	4,434	67,349
Total 1-4 Family Real Estate	**64,021**	**1,796**	**5,304**	**-**	**136,684**	**207,805**
Multi-Family Residential Real Estate	**192,369**	**862**	**3,852**	**-**	**114**	**197,197**
CRE Owner Occupied	316,335	20,559	4,430	-	384	341,708
CRE Non Owner Occupied	332,196	1,617	5,435	-	-	339,248
Agriculture Land	98,039	2,355	2,002	-	-	102,396
Other CRE	59,561	60	2,297	-	746	62,664
Total Commercial Real Estate	**806,131**	**24,591**	**14,164**	**-**	**1,130**	**846,016**
Construction	**67,751**	**706**	**-**	**-**	**20,787**	**89,244**
Commercial Working Capital	193,043	8,301	1,490	-	-	202,834
Commercial Other	262,076	3,749	1,752	-	-	267,577
Total Commercial	**455,119**	**12,050**	**3,242**	**-**	**-**	**470,411**
Home Equity and Home Improvement	**-**	**-**	**696**	**-**	**118,317**	**119,013**
Consumer Finance	**-**	**-**	**90**	**-**	**16,594**	**16,684**
Total Loans	**$ 1,585,391**	**$ 40,005**	**$ 27,348**	**$ -**	**$ 293,626**	**$ 1,946,370**

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 have been recorded based on management's estimate of the fair value of the loans. The outstanding balance of those loans by segment is as follows (In thousands):

	December 31, 2017
1-4 Family Residential Real Estate	$ 1,154
Multi-Family Residential Real Estate	309
Commercial Real Estate Loans	2,921
Commercial	407
Consumer	2
Total Outstanding Balance	$4,793
Recorded Investment, net of allowance of $0	$ 3,828

Accretable yield, or income expected to be collected, is as follows:

		2017
Balance at January 1, 2017	$	-
New Loans Purchased		1,018
Accretion of Income		(204)
Reclassifications from Non-accretable		-
Charge-off of Accretable Yield		(10)
Balance at December 31, 2017	$	804

For those purchased loans disclosed above, the Company did not increase the allowance for loan losses during the twelve months ended December 31, 2017. No allowances for loan losses were reversed during the same period.

Contractually required payments receivable of loans purchased with evidence of credit deterioration during the period ended December 31, 2017, using information as of the date of acquisition are included in the table below. There were no such loans purchased during the year ended December 31, 2016. (In Thousands)

1-4 Family Residential Real Estate	$1,720
Commercial Real Estate	4,724
Commercial	785
Consumer	4
Total	$ 7,233

Cash Flows Expected to be Collected at Acquisition $ 5,721

Fair Value of Acquired Loans at Acquisition $ 4,703

Loans purchased with evidence of deterioration of credit quality acquired prior to 2017 were $169,000 and $11,000 at December 31, 2016 and 2015, respectively and were paid off during 2017.

Loans to executive officers, directors, and their affiliates are as follows:

	Years Ended December 31	
	2017	2016
	(In Thousands)	
Beginning balance	**$ 16,199**	$ 7,349
New loans	**5,857**	4,783
Effect of changes in composition of related parties	**-**	12,320
Repayments	**(5,328)**	(8,253)
Ending Balance	**$ 16,728**	$ 16,199

Foreclosure Proceedings

Consumer mortgage loans collateralized by residential real estate property that are in the process of foreclosure totaled $626,000 as of December 31, 2017.

8. Mortgage Banking

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

	Years Ended December 31		
	2017	**2016**	**2015**
	(In Thousands)		
Gain from sale of mortgage loans	**$ 4,664**	$ 5,311	$ 4,564
Mortgage loan servicing revenue (expense):			
Mortgage loan servicing revenue	**3,714**	3,560	3,503
Amortization of mortgage servicing rights	**(1,464)**	(1,724)	(1,620)
Mortgage servicing rights valuation adjustments	**90**	123	266
	2,340	1,959	2,149
Net mortgage banking income	**$ 7,004**	$ 7,270	$ 6,713

The unpaid principal balance of residential mortgage loans serviced for third parties was $1.39 billion at December 31, 2017, and $1.37 billion at December 31, 2016.

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

	Years Ended December 31		
	2017	**2016**	**2015**
	(In Thousands)		
Mortgage servicing assets:			
Balance at beginning of period	**$ 10,117**	$ 9,893	$ 9,923
Loans sold, servicing retained	**1,587**	1,948	1,590
Amortization	**(1,464)**	(1,724)	(1,620)
Carrying value before valuation allowance at end of period	**10,240**	10,117	9,893
Valuation allowance:			
Balance at beginning of period	**(522)**	(645)	(911)
Impairment recovery (charges)	**90**	123	266
Balance at end of period	**(432)**	(522)	(645)
Net carrying value of MSRs at end of period	**$ 9,808**	$ 9,595	$ 9,248
Fair value of MSRs at end of period	**$ 9,930**	$ 9,770	$ 9,802

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

The Company had no actual losses from secondary market buy-backs in 2017, 2016 or 2015. Based on management's estimate of potential losses from secondary market buyback activity, a liability of $43,000 and $79,000 was accrued at December 31, 2017 and 2016, respectively, and is reflected in other liabilities in the Consolidated Statements of Financial Condition. Expense (credit) recognized related to the accrual was $(36,000), $(135,000) and $(95,000) for the years ended December 31, 2017, 2016 and 2015, respectively.

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

	December 31			
	2017		**2016**	
Investor	**Number of Loans**	**Principal Outstanding**	**Number of Loans**	**Principal Outstanding**
	(In Thousands)			
Fannie Mae	**4,920**	**$ 461,783**	5,004	$ 470,692
Freddie Mac	**9,420**	**913,632**	9,229	889,280
Federal Home Loan Bank	**88**	**9,723**	101	11,081
Other	**19**	**930**	16	965
Totals	**14,447**	**$ 1,386,068**	14,350	$ 1,372,018

Custodial escrow balances maintained in connection with serviced loans were $13.5 million and $12.6 million at December 31, 2017 and 2016, respectively.

Significant assumptions at December 31, 2017, used in determining the value of MSRs include a weighted average prepayment speed assumption ("PSA") of 151 and a weighted average discount rate of 12.01%. Significant assumptions at December 31, 2016, used in determining the value of MSRs include a weighted average prepayment rate of 152 PSA and a weighted average discount rate of 12.01%.

A sensitivity analysis of the current fair value to immediate 10% and 20% adverse changes in those assumptions as of December 31, 2017, 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	20% Adverse Change
	(In Thousands)	
Assumption:		
Decline in fair value from increase in prepayment rate	**$ 362**	**$ 735**
Decline in fair value from increase in discount rate	**238**	**472**

9. Premises and Equipment

Premises and equipment are summarized as follows:

	December 31 2017	2016
	(In Thousands)	
Cost:		
Land	**$ 7,977**	$ 7,534
Land improvements	**1,326**	1,310
Buildings	**44,563**	41,895
Leasehold improvements	**971**	971
Furniture, fixtures and equipment	**34,216**	31,253
Construction in process	**1,402**	787
	90,455	83,750
Less allowances for depreciation and amortization	**(50,238)**	(46,792)
	$ 40,217	$ 36,958

Depreciation expense was $3.6 million, $3.4 million and $3.3 million for the years ended December 31, 2017, 2016 and 2015, respectively.

Lease Agreements

The Company has entered into lease agreements covering ten First Insurance offices, four banking center locations, one loan production office, 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. First Federal and First Insurance share office space for one lease as a branch and insurance office.

