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

FORM 10-Q

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

For the quarterly period ended March 31, 2005

Commission file number 000-51331

BankFinancial Corporation
(Exact name of registrant as specified in its charter)

| | |
|---|---|
| Maryland | APPLIED FOR |
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification No.) |

15W060 North Frontage Road, Burr Ridge, IL 60527
(Address of principal executive offices)

(630) 242-7700
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all the reports 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 report), and (2) has been subject to such filing requirements for the past 90 days. YES NO X

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). YES___ NO X

There were no shares of common stock, par value $.01, outstanding as of May 27, 2005.

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BankFinancial Corporation
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Part I. Financial Information

Part II. Other Information

Part I. Financial Information

BankFinancial Corporation, a Maryland Corporation (the "Company"), was formed to serve as the stock holding company for BankFinancial, F.S.B. (the "Bank") as part of the mutual-to-stock conversion of BankFinancial MHC, Inc. (the "MHC"). As of March 31, 2005, the conversion had not been completed. Accordingly, as of that date, the Company had no assets or liabilities, and had not conducted any business other than that of an organizational nature. Financial and other information with respect to the MHC as of March 31, 2005 is attached as Exhibit 99 to this quarterly report.

For a further discussion of the Company's formation and the operations of the MHC and the Bank, see the Company's Prospectus as filed on April 29, 2005 with the Securities and Exchange Commission pursuant to Rule 424(b)(3) of the Rules and Regulations of the Securities Act of 1933 (File Number 333-119217).

## Part II - Other Information

### Item 1. Legal Proceedings

The Company is not engaged in any legal proceedings of a material nature as of the date of the filing.

### Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

Not applicable.

### Item 3. Defaults Upon Senior Securities

Not applicable.

### Item 4. Submission of Matters to a Vote of Security Holders

Not applicable

### Item 5. Other Information

Not applicable

### Item 6. Exhibits

The following exhibits are either filed as part of this report or are incorporated herein by reference:

| | |
|---|---|
| 31.1 | Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 |
| 31.2 | Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 |
| 32 | Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 |
| 99 | Selected Financial Information |

## SIGNATURES

Pursuant to the requirements 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.

BankFinancial Corporation

| | |
|---|---|
| Dated: May 27, 2005 | /s/ F. Morgan Gasior<br>F. Morgan Gasior<br>Chairman of the Board, Chief Executive Officer and President |
| Dated: May 27, 2005 | /s/ Paul A. Cloutier<br>Paul A. Cloutier<br>Executive Vice President and Chief Financial Officer |

Exhibit 31.1

## Certification of Chief Executive Officer
## Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, F. Morgan Gasior, Chairman of the Board, Chief Executive Officer and President, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of BankFinancial Corporation, a Maryland corporation;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:

    a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

    b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

    c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors:

    a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

    b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 27, 2005

/s/ F. Morgan Gasior
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F. Morgan Gasior
Chairman of the Board, Chief
Executive Officer and President

Exhibit 31.2

# Certification of Chief Financial Officer
## Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Paul A. Cloutier, Executive Vice President and Chief Financial Officer, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of BankFinancial Corporation, a Maryland corporation;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:

   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors:

   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 27, 2005

/s/ Paul A. Cloutier
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Paul A. Cloutier
Executive Vice President
and Chief Financial Officer

Exhibit 32

Certification of Chief Executive Officer and Chief Financial Officer
Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

F. Morgan Gasior, Chairman of the Board, Chief Executive Officer and President of BankFinancial Corporation, a Maryland corporation (the "Company") and Paul A. Cloutier, Executive Vice President and Chief Financial Officer of the Company, each certify in his capacity as an officer of the Company that he has reviewed the quarterly report on Form 10-Q for the quarter ended March 31, 2005 (the "Report") and that to the best of his knowledge:

1. the Report fully complies with the requirements of Sections 13(a) or 15(d) of the Securities Exchange Act of 1934; and

2. the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: May 27, 2005

/s/ F. Morgan Gasior
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F. Morgan Gasior
Chairman of the Board, Chief Executive Officer and President

Date: May 27, 2005

/s/ Paul A. Cloutier
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Paul A. Cloutier
Executive Vice President and Chief Financial Officer

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

Exhibit 99

Note Concerning Forward-Looking Statements

This document contains forward-looking statements, which can be identified by the use of such words such as "estimate," "project," "believe," "intend," "anticipate," "plan," "seek," "expect," "will," "may" and words of similar meaning. These forward-looking statements include, but are not limited to:

- statements of our goals, intentions and expectations;
- statements regarding our business plans, prospects, growth and operating strategies;
- statements regarding the asset quality of our loan and investment portfolios; and
- estimates of our risks and future costs and benefits.

