FIRST DEFIANCE FINANCIAL CORP
Form 10-K
March 13, 2006

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, 2005

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:
None

Securities registered pursuant to Section 12(g) of the Act:
Common Stock, Par Value $0.01 Per Share
(Title of class)

Indicate by check mark if the registrant is a well-known seasoned issued, 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 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. |X|

Indicate by check mark whether the Registrant is an accelerated filer (as defined in Rule 12b-2 of the Act) Yes |X| No |_|

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes |_| No |X|

As of March 3, 2006, there were issued and outstanding 7,152,942 shares of the Registrant's common stock.

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, 2005 was approximately $175.5 million

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Documents Incorporated by Reference

Part II and Part III - Portions of the Proxy Statement for the Annual Meeting of Shareholders to be held on April 18, 2006 are incorporated by reference into Part II and III thereof.

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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 (the Subsidiaries), focuses on traditional banking and property and casualty, life and group health insurance products. The Company's traditional banking activities include originating and servicing residential, commercial, and consumer loans and providing a broad range of depository services. The Company's insurance activities consist primarily of commissions relating to the sale of property and casualty, life and group health insurance and investment products.

At December 31, 2005, the Company had consolidated assets of $1.461 billion, consolidated deposits of $1.070 billion, and consolidated stockholder's equity of $151.2 million. The Company was incorporated in Ohio in June of 1995. Its principal executive offices are located at 601 N. Clinton Street, Defiance, Ohio 43512, and its telephone number is (419) 782-5015.

First Defiance's Internet site, 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 SEC

The Subsidiaries

The Company's core business operations are conducted through the following

Subsidiaries:

First Federal Bank of the Midwest: First Federal Bank of the Midwest (First Federal) is a federally chartered stock savings bank headquartered in Defiance, Ohio. As of December 31, 2005, it conducts operations through its main office and 25 full service branch offices in Allen, Defiance, Fulton, Hancock, Henry, Lucas, Ottawa, Paulding, Putnam, Seneca, Williams and Wood Counties in northwest Ohio.

On January 21, 2005, First Defiance completed the acquisition of ComBanc, Inc. (ComBanc) and its subsidiary, the Commercial Bank, Delphos, Ohio. That acquisition added four branch offices located in Allen County, Ohio which is adjacent to First Defiance's existing footprint. On April 8, 2005, First Defiance completed the acquisition of the Genoa Savings and Loan Company, (Genoa) which added three offices in the metropolitan Toledo, Ohio area.

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

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First Insurance & Investments: First Insurance & Investments (First Insurance) is a wholly owned subsidiary of First Defiance. First Insurance is an insurance agency that does business in the Defiance, Ohio area. First Insurance offers property and casualty insurance, life insurance, group health insurance, and investment products.

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, the Chief Operating Officer, and the Chief Executive Officer of First Federal can each approve transactions up to $1 million. Two of the three officers are required to approve transactions between $1 million and $5 million. All transactions in excess of $5 million must be approved by the Board of Directors.

First Defiance's investment portfolio includes 19 CMO and REMIC issues totaling $21.0 million, all of which are fully amortizing securities. All such investments are considered derivative securities. None of the securities are considered to be "high risk" based on the stress test developed by the banking regulators. Management does not believe the risks associated with any of these investments are significantly different from risks associated with other pass-through mortgage-backed securities. First Defiance does not invest in off-balance sheet derivative securities.

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 amortized cost and fair value of securities at December 31, 2005 by contractual maturity are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. Money market mutual funds and other mutual funds are not due at a single maturity date. 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						
	Under 1 Year	Weighted Average Rate	1 - 5 Years	Weighted Average Rate	6-10 Years	Weighted Average Rate	Over 1 Years
				(Dollars in Thousands)			
Mortgage-backed securities	$ 3,590	4.80%	$ 10,394	4.81%	$ 5,436	4.88%	$ 1,7
REMICs and CMOs	4,303	4.21	11,620	4.45	4,749	4.67	3
U.S. government and federal agency obligations	6,000	3.46	33,550	4.60	1,570	4.84	
Obligations of states and political subdivisions (1)	745	6.64	5,885	6.23	5,698	6.47	10,9
Trust preferred stock	--		--		--		7,7
Total	$ 14,638		$ 61,449		$ 17,453		$ 20,8
Unamortized premiums/ (discounts)							
Unrealized loss on securities available for sale							
Total							