Future minimum commitments under non-cancelable operating leases are as follows (In Thousands):

2018	$ 826
2019	731
2020	629
2021	619
2022	530
Thereafter	7,690
Total	$ 11,025

Rental expenses under operating leases amounted to $691,000, $571,000 and $601,000 in 2017, 2016, and 2015, respectively.

10. Goodwill and Intangible Assets

Goodwill

The change in the carrying amount of goodwill for the year is as follows:

	December 31	
	2017	2016
	(In Thousands)	
Beginning balance	$ 61,798	$ 61,798
Goodwill acquired or adjusted during the year	36,771	-
Ending balance	$ 98,569	$ 61,798

Acquired Intangible Assets

Activity in intangible assets for the years ended December 31, 2017, 2016 and 2015 was as follows:

	Gross Carrying Amount	Accumulated Amortization	Net Value
		(In Thousands)	
Balance as of January 1, 2015	$ 14,302	$ (11,907)	$ 2,395
Intangible assets acquired	175	-	175
Amortization of intangible assets	-	(699)	(699)
Balance as of December 31, 2015	14,477	(12,606)	1,871
Amortization of intangible assets	-	(535)	(535)
Balance as of December 31, 2016	14,477	(13,141)	1,336
Intangible assets acquired	5,656	-	5,656
Amortization of intangible assets	-	(1,289)	(1,289)
Balance as of December 31, 2017	**$ 20,133**	**$ (14,430)**	**$ 5,703**

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

2018	$ 1,312
2019	1,097
2020	914
2021	744
2022	576
Thereafter	1,060
Total	$ 5,703

11. Deposits

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

	Years Ended December 31		
	2017	2016	2015
		(In Thousands)	
Checking and money market accounts	**$ 2,033**	$ 1,463	$ 1,186
Savings accounts	**102**	88	89
Certificates of deposit	**6,683**	4,710	4,066
Totals	**$ 8,818**	$ 6,261	$ 5,341

Accrued interest payable on deposit accounts amounted to $97,000 and $42,000 at December 31, 2017 and 2016, respectively, which was comprised of $68,000 and $29,000 for certificates of deposit and checking and money market accounts, respectively, at December 31, 2017, and $19,000 and $23,000 for certificates of deposit and checking and money market accounts, respectively, at December 31, 2016.

A summary of deposit balances is as follows:

	December 31	
	2017	**2016**
	(In Thousands)	
Non-interest bearing checking accounts	**$ 571,360**	$ 487,663
Interest bearing checking and money market accounts	**1,005,519**	816,665
Savings deposits	**302,022**	243,369
Retail certificates of deposit less than $250,000	**504,912**	400,080
Retail certificates of deposit greater than $250,000	**53,843**	33,851
	$ 2,437,656	$ 1,981,628

Scheduled maturities of certificates of deposit at December 31, 2017 are as follows (In Thousands):

2018	$ 252,895
2019	180,739
2020	52,453
2021	47,516
2022	25,016
Thereafter	136
Total	$ 558,755

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 commercial 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 commercial real estate loans, and agriculture real estate loans must have collateral of at least 300% of the borrowings. 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, 2017, and December 31, 2016, were $1.0 billion and $843.8 million, respectively. First Federal could obtain advances of up to approximately $567.4 million from the FHLB at December 31, 2017.

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

Principal Terms	Advance Amount (In Thousands)	Range of Maturities	Weighted Average Interest Rate
December 31, 2017			
Putable advances	**$ 5,000**	**March 2018**	**2.35%**
Single maturity fixed rate advances	**72,000**	**January 2018 to March 2022**	**1.46%**
Amortizable mortgage advances	**7,306**	**September 2018 to August 2027**	**1.85%**
	$ 84,306		
December 31, 2016			
Putable advances	$ 5,000	March 2018	2.35%
Single maturity fixed rate advances	92,000	November 2017 to March 2022	1.34%
Amortizable mortgage advances	6,943	September 2018	1.78%
	$ 103,943		

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):

2018	$ 35,018
2019	15,791
2020	21,436
2021	10,297
2022	154
Thereafter	3,878
Total minimum payments	86,574
Less amounts representing interest	(2,268)
Totals	$ 84,306

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, 2017 and 2016, 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, 2017 and 2016. 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 3.09% and 2.46% as of December 31, 2017 and 2016 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 can be redeemed at the Company's option at any time now.

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 2.97% and 2.34% as of December 31, 2017 and 2016 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 mature on December 15, 2035, but can be redeemed at the Company's option at any time now.

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:

	December 31	
	2017	**2016**
	(In Thousands)	
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. Securities Sold Under Agreements to Repurchase and Other Short Term Borrowings

Total securities sold under agreement to repurchase are summarized as follows:

	Years Ended December 31	
	2017	**2016**
	(In Thousands, Except Percentages)	
Securities sold under agreement to repurchase		
Amounts outstanding at year-end	**$ 26,019**	$ 31,816
Year-end interest rate	**0.20%**	0.22%
Average daily balance during year	**23,337**	52,821
Maximum month-end balance during the year	**26,019**	57,984
Average interest rate during the year	**0.23%**	0.26%

We utilize securities sold under agreements to repurchase to facilitate the needs of our customers and to facilitate secured short-term funding needs. Securities sold under agreements to repurchase are stated at the amount of cash received in connection with the transaction. We monitor levels on a continuous basis. We may be required to provide additional collateral based on the fair value of the underlying securities. Securities pledged as collateral under repurchase agreements are maintained with our safekeeping agent.

The remaining contractual maturity of the securities sold under agreements to repurchase in the consolidated balance sheets as of December 31, 2017 and 2016 is presented in the following tables.

	Overnight and Continuous	Up to 30 Days	30-90 Days	Greater than 90 Days	Total
At December 31, 2017			(In Thousands)		
Repurchase agreements:					
Mortgage-backed securities – residential	**$ 6,599**	**$ -**	**$ -**	**$ -**	**$ 6,599**
Collateralized mortgage obligations	**19,420**	**-**	**-**	**-**	**19,420**
Total borrowings	**$ 26,019**	**$ -**	**$ -**	**$ -**	**$ 26,019**
Gross amount of recognized liabilities for repurchase agreements					**$ 26,019**

	Overnight and Continuous	Up to 30 Days	30-90 Days	Greater than 90 Days	Total
At December 31, 2016			(In Thousands)		
Repurchase agreements:					
Mortgage-backed securities – residential	$ 21,222	$ -	$ -	$ -	$ 21,222
Collateralized mortgage obligations	10,594	-	-	-	10,594
Total borrowings	$ 31,816	$ -	$ -	$ -	$ 31,816
Gross amount of recognized liabilities for repurchase agreements					$ 31,816

As of December 31, 2017 and 2016, First Federal had the following undrawn lines of credit facilities available for short-term borrowing purposes:

A $20.0 million line of credit with First Tennessee Bank. The rate on the line of credit is at three-month LIBOR, which floats quarterly. This line was undrawn upon as of December 31, 2017 and 2016.

A $11.2 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, 2017, was 1.25%. This line was undrawn upon as of December 31, 2017 and 2016.

A $20.0 million line of credit with MUFG Union Bank, N.A. The rate on this line of credit is Union Bank's fed funds rate, which floats daily. This line was undrawn upon as of December 31, 2017 and 2016.

15. Other Noninterest Expense

The following is a summary of other noninterest expense:

	Years Ended December 31		
	2017	2016	2015
	(In Thousands)		
Legal and other professional fees	**$ 3,603**	$ 2,902	$ 3,359
Marketing	**2,070**	1,835	1,752
State financial institutions tax	**1,819**	1,781	1,783
REO expenses and write-downs	**177**	244	1,064
Printing and office supplies	**626**	512	457
Amortization of intangibles	**1,289**	535	699
Postage	**523**	456	459
Check charge-offs and fraud losses	**277**	266	207
Credit and collection expense	**359**	303	334
Other	**8,067**(1)	7,118(2)	5,402
Total other noninterest expense	**$ 18,810**	$ 15,952	$ 15,516

1) Includes $1.1 million of acquisition related expenses included in other.
2) Includes $443,000 of acquisition related expenses and $300,000 of costs associated with termination of a lease agreement.