These forward-looking statements are based on our current beliefs and expectations and are inherently subject to significant business, economic and competitive uncertainties and contingencies, many of which are beyond our control. In addition, these forward-looking statements are subject to assumptions with respect to future business strategies and decisions that are subject to change. We are under no duty to and do not take any obligation to update any forward-looking statements after the date of this document.

The following factors, among others, could cause actual results to differ materially from the anticipated results or other expectations expressed in the forward-looking statements:

- general economic conditions, either nationally or in our market areas, that are worse than expected;
- competition among depository and other financial institutions;
- inflation and changes in the interest rate environment that reduce our margins or reduce the fair value of financial instruments;
- adverse changes in the securities markets;
- changes in laws or government regulations or policies affecting financial institutions, including changes in regulatory fees and capital requirements;
- our ability to enter new markets successfully and capitalize on growth opportunities;
- our ability to successfully integrate acquired entities;
- changes in consumer spending, borrowing and savings habits;
- changes in accounting policies and practices, as may be adopted by the bank regulatory agencies, the Financial Accounting Standards Board, the Securities and Exchange Commission and the Public Company Accounting Oversight Board;
- changes in our organization, compensation and benefit plans;
- adverse developments concerning Fannie Mae or Freddie Mac and changes in market interest rates affecting the value of the Fannie Mae and Freddie Mac floating rate preferred stocks in our investment securities portfolio;



- changes in our financial condition or results of operations that reduce capital available to pay dividends;
- regulatory changes or actions; and
- changes in the financial condition or future prospects of issuers of securities that we own.

Because of these and a wide variety of other risks and uncertainties, including, without limitation, the risks and uncertainties set forth below, our actual future results may be materially different from the results indicated by these forward-looking statements:

- the strength of the United States economy in general and the strength of the local economies in which the Company conducts its operations which may be less favorable than expected and may result in, among other things, a deterioration in the credit quality and value of the Company's assets;

- the effects of, and changes in, federal, state and local laws, regulations and policies affecting banking, securities, taxation, insurance and monetary and financial matters, as well as any laws and regulations otherwise affecting the Company, including laws and regulations intended to enhance national security;

- the effects of changes in interest rates (including the effects of changes in the rate of prepayments of the Company's assets) and the policies of the Board of Governors of the Federal Reserve System;

- the ability of the Company to compete with other financial institutions as effectively as the Company currently intends due to increases in competitive pressures in the financial services sector;

- the inability of the Company to obtain new customers and to retain existing customers;

- the timely development and acceptance of products and services, including products and services offered through alternative delivery channels such as the Internet;

- technological changes implemented by the Company and by other parties, including third party vendors, which may be more difficult or more expensive than anticipated or which may have unforeseen consequences to the Company and its customers, including technological changes implemented for, or related to, the Company's Internet website or new products such as prepaid solutions cards, payroll cards and other similar products and services;

- the ability of the Company, and certain of its vendors, to develop and maintain secure and reliable electronic systems, including systems developed for the Company's Internet website or new products such as prepaid solutions cards, payroll cards and other similar products and services.

- the ability of the Company to retain key executives and employees and the difficulty that the Company may experience in replacing key executives and employees in an effective manner;

- changes in consumer spending and saving habits that affect the Company's business adversely;

- the economic impact of terrorist activities and military actions;

- business combinations and the integration of acquired businesses which may be more difficult or expensive than expected;

- the costs, effects and outcomes of existing or future litigation;

- changes in accounting policies and practices, as may be adopted by state and federal regulatory agencies and the Financial Accounting Standards Board; and

- the ability of the Company to manage the risks associated with the foregoing as well as anticipated.