(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		
	2005	2004	2003

	(In Thousands)		
Available-for-sale securities:			
Corporate bonds	$ --	$ 6,468	$ 7,716
U. S. treasury and federal agency obligations	41,065	50,313	76,875
Obligations of state and political subdivisions	23,818	32,092	32,835
CMOs, REMICS and mortgage-backed securities	40,395	41,765	43,433
Other	7,801	6,365	7,400
Total	$ 113,079	$ 137,003	$ 168,259
Held-to-maturity securities:			
Mortgage-backed securities	$ 1,330	$ 1,725	$ 2,186
Obligations of state and political subdivisions	445	530	590
Total	$ 1,775	$ 2,255	$ 2,776

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

Interest-Bearing Deposits

First Defiance had interest-earning deposits in the FHLB of Cincinnati amounting to $8.1 million and $456,000 at December 31, 2005 and 2004, 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, 2005, First Federal serviced 7,511 loans totaling $602.5 million. The vast majority of the loans serviced for others are fixed rate conventional mortgage loans.

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

The following table shows the delinquency statistics for the mortgage loans serviced by the Company as of the dates presented.

December 31		
2005	2004	20

	Number of Loans	Percentage of Servicing Portfolio	Number of Loans	Percentage of Servicing Portfolio	Number of Loans
Loans delinquent for:					
30-59 days	22	0.29%	9	0.16%	2
60-89 days	7	0.09	3	0.05	1
90 days and over	16	0.21	6	0.11	5
Total delinquencies	45	0.60%	18	0.32%	8
Foreclosures	14	0.19%	5	0.09%	2

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					
	2005			2004		
Rate	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 5.00%	865	$ 74,784	12.41%	770	$ 72,321	15.59%
5.00% - 5.99%	3,689	310,665	51.56	2,881	244,842	52.79
6.00% - 6.99%	2,356	19,0172	31.56	1,609	126,132	27.20
7.00% - 7.99%	465	21,766	3.61	383	17,810	3.84
8.00% - 8.99%	108	4,483	0.74	63	2,503	0.54
9.00% and over	28	641	0.10	4	182	0.04
Total	7,511	$602,511	100.00%	5,710	$463,790	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.

	2005				2004		
Maturity	Number of Loans	% of Number of Loans	Unpaid Principal Amount	% of Unpaid Principal Amount	Number of Loans	% of Number of Loans	Unp Prin Amo

(Dollars in Thousands)

1-5 years	546	7.27%	$ 40,710	6.76%	392	6.88%	$ 3
6-10 years	602	8.01	27,965	4.64	614	10.75	4
11-15 years	2,573	34.26	177,564	29.47	2,122	37.16	15
16-20 years	1,006	13.39	83,444	13.85	787	13.78	6
21-25 years	207	2.76	17,254	2.86	107	1.87	
More than 25 years	2,577	34.31	255,574	42.42	1,688	29.56	16
Total	7,511	100.00%	$602,511	100.00%	5,710	100.00%	$46

	2003			
Maturity	Number of Loans	% of Number of Loans	Unpaid Principal Amount	% of Unpaid Principal Amount
	(Dollars in Thousands)			
1-5 years	302	5.61%	$ 22,838	5.27%
6-10 years	673	12.49	47,819	11.04
11-15 years	2,130	39.54	156,847	36.21
16-20 years	762	14.15	66,135	15.27
21-25 years	74	1.37	5,147	1.19
More than 25 years	1,446	26.84	134,347	31.02
Total	5,387	100.00%	$433,133	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 securities. 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, 2005, First Federal's limit on loans-to-one borrower was $20.0 million and its five largest loans (including available lines of credit) or groups of loans to one borrower, including related entities, were $16.9 million, $15.5 million, $11.3 million, $8.2 million and $8.2 million. All of these loans or groups of loans were performing in accordance with their terms at December 31, 2005.