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, and who completed 20 years of service after age 40 receive full medical coverage at no 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.

First Federal employees who were born after December 31, 1950, are not eligible for the medical coverage described above at retirement. Rather, a one-time 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, 2017, 2016 and 2015 are the following amounts that have not yet been recognized in net periodic benefit cost:

	December 31		
	2017	2016	2015
	(In Thousands)		
Unrecognized prior service cost	**$ 39**	$ 52	$ 53
Unrecognized actuarial losses	**551**	392	593
Total loss recognized in Accumulated Other Comprehensive Income	**590**	444	646
Income tax effect	**(206)**	(155)	(226)
Net loss recognized in Accumulated Other Comprehensive Income	**$ 384**	$ 289	$ 420

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, 2018, is $18,000 ($14,000 net of tax) and $9,000 ($7,000 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	
	2017	2016
	(In Thousands)	
Change in benefit obligation:		
Benefit obligation at beginning of year	**$ 2,985**	$ 3,115
Service cost	**58**	53
Interest cost	**117**	128
Participant contribution	**29**	29
Plan amendments for acquisitions	**-**	12
Actuarial (gains) / losses	**166**	(184)
Benefits paid	**(161)**	(168)
Benefit obligation at end of year	**3,194**	2,985
Change in fair value of plan assets:		
Balance at beginning of year	**-**	-
Employer contribution	**132**	139
Participant contribution	**29**	29
Benefits paid	**(161)**	(168)
Balance at end of year	**-**	-
Funded status at end of year	**$ (3,194)**	$ (2,985)

Net periodic postretirement benefit cost includes the following components:

	Years Ended December 31		
	2017	2016	2015
	(In Thousands)		
Service cost-benefits attributable to service during the period	**$ 58**	$ 53	$ 65
Interest cost on accumulated postretirement benefit obligation	**117**	128	130
Net amortization and deferral	**19**	30	47
Net periodic postretirement benefit cost	**194**	211	242
Net (gain) / loss during the year	**166**	(184)	(204)
Plan amendment for acquisition	**-**	12	-
Amortization of prior service cost and actuarial losses	**(19)**	(30)	(47)
Total recognized in comprehensive income	**147**	(202)	(251)
Total recognized in net periodic postretirement benefit cost and other comprehensive income	**$ 341**	$ 9	$ (9)

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

	2017	2016	2015
Weighted average discount rates:			
Used to determine benefit obligations at December 31	**3.50%**	4.00%	4.25%
Used to determine net periodic postretirement benefit cost for years ended December 31	**4.00%**	4.25%	4.25%
Assumed health care cost trend rates at December 31:			
Health care cost trend rate assumed for next year	**7.00%**	7.50%	6.50%
Rate to which the cost trend rate is assumed to decline (the ultimate trend rate)	**5.00%**	5.00%	5.00%
Year that rate reaches ultimate trend rate	**2022**	2022	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)
2018	$ 174
2019	181
2020	194
2021	210
2022	191
2023 through 2027	1,073

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:

	One-Percentage-Point Increase		One-Percentage-Point Decrease	
	Year Ended December 31		Year Ended December 31	
	2017	2016	**2017**	2016
	(In Thousands)			
Effect on total of service and interest cost	**$ 25**	$ 27	**$ (21)**	$ (22)
Effect on postretirement benefit obligation	**392**	369	**(333)**	(314)

The Company expects to contribute $174,000 before reflecting expected Medicare retiree drug subsidy payments in 2018.

17. Regulatory Matters

First Defiance and First Federal are 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 Defiance's financial statements. Under capital adequacy guidelines, First Defiance and First Federal must maintain capital amounts in excess of minimum ratios based on quantitative measures of their assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting practices.

In July 2013, the Federal Reserve and the FDIC approved the final rules implementing the Basel Committee on Banking Supervision's capital guidelines for U.S. banks (commonly known as Basel III). Under the final rules, which began for the Company and the Bank on January 1, 2015 and are subject to a phase-in period through January 1, 2019, minimum requirements will increase for both quantity and quality of capital held by the Company and the Bank. The rules include a minimum common equity Tier

1 capital to risk-weighted assets ratio ("CET1") of 4.5% and a capital conservation buffer of 2.5% of risk-weighted assets, which when fully phased-in, effectively results in a minimum CET1 ratio of 7.0%. Basel III raises the minimum ratio of Tier 1 capital to risk-weighted assets from 4.0% to 6.0% (which, with the capital conservation buffer, effectively results in a minimum Tier 1 capital ratio of 8.5% when fully phased-in), which effectively results in a minimum total capital to risk-weighted assets ratio of 10.5% (with the capital conservation buffer fully phased-in), and requires a minimum leverage ratio of 4.0%. Basel III also makes changes to risk weights for certain assets and off-balance sheet exposures.

The federal banking agencies have also established a system of "prompt corrective action" to resolve certain problems of undercapitalized banks. The regulatory agencies can initiate certain mandatory actions if First Federal fails to meet the minimum capital requirements, which could have a material effect on the Company's financial statements.

The following schedule presents First Defiance consolidated and First Federal's regulatory capital ratios as of December 31, 2017 and 2016 (Dollars in Thousands):

December 31, 2017

	Actual		Minimum Required for Adequately Capitalized		Minimum Required to be Well Capitalized for Prompt Corrective Action	
	Amount	**Ratio**	**Amount**	**Ratio(1)**	**Amount**	**Ratio**
CET1 Capital (to Risk-Weighted Assets) (2)						
Consolidated	$274,832	10.43%	$118,596	4.5%	N/A	N/A
First Federal	$298,571	11.33%	$118,534	4.5%	$171,216	6.5%
Tier 1 Capital (2)						
Consolidated	$309,832	10.80%	$114,773	4.0%	N/A	N/A
First Federal	$298,571	10.43%	$114,539	4.0%	$143,173	5.0%
Tier 1 Capital (to Risk Weighted Assets) (2)						
Consolidated	$309,832	11.76%	$158,128	6.0%	N/A	N/A
First Federal	$298,571	11,33%	$158,046	6.0%	$2210,728	8.0%
Total Capital (to Risk Weighted Assets) (2)						
Consolidated	$336,515	12.77%	$210,838	8.0%	N/A	N/A
First Federal	$325,254	12.35%	$210,728	8.0%	$263,410	10.0%

(1) Excludes capital conservation buffer of 1.25% as of December 31, 2017.
(2) Core capital is computed as a percentage of adjusted total assets of $2.87 billion for consolidated and $2.86 billion for the Bank. Risk-based capital is computed as a percentage of total risk-weighted assets of $2.64 billion for consolidated and $2.63 billion for the Bank.