These risks and uncertainties should be considered in evaluating forward-looking statements and undue reliance should not be placed on such statements. Additional information concerning the Company and its business, including other factors that could materially affect the Company's financial results, is included in the Company's filings with the Securities and Exchange Commission.

## Selected Consolidated Financial Data

The following tables set forth selected consolidated historical financial and other data of BankFinancial MHC, Inc. ("MHC") for the periods and at the dates indicated. The information at December 31, 2004 is derived in part from, and should be read together with, the audited consolidated financial statements and notes thereto of MHC, included in the prospectus of BankFinancial Corporation, a Maryland corporation, as filed as filed on April 29, 2005 with the Securities and Exchange Commission pursuant to Rule 424(b)(3) of the Rules and Regulations of the Securities Act of 1933 (File Number 333-119217). The information at March 31, 2005 and for the three months ended March 31, 2005 and 2004 is derived from unaudited consolidated financial statements of MHC. However, in the opinion of management of MHC, all adjustments, consisting of normal recurring adjustments, necessary for a fair presentation of the results of operations for the unaudited periods have been made. The selected operating data presented below for the three months ended March 31, 2005, are not necessarily indicative of the results that may be expected for the year ending December 31, 2005.

| | At March 31, 2005 | At December 31, 2004 |
|---|---|---|
| | (In thousands) | |
| Selected Financial Condition Data: | | |
| Total assets | $1,495,497 | $1,492,782 |
| Loans, net | 1,090,316 | 1,091,952 |
| Loans held-for-sale | 5,737 | 5,531 |
| Securities available-for-sale at fair value | 274,506 | 268,093 |
| Goodwill | 10,865 | 10,865 |
| Core deposit intangible | 9,472 | 9,882 |
| Deposits | 1,108,637 | 1,115,696 |
| Borrowings | 272,073 | 264,742 |
| Equity | 99,009 | 94,888 |

| | Three Months Ended March 31, 2005 | 2004 |
|---|---|---|
| | (In thousands) | |
| Selected Operating Data: | | |
| Interest and dividend income | $ 18,042 | $ 16,030 |
| Interest expense | 6,834 | 6,176 |
| Net interest income | 11,208 | 9,854 |
| Provision (credit) for loan losses | (76) | -- |
| Net interest income after provision (credit) for loan losses | 11,284 | 9,854 |
| Noninterest income | 1,852 | 2,147 |
| Noninterest expense | 10,729 | 10,810 |
| Income before income tax expense | 2,407 | 1,191 |
| Income tax expense | 771 | 291 |
| Net income | $ 1,636 | $ 900 |

| | Three Months Ended March 31, 2005 | 2004 |
|---|---|---|
| Selected Financial Ratios and Other Data: | | |
| Performance Ratios: | | |
| Return on assets (ratio of net income to average total assets) (1) | 0.44% | 0.25% |
| Return on equity (ratio of net income to average equity) (1) | 6.65 | 3.84 |
| Net interest rate spread (1) (2) | 2.99 | 2.69 |
| Net interest margin (1)(3) | 3.19 | 2.87 |
| Average equity to average assets | 6.60 | 6.41 |
| Efficiency ratio (4) | 82.15 | 90.08 |
| Noninterest expense to average total assets (1) | 2.88 | 2.96 |
| Average interest-earning assets to average interest-bearing liabilities | 110.21 | 109.82 |

| | At March 31, 2005 | At December 31, 2004 |
|---|---|---|
| Selected Financial Ratios and Other Data: | | |
| Asset Quality Ratios: | | |
| Nonperforming assets to total assets . | 0.41% | 0.44% |
| Nonperforming loans to total loans | 0.56 | 0.59 |
| Allowance for loan losses to nonperforming loans | 177.15 | 168.90 |
| Allowance for loan losses to total loans | 1.00 | 1.00 |
| Capital Ratios: | | |
| Equity to total assets at end of period | 6.62% | 6.36% |
| Tier 1 leverage ratio (bank only) | 7.24 | 7.12 |
| Other Data: | | |
| Number of full service offices | 16 | 16 |

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(1) Ratios for the three months ended March 31, 2005 and 2004 are annualized.