Loan Portfolio Composition - The net increase in net loans receivable over the prior year was $285.6 million, $143.7 million, and $174.2 million in 2005, 2004, and 2003, respectively. First Defiance acquired net loans of $117.5 million in the ComBanc acquisition and $66.9 million in the Genoa acquisition. The loan portfolio contains no foreign loans nor any concentrations to identified borrowers engaged in the same or similar industries exceeding 10% of total loans.

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

	December 31				
	2005		2004		20
	Amount	%	Amount	%	Amount
	(Dollars in Thousands)				
Real estate:					
One to four family residential	$ 275,497	23.2%	$ 187,775	20.9%	$ 162,111
Five or more family residential	50,040	4.2	39,049	4.4	30,322
Nonresidential real estate	501,943	42.2	376,115	42.0	311,101
Construction	21,173	1.8	15,507	1.7	16,830
Total real estate loans	848,653	71.4	618,446	69.0	520,364
Other:					
Consumer finance	54,657	4.6	45,213	5.1	39,808
Commercial	171,289	14.4	141,644	15.8	120,677
Home equity and improvement	113,000	9.5	90,839	10.1	70,038
Mobile home	640	.1	299	--	449
Total non-real estate loans	339,586	28.6	277,995	31.0	230,972
Total loans	1,188,239	100.0%	896,441	100.0%	751,336
Less:					
Loans in process	8,782		6,341		6,079
Deferred loan origination fees	1,303		1,232		1,158
Allowance for loan losses	13,673		9,956		8,844
Net loans	$1,164,481		$ 878,912		$ 735,255

	December 31			
	2002		2001	
	Amount	%	Amount	%
	(Dollars in Thousands)			
Real estate:				
One to four family residential	$ 142,355	24.7%	$ 167,092	32.8%
Five or more family residential	32,324	5.6	21,757	4.3
Nonresidential real estate	195,431	33.9	152,274	29.9
Construction	15,357	2.6	7,875	1.5
Total real estate loans	385,467	66.8	348,998	68.5
Other:				

Consumer finance	37,562	6.5	40,721	8.0
Commercial	104,070	18.0	83,690	16.4
Home equity and improvement	49,889	8.7	36,179	7.1
Mobile home	17	--	12	--
Total non-real estate loans	191,538	33.2	160,602	31.5
Total loans	577,005	100.0%	509,600	100.0%
Less:				
Loans in process	7,255		2,887	
Deferred loan origination fees	1,212		1,024	
Allowance for loan losses	7,496		6,548	
Net loans	$ 561,042		$ 499,141	

In addition to the loans reported above, First Defiance had $5.2 million, $2.3 million, $5.9 million, $15.3 million and $672,000 in loans classified as held for sale at December 31, 2005, 2004, 2003, 2002 and 2001, 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, 2005 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.

	Due Before December 31		Due 3-5	Due 5-10	Due 10-
			Years After December		
	2006	2007	2005	2005	2005
			(In Thousands)		
Real estate	$ 149,864	$ 59,133	$ 149,742	$ 363,642	$ 55,2
Nonreal estate:					
Commercial	91,203	25,436	43,518	10,561	4
Home equity and improvement	8,926	2,385	25,120	6,999	7
Mobile home	122	87	260	148	
Consumer finance	24,437	12,513	16,832	755	1
Total	$ 274,552	$ 99,554	$ 235,472	$ 382,105	$ 56,5

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, 2005 which have fixed interest rates or which have floating or adjustable interest rates.

	Fixed Rates	Floating or Adjustable Rates	Total
		(In Thousands)	
Real estate	$ 170,919	$ 533,031	$ 703,950
Commercial	19,108	60,977	80,085
Other	57,269	77,545	134,814
	$ 247,296	$ 671,553	$ 918,849

Originations, Purchases and Sales of Loans - The lending activities of First Defiance 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, builders, and existing customers; newspapers and radio advertising; and walk-in customers.