December 31, 2016

	Actual		Minimum Required for Adequately Capitalized		Minimum Required to be Well Capitalized for Prompt Corrective Action	
	Amount	Ratio	Amount	Ratio(1)	Amount	Ratio
CET1 Capital (to Risk-Weighted Assets) (2)						
Consolidated	$234,809	10.45%	$101,108	4.5%	N/A	N/A
First Federal	$242,928	10.81%	$101,116	4.5%	$146,057	6.5%
Tier 1 Capital (2)						
Consolidated	$269,809	11.24%	$95,975	4.0%	N/A	N/A
First Federal	$242,928	10.14%	$95,791	4.0%	$119,739	5.0%
Tier 1 Capital (to Risk Weighted Assets) (2)						
Consolidated	$269,809	12.01%	$134,811	6.0%	N/A	N/A
First Federal	$242,928	10.81%	$134,822	6.0%	$179,763	8.0%
Total Capital (to Risk Weighted Assets) (2)						
Consolidated	$295,693	13.16%	$179,748	8.0%	N/A	N/A
First Federal	$268,812	11.96%	$179,763	8.0%	$224,703	10.0%

(1) Excludes capital conservation buffer of 0.625% as of December 31, 2016.
(2) Core capital is computed as a percentage of adjusted total assets of $2.21 billion for consolidated and the Bank. Risk-based capital is computed as a percentage of total risk-weighted assets of $2.04 billion for consolidated and the Bank.

Dividend Restrictions - Dividends paid by First Federal to First Defiance are subject to various regulatory restrictions. First Federal paid $13.0 million in dividends to First Defiance in 2017 and $22.0 million in 2016. First Federal may not pay dividends to First Defiance in excess of its net profits (as defined by statute) for the last two fiscal years, plus any year to date net profits without the approval of the OCC. First Insurance paid $1.8 million in dividends to First Defiance in 2017 and $1.2 million in dividends in 2016. First Defiance Risk Management paid $1.0 million in dividends to First Defiance in 2017 and 2016.

18. Income Taxes

Income tax expense for 2017 was impacted by the adjustment of our deferred tax assets and liabilities related to the reduction in the U.S. federal statutory income tax rate to 21% under the Tax Cuts and Jobs Act, which was enacted on December 22, 2017. As a result of the new law, which is more fully discussed below, the Company recognized a net tax expense of $154,000.

The components of income tax expense are as follows:

	Years Ended December 31		
	2017	2016	2015
	(In Thousands)		
Current:			
Federal	**$ 14,588**	$ 13,125	$ 11,299
State and local	**181**	244	146
Deferred	**1,261**	(615)	(35)
Tax reform revaluation	**154**	-	-
	$ 16,184	$ 12,754	$ 11,410

The effective tax rates differ from federal statutory rate applied to income before income taxes due to the following:

	Years Ended December 31		
	2017	2016	2015
	(In Thousands)		
Tax expense at statutory rate (35%)	**$ 16,958**	$ 14,559	$ 13,240
Increases (decreases) in taxes from:			
State income tax – net of federal tax benefit	**119**	159	95
Tax exempt interest income, net of TEFRA	**(1,218)**	(1,168)	(1,219)
Bank owned life insurance	**(1,212)**	(341)	(255)
Captive insurance	**(364)**	(414)	(415)
BOLI surrender	**1,721**	-	-
Tax reform revaluation	**154**	-	-
Other	**26**	(41)	(36)
Totals	**$ 16,184**	$ 12,754	$ 11,410

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	
	2017	2016
	(In Thousands)	
Deferred federal income tax assets:		
Allowance for loan losses	**$ 5,415**	$ 9,059
Postretirement benefit costs	**671**	1,044
Deferred compensation	**1,354**	1,847
Impaired loans	**1,432**	1,087
Accrued vacation	**123**	454
Allowance for real estate held for sale losses	**71**	226
Deferred loan origination fees and costs	**332**	462
Accrued bonus	**333**	626
Other	**1,578**	1,554
Total deferred federal income tax assets	**11,309**	16,359
Deferred federal income tax liabilities:		
FHLB stock dividends	**1,558**	2,279
Goodwill	**4,377**	5,967
Mortgage servicing rights	**2,060**	3,358
Fixed assets	**1,039**	1,217
Other intangible assets	**990**	301
Loan mark to market	**5**	59
Net unrealized gains on available-for-sale securities	**194**	272
Prepaid expenses	**539**	694
Other	**316**	-
Total deferred federal income tax liabilities	**11,078**	14,147
Net deferred federal income tax asset/ (liability)	**$ 231**	$ 2,212

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, 2017.

Retained earnings at December 31, 2017, 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, 2017, was approximately $2.31 million.

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

Balance at January 1, 2015	$ -
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	-
Settlements	-
Balance at December 31, 2015	$ -

Balance at January 1, 2016	$ -
Additions based on tax positions related to the current year	-
Additions for tax positions of prior years	398
Reductions for tax positions of prior years	-
Reductions due to the statute of limitations	-
Settlements	-
Balance at December 31, 2016	$ 398

Balance at January 1, 2017	**$ 398**
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	**-**
Settlements	**(398)**
Balance at December 31, 2017	**$ -**

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 was $0, $40,000 and $0 for the years ended December 31, 2017, 2016 and 2015. The amount accrued for interest and penalties was $0, $40,000 and $0 at December 31, 2017, 2016 and 2015.

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 2014. The Company currently operates primarily in the states of Ohio and Michigan, which tax financial institutions based on their equity rather than their income.

Tax Cuts and Jobs Act – The Tax Cuts and Jobs Act was enacted on December 22, 2017. Among other things, the new law (i) establishes a new, flat corporate federal statutory income tax rate of 21%, (ii) eliminates the corporate alternative minimum tax and allows the use of any such carryforwards to offset regular tax liability for any taxable year, (iii) limits the deduction for net interest expense incurrent by U.S. corporations, (iv) allows businesses to immediately expense, for tax purposes, the cost of new investments in certain qualified depreciable assets, (v) eliminates or reduces certain deductions related to meals and entertainment expenses, (vi) modifies the limitation on excessive employee remuneration to eliminate the exception for performance-based compensation and clarifies the definition of a covered employee and (vii) limits the deductibility of deposit insurance premiums. The Tax Cuts and Jobs Act also significantly changes U.S. tax law related to foreign operations, however, such changes do not impact First Defiance.

As stated above, as a result of the enactment of the Tax Cuts and Jobs Act on December 22, 2017, First Defiance re-measured its deferred tax assets and liabilities based upon the newly enacted U.S. statutory federal income tax rate of 21%, which is the tax rate at which these assets and liabilities are expected to reverse in the future. First Defiance recognized a net tax expense related to the re-measurement of its deferred tax assets and liabilities totaling $154,000.

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 (the "First Defiance 401(k)") if they meet certain age and service requirements. 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. 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 $1.19 million, $979,000 and $892,000 for the years ended December 31, 2017, 2016 and 2015, 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 $248,000, $71,000 and $78,000 of expense recorded for the years ended December 31, 2017, 2016 and 2015, respectively, with a liability of $1.69 million, $1.04 million and $970,000 for future benefits recorded at December 31, 2017, 2016 and 2015, respectively. The acquisition of CSB added $402,000 to this liability. The discount rate was reduced to 4.00% as of December 31, 2016, resulting in an increase to the Company's liability, and remained unchanged at December 31, 2017.

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 replaced all plans existing at the time of its approval. All awards outstanding under prior plans remain in effect in accordance with their respective terms. Any new awards are 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, 2017, 43,200 options had 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. 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.

The Company approved a Short-Term ("STIP") Equity Incentive Plan and a Long-Term ("LTIP") Equity Incentive Plan for selected members of management.

Under the 2016 and 2017 STIPs, the participants could earn up to 10% 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 benefits under the STIPs is determined as of December 31 of the same year and paid out in cash in the first quarter of the following year. The participants are required to be employed on the day of payout in order to receive such payment.

Under each LTIP, the participants may earn up to 20% to 45% of their salary 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 24,757; 24,526; and 20,657 RSU's to the participants in the 2015, 2016 and 2017 LTIPs, respectively, effective January 1 in the year the award was made, which represents the maximum target award. The amount of benefit under each LTIP will be determined individually at the end of the 36 month performance period ending December 31. The benefits earned under each LTIP will be paid out in equity in the first quarter following the end of the performance period. The participants are required to be employed on the day of payout in order to receive such payment.