(2) The net interest rate spread represents the difference between the yield on average interest-earning assets and the cost of average interest-bearing liabilities for the period.

(3) The net interest margin represents net interest income divided by average total interest-earning assets for the period.

(4) The efficiency ratio represents noninterest expense divided by the sum of net interest income and noninterest income.

Comparison of Financial Condition at March 31, 2005 and December 31, 2004

Total assets increased $2.7 million, or 0.2%, to $1.495 billion at March 31, 2005, from $1.493 billion at December 31, 2004. The increase was primarily the result of an increase in the fair value of securities available for sale, offset by decreases in loans receivable, cash and cash equivalents and other assets.

Net loans receivable decreased by $1.6 million, or 0.1%, to $1.090 billion at March 31, 2005, from $1.092 billion at December 31, 2004. One- to four-family residential loans, which include home equity and other second mortgage loans, decreased $5.0 million, or 1.4%. Multi-family mortgage and non-residential real estate loans decreased $8.9 million, or 1.8%, primarily as a result of $18.6 million in loan pay-downs received during the quarter. Construction loans increased $8.9 million during the first quarter, or 14.8%, due to increased originations and improving weather conditions. Commercial loans and commercial leases increased a combined $4.0 million, or 2.2%, reflecting continued emphasis on originating loans of this type and increasing line of credit usage by commercial borrowers.

Net securities available-for-sale increased $6.4 million, or 2.4%, to $274.5 million at March 31, 2005, from $268.1 million at December 31, 2004. The increase was partially due to the securitization of $10.5 million of adjustable-rate, one- to four-family residential real estate loans, which was partially offset by $8.1 million of principal repayments received on mortgage-backed securities. In addition, the fair value of MHC's portfolio of Fannie Mae and Freddie Mac floating rate preferred stocks increased $5.4 million, or 7.0%, to $82.9 million at March 31, 2005, from $77.5 million at December 31, 2004, due to increases in the quoted market prices for certain of these securities.

Cash and cash equivalents remained relatively stable during the first quarter, decreasing by $718,000 to $28.6 million at March 31, 2005 from $29.3 million at December 31, 2004.

Other assets decreased by $1.8 million, or 12.1%, to $12.8 million at March 31, 2005, from $14.6 million at December 31, 2004. The decrease in other assets was primarily due to a decrease of $1.6 million in deferred tax assets that relates to the increase in the fair value of MHC's portfolio of Fannie Mae and Freddie Mac floating rate preferred stocks.

Deposits decreased $7.1 million, or 0.6%, to $1.109 billion at March 31, 2005, from $1.116 billion at December 31, 2004. Core deposits (savings, money market, noninterest bearing demand and NOW accounts) represented 60.9% of total deposits at March 31, 2005, compared to 60.5% of total deposits at December 31, 2004. Retail certificates of deposit decreased $1.1 million, or 0.3%, to $415.3 million at March 31, 2005, from $416.4 million at December 31, 2004. Brokered certificates of deposit decreased $5.8 million, or 24.2%, to $18.1 million at March 31, 2005, from $23.9 million at December 31, 2004.

Borrowings increased $7.3 million, or 2.8%, to $272.1 million at March 31, 2005, from $264.7 million at December 31, 2004. The increase was the result of additional usage of Federal Home Loan Bank borrowings during a period of deposit outflow, including the replacement of maturing brokered certificates of deposit with short-term Federal Home Loan Bank borrowings.

Total members' equity increased $4.1 million, or 4.3%, to $99.0 million at March 31, 2005, from $94.9 million at December 31, 2004. The increase in members' equity was primarily due to net income of $1.6 million for the three months ended March 31, 2005, and an increase in the fair value of securities available for sale. Total members' equity at March 31, 2005 reflected an unrealized gain on securities available for sale of $918,000, net of tax, compared to an unrealized loss on securities available-for-sale of $1.6 million, net of tax, at December 31, 2004. Substantially all of the unrealized gain was attributable to MHC's portfolio of Fannie Mae and Freddie Mac floating rate preferred stocks.