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

A commercial loan application is first reviewed and underwritten by one of the commercial loan officers, who may approve credits within their lending limit. Another loan officer with limits sufficient to cover the exposure must approve credits exceeding an individual's lending limit. All credits which exceed $100,000 in aggregate exposure must be presented for review or approval to the Senior Loan Committee comprised of senior lending personnel. Credits which exceed $1,000,000 in aggregate exposure must be presented for approval to the Executive Loan Committee, a committee of First Federal's Board of Directors.

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 any authorized lending limit or outside of policy must be approved by Senior Loan Committee and if necessary by the Executive Loan Committee. Indirect consumer loans originated by auto dealers are underwritten and approved by a designated underwriter in accordance with company policy and lending limits.

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

Adjustable-rate loans represented 17.3% of First Defiance's total originations of mortgage loans in 2005 compared to 22.1% and 14.71% during 2004 and 2003, respectively.

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

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

	Years Ended December 31		
	2005	2004	2003
	(In Thousands)		
Loan originations:			
Single family residential	$ 164,687	$ 132,463	$ 291,481
Multi-family residential	85,733	76,483	58,370
Non-residential real estate	162,823	137,524	165,164
Construction	27,637	20,983	20,553
Commercial	133,021	110,915	104,007
Home equity and improvement	34,221	38,552	38,150
Consumer finance	50,056	27,250	19,366
Total loans originated	658,178	544,170	697,091
Loans acquired in acquisitions	184,218	--	79,094
Loan reductions:			
Loan pay-offs	261,046	223,976	222,163
Mortgage loans sold	111,345	104,968	293,673
Periodic principal repayments	181,630	70,566	83,879
	554,021	399,510	599,715
Net increase in total loans	$ 288,375	$ 144,660	$ 176,470

The loans acquired in the Genoa acquisition by category were as follows (excluding mark to market adjustments): Single family residential - $36.3 million, multi-family residential - $719,000, non-residential real estate - $7.5 million, construction - $4.5 million, commercial - $1.7 million, home equity and improvement - $13.4 million and consumer finance - $3.7 million.

The loans acquired in the ComBanc acquisition by category were as follows (excluding mark to market adjustments): Single family residential - $33.1 million, multi-family residential - $2.8 million, non-residential real estate - $57.2 million, construction - $1.9 million, commercial - $12.7 million, home equity and improvement - $4.6 million and consumer finance - $7.2 million.

The loans acquired in the 2003 branch acquisition by category were as follows: Single family residential - $21.4 million, non-residential real estate

- $35.4 million, commercial - $16.8 million, home equity and improvement - $1.8 million and consumer finance - $3.6 million.

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, 2005, 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 Ov	
	Amount	Percentage	Amount	Percentage	Amount	Perce
			(Dollars in Thousands)			
Single - family residential	$ 6,002	0.51%	$ 2,832	0.24%	$ 1,495	0.
Nonresidential and Multi-family residential	3,565	0.30	7,526	0.64	2,533	0.
Home equity and improvement	1,191	0.10	301	0.03	281	0.
Consumer finance	614	0.05	145	0.01	356	0.
Commercial	571	0.05	496	0.04	287	0.
Total	$11,943	1.02%	$11,300	0.70%	$ 4,952	0.

Nonperforming Assets - All loans are reviewed on a regular basis and are placed on a non-accrual status when, in the opinion of management, the collectibility of additional interest is deemed insufficient to warrant further accrual. Generally, First Defiance places all loans more than 90 days past due on non-accrual status. When a loan is placed on nonaccrual status, total unpaid interest accrued to date is reversed. Subsequent payments are either applied to the outstanding principal balance or recorded as interest income, depending on the assessment of the ultimate collectibility 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 creating a valuation allowance.