In 2017, the Company also granted to employees 11,263 restricted shares, of which 2,727 were restricted stock units and 8,536 were restricted stock grants. Of the 11,263 restricted shares granted, 1,839 were issued to directors and have a one-year vesting period. The remaining 9,424 were issued to employees and have a three year vesting period. The fair value of all granted restricted shares was determined by the stock price at the date of the grant.

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.

The fair value of stock options granted was determined at the date of grant using the Black-Scholes stock option-pricing model and the following assumptions:

	Twelve Months Ended	
	December 31, 2017	**December 31, 2016**
Expected average risk-free rate	-	2.05%
Expected average life	-	8.96 years
Expected volatility	-	41.00%
Expected dividend yield	-	2.33%

Following is activity under the plans during 2017:

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, 2017	**54,750**	**$ 22.21**		
Forfeited or cancelled	**-**	**-**		
Exercised	**(11,550)**	**24.41**		
Granted	**-**	**-**		
Options outstanding, December 31, 2017	**43,200**	**$ 21.62**	**3.15**	**$ 1,311**
Vested or expected to vest at December 31, 2017	**43,200**	**$ 21.62**	**3.15**	**$ 1,311**
Exercisable at December 31, 2017	**31,100**	**$ 17.31**	**1.62**	**$ 1,078**

Information related to the stock option plans follows:

	Year Ended December 31		
	2017	2016	2015
	(In Thousands, except per share amounts)		
Intrinsic value of options exercised	**$ 301**	$ 752	$ 1,069
Cash received from option exercises	**199**	714	1,469
Tax benefit realized from option exercises	**54**	165	160
Weighted average fair value of options granted	**$ -**	$ 13.95	$ 13.13

As of December 31, 2017, there was $103,000 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 2.3 years.

At December 31, 2017, 72,538 RSU's were outstanding. Compensation expense is recognized over the performance period based on the achievement of established targets. Total expense of $2.0 million, $1.3 million and $1.1 million was recorded during the years ended December 31, 2017, 2016 and 2015, respectively, and approximately $774,000 and $773,000 is included within other liabilities at December 31, 2017 and 2016, 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, 2017	**75,468**	$ 32.31	**11,161**	$ 32.30
Granted	**23,384**	50.56	**27,755**	33.24
Vested	**(19,219)**	25.77	**(27,358)**	26.92
Forfeited	**(7,095)**	26.17	**(1,022)**	37.02
Unvested at December 31, 2017	**72,538**	$ 40.52	**10,536**	$ 50.56

The maximum amount of compensation expense that may be earned for the 2017 STIP and the 2015, 2016 and 2017 LTIPs at December 31, 2017, is approximately $3.9 million in the aggregate. However, the estimated expense expected to be earned as of December 31, 2017, based on the performance measures in the plans, is $3.4 million of which $960,000 was unrecognized at December 31, 2017 and will be recognized over the remaining performance period.

As of December 31, 2017, 143,422 shares were available for grant under the 2010 Equity Plan. Options forfeited or cancelled under all plans except the 2010 Equity Plan are no longer available for grant to other participants.

21. Parent Company Statements

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

Statements of Financial Condition	December 31	
	2017	2016
	(In Thousands)	
Assets		
Cash and cash equivalents	**$ 8,860**	$ 23,017
Investment in banking subsidiary	**377,546**	290,053
Investment in non-bank subsidiaries	**22,319**	15,456
Other assets	**1,157**	1,155
Total assets	**$ 409,882**	$ 329,681
Liabilities and stockholders' equity:		
Subordinated debentures	**$ 36,083**	$ 36,083
Accrued liabilities	**513**	580
Stockholders' equity	**373,286**	293,018
Total liabilities and stockholders' equity	**$ 409,882**	$ 329,681

Statements of Income	Years Ended December 31		
	2017	2016	2015
	(In Thousands)		
Dividends from subsidiaries	**$ 15,800**	$ 24,200	$ 30,900
Interest on investments	**-**	-	1
Interest expense	**(1,090)**	(753)	(613)
Other income	**1**	-	1
Noninterest expense	**(697)**	(644)	(588)
Income before income taxes and equity in earnings of subsidiaries	**14,014**	22,803	29,701
Income tax credit	**(605)**	(466)	(397)
Income before equity in earnings of subsidiaries	**14,619**	23,269	30,098
(Distributions in excess of) undistributed equity in earnings of subsidiaries	**17,649**	5,574	(3,675)
Net income	**$ 32,268**	$ 28,843	$ 26,423
Comprehensive income	**$ 32,270**	$ 25,436	$ 25,931

Statements of Cash Flows	Years Ended December 31		
	2017	2016	2015
	(In Thousands)		
Operating activities:			
Net income	**$ 32,268**	$ 28,843	$ 26,423
Adjustments to reconcile net income to net cash (used in) provided by operating activities:			
Distribution in excess of (undistributed equity in) earnings of subsidiaries	**(17,649)**	(5,574)	3,675
Change in other assets and liabilities	**(358)**	235	(205)
Net cash provided by (used in) operating activities	**14,261**	23,504	29,893
Investing activities:			
Cash paid for Commercial Bancshares	**(12,340)**	-	-
Capital contribution to subsidiary	**(6.491)**	-	-
Net cash used in investing activities	**(18,831)**	-	-
Financing activities:			
Repurchase of common stock	**-**	(6,293)	(8,436)
Cash dividends paid	**(9,859)**	(7,890)	(7,159)
Stock Options Exercised	**199**	714	1,469
Direct stock sales	**73**	63	64
Repayment of stock warrants	**-**	-	(11,979)
Net cash used in financing activities	**(9,587)**	(13,406)	(26,041)
Net increase (decrease) in cash and cash equivalents	**(14,157)**	10,098	3,852
Cash and cash equivalents at beginning of year	**23,017**	12,919	9,067
Cash and cash equivalents at end of year	**$ 8,860**	$ 23,017	$ 12,919

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:

- *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.

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, 2017	**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	$ -	$ 508	$ -	$ 508
Mortgage-backed - residential	-	59,269	-	59,269
REMICs	-	1,065	-	1,065
Collateralized mortgage obligations	-	93,876	-	93,876
Preferred stock	1	-	-	1
Corporate bonds	-	13,103	-	13,103
Obligations of state and political subdivisions	-	92,828		92,828
Mortgage banking derivative - asset	-	609	-	609
Mortgage banking derivative -liability	-	11	-	11

December 31, 2016	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	$ -	$ 3,915	$ -	$ 3,915
Mortgage-backed - residential	-	81,707	-	81,707
REMICs	-	1,307	-	1,307
Collateralized mortgage obligations	-	63,005	-	63,005
Preferred stock	2	-	-	2
Corporate bonds	-	13,013	-	13,013
Obligations of state and political subdivisions	-	88,043		88,043
Mortgage banking derivative - asset	-	491	-	491

There were no assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the years ended December 31, 2017 and 2016.