Comparison of Operating Results for the Three Months Ended March 31, 2005 and March 31, 2004

Net Income. MHC had net income of $1.6 million for the three months ended March 31, 2005, compared to net income of $900,000 for the three months ended March 31, 2004. The increase in net income is primarily attributable to a $1.4 million, or 13.7%, increase in net interest income.

Interest Income. Interest income increased $2.0 million, or 12.6%, to $18.0 million for the three months ended March 31, 2005, from $16.0 million for the three months ended March 31, 2004. The increase in interest income reflected a 47 basis point improvement in the average yield on interest-earning assets to 5.14% from 4.67%, and a $31.1 million, or 2.3%, increase in total average interest-earning assets.

Interest income from loans, the most significant portion of interest income, increased $1.8 million, or 13.2%, to $15.4 million for the three months ended March 31, 2005, from $13.6 million for the same period in 2004. The increase reflected a $22.8 million, or 2.1%, increase in the average balance of net loans receivable to $1.105 billion for the three months ended March 31, 2005, from $1.082 billion for the same period in 2004, and a 55 basis point increase in the average yield on loans to 5.58% for the three months ended March 31, 2005, compared to 5.03% for the three months ended March 31, 2004. The yields on construction and home equity loans are indexed on the prime rate. The quarterly yields of each of the these products has improved more than 100 basis points, which reflects the 175 basis points increase in the prime rate from March 2004 to March 2005. Interest income from one- to four-family residential real estate and multi-family mortgage loans increased $326,000, or 4.1%, to $8.3 million for the three months ended March 31, 2005, from $8.0 million for the three months ended March 31, 2004. Interest income from commercial loans and leases increased $644,000, or 25.2%, to $2.6 million for the three months ended March 31, 2005, from $1.9 million for the same period in 2004.

Interest income from securities available for sale increased $274,000, or 13.6%, to $2.3 million for the three months ended March 31, 2005, compared to $2.0 million for the three months ended March 31, 2004. The average yield on securities available for sale increased 20 basis points to 3.37% from 3.17%, and the average outstanding balance of securities available for sale increased $17.1 million, or 6.7%, to $271.4 million, from $254.3 million for the three months ended March 31, 2004.

Interest Expense. Interest expense increased $658,000, or 10.7%, to $6.8 million for the three months ended March 31, 2005, from $6.2 million for the three months ended March 31, 2004. The increase in the rate paid on average interest-bearing liabilities reflected an increase in the deposit rates paid to customers, which was offset by a decrease in the average rates paid on borrowings. The increase in interest expense reflected a 17 basis points increase in the rate paid on average interest-bearing liabilities to 2.15% for the three months ended March 31, 2005, from 1.98% for the three months ended March 31, 2004.

Interest expense on borrowings decreased by $693,000, or 22.7%, to $2.4 million for the three months ended March 31, 2005, from $3.1 million for the same period in 2004. The decrease in interest expense on borrowings was primarily the result of the lower yield adjustment amortization expense relating to MHC's restructuring of $170 million in Federal Home Loan Bank borrowings in July 2003. The yield adjustment amortization expense totaled $175,000, pre-tax, for the three months ended March 31, 2005, compared to $1.4 million, pre-tax, for the three months ended March 31, 2004. The decreased yield adjustment amortization expense was partially offset by a $5.9 million increase in average borrowings, and an increase in interest expense on the $30 million of term debt MHC incurred in connection with MHC's acquisition of Success Bancshares, Inc. in 2001. Interest expense on the term debt totaled $342,000 for the three months ended March 31, 2005, a $103,000, or 43.2%, increase over the $239,000 in interest expense on term debt for the same period in 2004.