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, 2017	**Level 1 Inputs**	**Level 2 Inputs**	**Level 3 Inputs**	**Total Fair Value**
		(In Thousands)		
Impaired loans				
Commercial Real Estate	**$ -**	**$ -**	**$ 1,787**	**$ 1,787**
Commercial			**2,817**	**2,817**
Total impaired loans	**-**	**-**	**4,604**	**4,604**
Mortgage servicing rights	**-**	**534**	**-**	**534**
Real estate held for sale				
CRE	**-**	**-**	**227**	**227**
Total Real Estate held for sale	**-**	**-**	**227**	**227**

December 31, 2016	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total Fair Value
	(In Thousands)			
Impaired loans				
1-4 Family Residential Real Estate	$ -	$ -	$ 316	$316
Commercial Real Estate	-	-	848	848
Commercial			332	332
Total impaired loans	-	-	1,496	1,496
Mortgage servicing rights	-	657	-	657
Real estate held for sale				
CRE	-	-	377	377
Total Real Estate held for sale	-	-	377	377

For Level 3 assets and liabilities measured at fair value on a recurring or nonrecurring basis as of December 31, 2017, 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)		
Impaired Loans- Applies to all loan classes	$4,604	Appraisals which utilize sales comparison, net income and cost approach	Discounts for collection issues and changes in market conditions	10-20%	10%
Real estate held for sale – Applies to all classes	$227	Appraisals which utilize sales comparison, net income and cost approach	Discounts for changes in market conditions	0%	0%

For Level 3 assets and liabilities measured at fair value on a recurring or nonrecurring basis as of December 31, 2016, 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)		
Impaired Loans- Applies to all loan classes	$1,496	Appraisals which utilize sales comparison, net income and cost approach	Discounts for collection issues and changes in market conditions	10-30%	11%
Real estate held for sale – Applies to all classes	$377	Appraisals which utilize sales comparison, net income and cost approach	Discounts for changes in market conditions	0-20%	7%

Impaired loans, which are measured for impairment using the fair value of the collateral for collateral dependent loans, had a fair value of $4.6 million, with no valuation allowance and a fair value of $1.5 million with a valuation allowance of $1,000 at December 31, 2017 and 2016, respectively. A provision expense of $993,000, $1.0 million, and a provision recovery of $580,000 for the years ended December 31, 2017, 2016 and 2015, respectively, 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 $534,000 with a valuation allowance of $432,000 and a fair value of $657,000 with a valuation allowance of $522,000 at December 31, 2017 and 2016, respectively. A recovery of $90,000, $123,000 and $266,000 for the years ended December 31, 2017, 2016 and 2015, respectively, 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 $20,000, $74,000 and $297,000 for the years ended December 31, 2017, 2016 and 2015, respectively, 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, 2017, and December 31, 2016. 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 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 asset.

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, 2017.

	Carrying Value	Fair Value Measurements at December 31, 2017 (In Thousands) Total	Level 1	Level 2	Level 3
Financial Assets:					
Cash and cash equivalents	**$ 113,693**	**$ 113,693**	**$ 113,693**	**$ -**	**$ -**
Investment securities	**261,298**	**261,299**	**1**	**261,298**	**-**
Federal Home Loan Bank Stock	**15,992**	**N/A**	**N/A**	**N/A**	**N/A**
Loans, net, including loans held for sale	**2,332,465**	**2,315,791**	**-**	**10,830**	**2,304,961**
Accrued interest receivable	**8,706**	**8,706**	**13**	**917**	**7,776**
Financial Liabilities:					
Deposits	**$ 2,437,656**	**$ 2,444,683**	**$ 571,360**	**$ 1,873,323**	**$ -**
Advances from Federal Home Loan Bank	**84,279**	**83,261**	**-**	**83,261**	**-**
Securities sold under repurchase agreements	**26,019**	**26,019**	**-**	**26,019**	**-**
Subordinated debentures	**36,083**	**35,385**	**-**	**-**	**35,385**

	Carrying Value	Fair Value Measurements at December 31, 2016 (In Thousands) Total	Level 1	Level 2	Level 3
Financial Assets:					
Cash and cash equivalents	$ 99,003	$ 99,003	$ 99,003	$ -	$ -
Investment securities	251,176	251,179	2	251,177	-
Federal Home Loan Bank Stock	13,798	N/A	N/A	N/A	N/A
Loans, net, including loans held for sale	1,924,210	1,911,280	-	9,917	1,901,363
Accrued interest receivable	6,760	6,760	9	867	5,884
Financial Liabilities:					
Deposits	$ 1,981,628	$ 1,987,723	$ 487,663	$ 1,500,060	$ -
Advances from Federal Home Loan Bank	103,943	103,019	-	103,019	-
Securities sold under repurchase agreements	31,816	31,816	-	31,816	-
Subordinated debentures	36,083	34,718	-	-	34,718

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 \$14.8 million and \$14.1 million of interest rate lock commitments at December 31, 2017 and 2016, respectively. There were \$23.2 million and \$22.5 million of forward commitments for the future delivery of residential mortgage loans at December 31, 2017 and 2016, 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, 2017			December 31, 2016		
	Assets	(Liabilities)		Assets	(Liabilities)	
	Carrying Value	Carrying Value	Derivative Net Carrying Value	Carrying Value	Carrying Value	Derivative Net Carrying Value
	(In Thousands)					
Derivatives not designated as hedging instruments						
Mortgage Banking Derivatives	**$ 609**	**$ 11**	**$ 598**	$ 491	$ -	$ 491

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,		
	2017	2016	2015
Derivatives not designated as hedging instruments	(In Thousands)		
Mortgage Banking Derivatives – Gain (Loss)	**$ 107**	$ (67)	$ 231

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**
2017	(In Thousands, Except Per Share Amounts)			
Interest income	**$ 24,036**	**$ 27,458**	**$ 28,081**	**$ 28,527**
Interest expense	**2,391**	**2,826**	**3,074**	**3,140**
Net interest income	**21,645**	**24,632**	**25,007**	**25,387**
Provision for loan losses	**55**	**2,118**	**462**	**314**
Net interest income after provision for loan losses	**21,590**	**22,514**	**24,545**	**25,073**
Gain on sale, call or write-down of securities	**-**	**267**	**158**	**159**
Noninterest income	**10,549**	**9,873**	**9,337**	**9,738**
Noninterest expense	**23,142**	**20,630**	**20,440**	**21,139**
Income before income taxes	**8,997**	**12,024**	**13,600**	**13,831**
Income taxes	**3,857**	**3,677**	**4,219**	**4,431**
Net income	**$ 5,140**	**$ 8,347**	**$ 9,381**	**$ 9,400**
Earnings per common share:				
Basic	**$ 0.54**	**$ 0.82**	**$ 0.92**	**$ 0.93**
Diluted	**$ 0.54**	**$ 0.82**	**$ 0.92**	**$ 0.92**
Average shares outstanding:				
Basic	**9,435**	**10,147**	**10,149**	**10,155**
Diluted	**9,490**	**10,204**	**10,209**	**10,222**

	Three Months Ended			
	March 31	June 30	September 30	December 31
	(In Thousands, Except Per Share Amounts)			
2016				
Interest income	$ 21,130	$ 21,480	$ 22,003	$ 22,770
Interest expense	1,942	2,084	2,183	2,231
Net interest income	19,188	19,396	19,820	20,539
Provision for loan losses	364	53	15	(149)
Net interest income after provision for loan losses	18,824	19,343	19,805	20,688
Gain on sale, call or write-down of securities	131	227	151	-
Noninterest income	8,505	8,348	8,375	8,293
Noninterest expense	17,274	17,347	18,292	18,180
Income before income taxes	10,186	10,571	10,039	10,801
Income taxes	3,017	3,307	2,994	3,436
Net income	$ 7,169	$ 7,264	$ 7,045	$ 7,365
Earnings per common share:				
Basic	$ 0.80	$ 0.81	$ 0.78	$ 0.82
Diluted	$ 0.80	$ 0.80	$ 0.78	$ 0.81
Average shares outstanding:				
Basic	8,994	8,968	8,976	8,969
Diluted	9,064	9,036	9,050	9,035

25. 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 in the accompanying consolidated condensed statements of income. Reclassification adjustments related to the defined benefit postretirement medical plan are included in compensation and benefits in the accompanying consolidated condensed statements of income.