Interest expense on deposits increased $1.4 million to $4.5 million for the three months ended March 31, 2005, from $3.1 million for the same period in 2004. The increase in interest expense on deposits reflected an $18.0 million, or 1.8%, increase in average interest-bearing deposits to $1.001 billion for the three months ended March 31, 2005, from $982.9 million for the same period in 2004. The increase in interest expense on deposits also reflected a 52 basis point increase in the average rate paid on deposits to 1.79% for the three months ended March 31, 2005, from 1.27% for the three months ended March 31, 2004. Interest expense increased for all categories of deposits. Interest expense on money market accounts increased $597,000, or more than 100%, reflecting an increase of $42.9 million in the average balance of money market accounts deposits to $205.5 million for the three months ended March 31, 2005, from $162.7 million for the three months ended March 31, 2004, and a 94 basis point increase in the rate paid on these accounts to 2.01% from 1.08%. MHC has $97.2 million in indexed money market accounts; the rates on these accounts have increased along with short-term market interest rates. Rates paid on certain NOW accounts, savings accounts and money market accounts were increased beginning in the third quarter of 2004 in response to increasing short-term market interest rates and anticipated increases in the rates paid by MHC's competitors. Rates on other selected money market products and certificates of deposit were also increased for competitive reasons. Interest expense on certificates of deposit increased $442,000, or 19.6%, reflecting an increase of 46 basis points to 2.47% from 2.01%, which was partially offset by a $12.8 million decrease in the average balance of certificates of deposit to $436.8 million for the three months ended March 31, 2005, from $449.6 million for the three months ended March 31, 2004.

Net Interest Income. Net interest income increased by $1.4 million, or 13.7%, to $11.2 million for the three months ended March 31, 2005, from $9.9 million for the three months ended March 31, 2004. The increase in net interest income reflected an improvement in MHC's net interest rate spread to 2.99% for the three months ended March 31, 2005, from 2.69% for the three months ended March 31, 2004. Net interest margin improved to 3.19% for the three months ended March 31, 2005, from 2.87% for the three months ended March 31, 2004.

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

Based on MHC's evaluation of the above factors, including a decline in the ratio of nonperforming loans to total loans to 0.56% at March 31, 2005, compared to 0.59% at December 31, 2004, MHC recorded a credit for loan losses of $76,000 for the three months ended March 31, 2005. No provision for loan losses was recorded for the three months ended March 31, 2004. The allowance for loan losses allocated to impaired loans decreased $134,000 to $1.9 million at March 31, 2005, compared to $2.1 million at December 31, 2004. The allowance for loan losses represented 177.15% of nonperforming loans at March 31, 2005, and 168.90% of nonperforming loans at December 31, 2004. The allowance for loan losses was $10.9 million, or 1.00%, of total loans at March 31, 2005, compared to $11.0 million, or 1.00%, of total loans at December 31, 2004. MHC used the same general methodology in evaluating the allowance at both dates.

To the best of MHC's knowledge, all losses that are both probable and reasonable to estimate for each reporting period have been recorded.

Noninterest Income. Noninterest income decreased $295,000 to $1.9 million for the three months ended March 31, 2005, from $2.1 million for the same period in 2004. The decrease is attributed to several factors, including decreases in commissions from insurance and annuities sales, decreased gains on loan and investment sales, and reduced income from real estate owned operations and other income. These decreases were partially offset by a $259,000 improvement in the amortization and impairment of mortgage servicing rights. Gain on sales of loans decreased $105,000, or 55.9%, to $83,000 for the quarter ended March 31, 2005, from $188,000 for the same period in 2004. Current quarter loan sales reflect $7.8 million of loan sale proceeds, compared to $17.8 million of loan sale proceeds for the same period in 2004. MHC had no gain on the sale of securities for the quarter ended March 31, 2005, compared to a gain of $258,000 for the quarter ended March 31, 2004.

Non-interest Expense. Noninterest expense was $10.7 million for the three months ended March 31, 2005, an improvement of $81,000, or 0.7%, compared to noninterest expense of $10.8 million for the three months ended March 31, 2004. Total non-interest expense includes $6.9 million in compensation and benefits expense for the quarter ended March 31, 2005, compared to $6.8 million in compensation and benefits expense for the same period in 2004.

Income Tax Expense. MHC recorded income tax expense of $771,000 for the three months ended March 31, 2005, compared to $291,000 for the three months ended March 31, 2004. The effective tax rates for the three-month periods ended March 31, 2005 and 2004 were 32.0% and 24.4%, respectively.