	Before Tax Amount	Tax Effect	Net of Tax Amount
Twelve months ended December 31, 2017:		(In Thousands)	
Securities available for sale and transferred securities:			
Change in net unrealized gain/(loss) during the period	**$ 733**	**$ 256**	**$ 477**
Reclassification adjustment for net gains included in net income	**(584)**	**(204)**	**(380)**
Defined benefit postretirement medical plan:			
Net gain on defined benefit postretirement medical plan realized during the period	**(166)**	**(59)**	**(107)**
Reclassification adjustment for net amortization and deferral on defined benefit postretirement medical plan (included in compensation and benefits)	**19**	**7**	**12**
Total other comprehensive income	**$ 2**	**$ 0**	**$ 2**

	Before Tax Amount	Tax Effect	Net of Tax Amount
Twelve months ended December 31, 2016:		(In Thousands)	
Securities available for sale and transferred securities:			
Change in net unrealized gain/(loss) during the period	$ (4,933)	$ (1,726)	$ (3,207)
Reclassification adjustment for net gains included in net income	(509)	(178)	(331)
Defined benefit postretirement medical plan:			
Net gain on defined benefit postretirement medical plan realized during the period	172	60	112
Reclassification adjustment for net amortization and deferral on defined benefit postretirement medical plan (included in compensation and benefits)	30	11	19
Total other comprehensive income	$ (5,240)	$ (1,833)	$ (3,407)

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

	Securities Available For Sale	Post-retirement Benefit	Accumulated Other Comprehensive Income
		(In Thousands)	
Balance January 1, 2017	**$ 504**	**$ (289)**	**$ 215**
Other comprehensive income before reclassifications	**477**	**(108)**	**369**
Amounts reclassified from accumulated other comprehensive loss	**(380)**	**13**	**(367)**
Net other comprehensive income during period	**97**	**(95)**	**2**
Balance December 31, 2017	**$ 601**	**$ (384)**	**$ 217**
Balance January 1, 2016	$ 4,042	$ (420)	$ 3,622
Other comprehensive income before reclassifications	(3,207)	112	(3,095)
Amounts reclassified from accumulated other comprehensive loss	(331)	19	(312)
Net other comprehensive income during period	(3,538)	131	(3,407)
Balance December 31, 2016	$ 504	$ (289)	$ 215

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, 2017. 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, 2017, 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, 2017, 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 by this item relating to our directors, nominees for directorship and executive officers is incorporated herein by reference from the section captioned "Composition of the Board" under the heading "PROPOSAL 1 – Election of Directors" and the section immediately following the heading "EXECUTIVE OFFICERS" in the definitive proxy statement to be filed on or about March 12, 2018 for the annual meeting of First Defiance shareholders to be held on April 24, 2018 (the "Proxy Statement"). Information regarding our Audit Committee and compliance with Section 16(a) of the Securities Act of 1943 required by this item is incorporated herein by reference from the sections respectively captioned, "Board Committees" under the "PROPOSAL 1 – Election of Directors" and the section immediately following the heading "SECTION 16(a) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE" of the Proxy Statement. There have been no material changes to the procedures by which shareholders may recommend nominees to the board of directors.

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 regarding director compensation is set forth under the section captioned "Director Compensation" under the heading "PROPOSAL 1 – Election of Directors" of the Proxy Statement, and is incorporated herein by reference. Executive compensation information has been provided under the headings "COMPENSATION DISCUSSION AND ANALYSIS" and "EXECUTIVE COMPENSATION" in the Proxy Statement, and is incorporated herein by reference.

The Compensation Committee Report and information related to compensation committee interlocks and insider participation have been respectively set forth under the section immediately following the heading "COMPENSATION COMMITTEE REPORT" and under the section captioned "Compensation Committee Interlocks and Insider Participation" following the heading "PROPOSAL 1 – Election of Directors" in the Proxy Statement, and are incorporated herein by reference.

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

The information regarding security ownership of certain beneficial owners and management and information relating thereto is set forth in the section under the heading "BENEFICIAL OWNERSHIP" in the Proxy Statement, and is incorporated herein by reference.

Equity Compensation Plans

The following table provides information as of December 31, 2017, with respect to the shares of First Defiance common stock that are reserved for issuance under First Defiance's existing equity compensation plans.

Plan Category	Number of securities to be Issued Upon Exercise of Outstanding Options, Warrants and Rights	Weighted Average Exercise Price of Outstanding Options, Warrants and Rights	Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans (Excluding Securities Reflected in Column (a)
	(a)	(b)	(c)
Equity Compensation Plans Approved by Security Holders	43,200	$21.62	143,422

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

The information required by this item, including related transactions and director independence, is set forth respectively in the section following the heading "RELATED PERSON TRANSACTIONS" and in the section captioned "Composition of the Board" following the heading "PROPOSAL 1 – Election of Directors" in the Proxy Statement, which are both incorporated by reference.

Item 14. Principal Accountant Fees and Services

The information required by this item is set forth under the section captioned "Audit Fees" following the heading "INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM" in the Proxy Statement, and 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, 2017 and 2016
(C) Consolidated Statements of Income for the years ended December 31, 2017, 2016 and 2015
(D) Consolidated Statements of Comprehensive Income for the years ended December 31, 2017, 2016 and 2015
(E) Consolidated Statements of Changes in Stockholders' Equity for the years ended December 31, 2017, 2016 and 2015
(F) Consolidated Statements of Cash Flows for the years ended December 31, 2017, 2016 and 2017
(G) Notes to Consolidated Financial Statements

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

(3) The exhibits required by this item are listed in the Exhibit Index of this Form 10-K. The management contracts and compensation plans or arrangements required to be filed with this Form 10-K are listed as Exhibits 10.1 through 10.24.

Item 16. 10-K Summary

None.

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, 2018

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, 2018.

Signature	Title
/s/ William J. Small William J. Small	Chairman of the Board
/s/ Donald P. Hileman Donald P. Hileman	President and Chief Executive Officer
/s/ Kevin T. Thompson Kevin T. Thompson	Executive Vice President and Chief Financial Officer (principal accounting officer)
/s/ John L. Bookmyer John L. Bookmyer	Director, Vice Chairman
/s/ Dr. Douglas A. Burgei Dr. Douglas A. Burgei	Director
/s/ Thomas A. Reineke Thomas A. Reineke	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/ Charles D. Niehaus Charles D. Niehaus	Director
/s/ Terri A. Bettinger Terri A. Bettinger	Director
/s/ Thomas K. Herman II Thomas K. Herman II	Director
/s/ Mark A. Robison Mark A. Robison	Director

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	
2.1	Agreement and Plan of Merger, dated August 23, 2016, by and between First Defiance and Commercial Bancshares, Inc.	(28)
2.2	Amendment to Agreement and Plan of Merger, dated October 31, 2016, by and between First Defiance and Commercial Bancshares, Inc.	(12)
3.1	Articles of Incorporation of First Defiance, as amended	(1)
3.2	Code of Regulations of First Defiance	(1)
4.1	Agreement to furnish instruments and agreements defining rights of holders of long-term debt	(26)
10.3	Employment Agreement with Gregory R. Allen	(5)
10.4	2005 Stock Option and Incentive Plan	(6)
10.7	Form of Contingent Award Agreement under LTIP	(10)
10.8	Form of Stock Option Award Agreement under 2005 Stock Option and Incentive Plan	(3)
10.9	First Federal Amended and Restated Executive Group Life Plan – Post Separation	(13)
10.10	2010 Equity Incentive Plan	(14)
10.11	First Defiance Deferred Compensation Plan	(22)
10.13	2010 Equity Plan Form of Long-Term Incentive Performance-Based Award Agreement	(16)
10.14	2010 Equity Plan Form of Short-Term Incentive Performance-Based Award Agreement	(17)
10.15	First Amendment to First Defiance Financial Corp. 2010 Equity Incentive Plan	(18)
10.16	First Defiance Financial Corp. and Affiliates Incentive Compensation Plan	(19)
10.18	First Defiance Financial Corp. Long-Term Restricted Stock Unit Award Agreement (2012 Long Term Incentive)	(21)
10.19	Employment Agreement with Donald P. Hileman	(23)
10.20	Employment Agreement with Kevin T. Thompson	(24)
10.21	Form of Restricted Stock Award Agreement	(25)
10.22	Change of Control and Non-Solicitation Agreement with John R. Reisner	(27)
10.23	Form of Restricted Stock Unit Award Agreement	(12)
21	List of Subsidiaries of the Company	(29)
23.1	Consent of Crowe Horwath LLP	(29)
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	(29)
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	(29)
32.1	Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	(29)
32.2	Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	(29)

101	Interactive data files pursuant to Rule 405 of Regulation S-T: (i) the Consolidated Statements of Financial Condition, (ii) the Consolidated Statements of Income, (iii) the Consolidated Statements of Comprehensive Income, (iv) the Consolidated Statements of Changes in Stockholders' Equity, (v) the Consolidated Statements of Cash Flows, and (vi) the Notes to the Consolidated Financial Statements tagged as blocks of text and in detail.	(29)

(1) Incorporated herein by reference to the like numbered exhibit in the Registrant's Form S-3 filed on November 10, 2009 (File No. 333-163014)
(2) Incorporated herein by reference to exhibit 10.16 in the Registrant's 2008 Form 10-K (Film No. 09683948)
(3) Incorporated herein by reference to exhibit 10.4 in Form 8-K filed October 1, 2007 (Film No. 071144951)
(4) Incorporated herein by reference to Appendix A to the 2005 Proxy Statement (Film No. 05692264)
(5) Incorporated herein by reference to exhibit 10.2 in Form 8-K filed December 12, 2008 (Film No. 081245224)
(6) Incorporated herein by reference to the like numbered exhibit in the Registrant's 2016 Form 10-K (File No. 17645447)
(7) Incorporated herein by reference to exhibit 10.1 in Form 10-Q filed November 2, 2010 (Film No. 101158262)
(8) Incorporated herein by reference to Annex A to 2010 Proxy Statement (Film No. 10693151)
(9) Incorporated herein by reference to exhibit 10.1 in Form 10-Q filed November 8, 2011 (Film No. 111188059)
(10) Incorporated herein by reference to exhibit 10.2 in Form 10-Q filed November 8, 2011 (Film No. 111188059)
(11) Incorporated herein by reference to exhibit 10.1 in Form 8-K filed March 15, 2012 (Film No. 12694926)
(12) Incorporated herein by reference to exhibit 10.2 in Form 8-K filed March 15, 2012 (Film No. 12694926)
(13) Incorporated herein by reference to exhibit 10.4 in Form 8-K filed March 15, 2012 (Film No. 12694926)
(14) Incorporated herein by reference to exhibit 10.1 in Form 8-K filed December 23, 2005 (Film No. 051284175)
(15) Incorporated herein by reference to exhibit 10.1 in Form 8-K filed December 30, 2013 (Film No. 131303552)
(16) Incorporated herein by reference to exhibit 10.2 in Form 8-K filed December 30, 2013 (Film No. 131303552)
(17) Incorporated herein by reference to exhibit 10.3 in Form 8-K filed December 30, 2013 (Film No. 131303552)
(18) Incorporated herein by reference to like numbered exhibit in Registrant's 2014 Form 10-K (Film No. 15655545)
(19) Incorporated herein by reference to exhibit 10.23 in Registrant's 2015 Form 10-K (Film No. 161468309)
(20) Incorporated herein by reference to the like numbered exhibit in Form 8-K filed August 24, 2016 (Film No. 161848221)
(21) Included herein

SHAREHOLDER INFORMATION

ANNUAL MEETING

The Annual Meeting of Shareholders will be conducted virtually at 1:00 p.m. on Tuesday, April 24, 2018. Shareholders may access the Annual Meeting by going to **www.virtualshareholdermeeting.com/fdef2018**

INVESTOR INFORMATION

Shareholders, investors and analysts interested in additional information about First Defiance Financial Corp., may contact Investor Relations at the corporate office, 419-782-5104.

STOCK TRANSFER AGENT

Shareholders with questions concerning the transfer of shares, lost certificates, dividend payments, dividend reinvestment, receipt of multiple dividend checks, duplicate mailings or changes of address should contact:

Broadridge Corporate Issuer Solutions
PO Box 1342
Brentwood, NY 11717
1-844-318-0128 or 1-720-358-3594
shareholder@broadridge.com

SECURITIES LISTING

First Defiance Financial Corp. common stock trades on the NASDAQ Global Select Market under the symbol FDEF. As of February 23, 2018, there were approximately 2,407 stockholders of record and 10,182,308 shares outstanding.

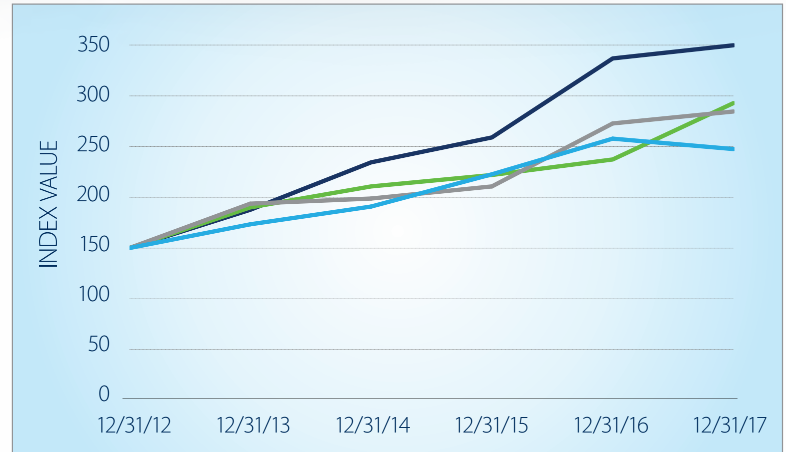
DIVIDEND POLICY

The First Defiance Financial Corp. Board reviews and determines, on a quarterly basis, whether to declare a dividend. Dividends declared in 2017 totaled $1.00 per share.

DIVIDEND REINVESTMENT PLAN

Shareholders may automatically reinvest dividends in additional First Defiance Financial Corp. common stock through the Dividend Reinvestment Plan, which also provides for purchase by voluntary cash contributions. For additional information, please contact: Broadridge Corporate Issuer Solutions at 1-844-318-0128 or 1-720-358-3594.

TOTAL RETURN PERFORMANCE



AUDITORS

Crowe Horwath LLP
330 East Jefferson Boulevard
South Bend, IN 46624

GENERAL COUNSEL

Vorys, Sater, Seymour & Pease LLP
301 East Fourth Street, Suite 3500
Cincinnati, OH 45202

PRICE RANGE

Year Ended December 31, 2017

	HIGH	LOW
First Quarter	$51.15	$46.27
Second Quarter	$56.90	$48.78
Third Quarter	$53.99	$47.01
Fourth Quarter	$56.91	$50.28

Year Ended December 31, 2016

	HIGH	LOW
First Quarter	$40.98	$34.80
Second Quarter	$41.21	$37.53
Third Quarter	$46.83	$35.90
Fourth Quarter	$52.31	$36.91

Better together.

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FINANCIAL CORP.

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Fdef.com

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GROUP

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Firstinsurancegrp.com

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For investor relations information, visit Fdef.com

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