Impaired loans acquired in the ComBanc and Genoa acquisitions have been accounted for under the provisions of AICPA Statement of Position 03-3 - Accounting for Certain Loans or Debt Securities Acquired in a Transfer. Such loans were recorded at their fair value, which was estimated based on the expected cash flow of the acquired loan. In the Genoa acquisition, 10 loan relationships with a stated value of $1.5 million were recorded at $735,000. In the ComBanc acquisition, 13 loan relationships with a stated value of $3.4 million were recorded at $2.1 million. At December 31, 2005, those loans had a contractual balance of $4.6 million and were recorded at $2.6 million. If management expectations about the cash flow of those loans changes over time, the difference will be treated as "accretable" and will be recognized as a yield adjustment over the remaining life of the respective loan. There were no significant changes in the expected cash flows of the 23 loans identified as impaired in the acquisitions during 2005.

Loans originated by First Federal having recorded investments of $822,000, $505,000, and $563,000 were considered impaired as of December 31, 2005, 2004 and 2003, respectively. These amounts exclude large groups of small-balance homogeneous loans that are collectively evaluated for impairment such as residential mortgage, consumer installment, and credit card loans. There was $61,000 of interest received and recorded in income during 2005 related to impaired loans. There was $36,000 and $29,000 recorded in 2004 and 2003 respectively. Unrecorded interest income based on the loan's contractual terms on these impaired loans and all non-performing loans in 2005, 2004 and 2003 was $235,000, $102,000, and $73,000, respectively. The average recorded investment in impaired loans during 2005, 2004 and 2003 (excluding loans accounted for under SOP 03-3) was $1.1 million, $732,000 and $892,000, respectively. The total allowance for loan losses related to these loans was $380,000, $253,000, and $297,000 at December 31, 2005, 2004 and 2003, 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 the lower of the restated loan balance, less any allowance for loss, or fair value. 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 an allowance for losses is established by a charge to operations if the carrying value of property exceeds its estimated net realizable value.

As of December 31, 2005, First Defiance's total non-performing loans amounted to $5.0 million or .42% of total loans, compared to $1.9 million or 0.21% of total loans, at December 31, 2004. Non-performing loans are loans which are more than 90 days past due and are all classified as non-accrual at December 31, 2005. The nonperforming loan balance includes $1.9 million of loans originated by First Federal also considered impaired and $3.1 million of acquired loans accounted for under SOP 03-3.

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				
	2005	2004	2003	2002	20
	(Dollars in Thousands)				
Nonperforming loans:					
Single-family residential	$ 2,648	$ 419	$ 471	$ 404	$ 1,
Nonresidential and multi-family residential real estate	1,917	1,014	1,092	1,217	
Commercial	287	450	949	879	
Mobile home	--	--	--	--	
Consumer finance	100	10	33	25	
Total nonperforming loans	4,952	1,893	2,545	2,525	2,
Real estate owned	315	49	397	175	
Other repossessed assets	89	49	7	31	
Total repossessed assets	404	98	404	206	
Total nonperforming assets	$ 5,356	$ 1,991	$ 2,949	$ 2,731	$ 2,
Troubled debt restructurings	$ --	$ --	$ --	$ --	$
Total nonperforming assets as a percentage of total assets of continuing operations	0.37%	0.18%	0.28%	0.31%	0
Total nonperforming loans and troubled debt restructurings as a percentage of total loans	0.42%	0.21%	0.34%	0.43%	0
Allowance for loan losses as a percent of total nonperforming assets	255.28%	500.05%	299.90%	274.48%	259

In addition to the $5.4 million of loans reported above and $3.0 million of loans considered impaired (including loans accounted for under SOP 03-3), which are not included in the loans reported above, there are approximately $46.2 million of performing loans where known information about possible credit problems of the borrowers causes management to have doubts as to the ability of such borrowers to comply with the present loan repayment terms and which may result in the inclusion of such loans in non-performing loans at some future date. In analyzing these loans for the purpose of determining the adequacy of the allowance for loan losses, management has determined that these loans generally have significant collateral, strong guarantors, or both.

Allowance for Loan Losses - First Defiance maintains an allowance for loan losses to absorb probable losses in the loan portfolio. The balance of the allowance is based upon an assessment of prior loss experience, the volume and type of lending conducted by First Defiance, industry standards, past due loan amounts and trends, general economic conditions and other factors related to the collectibility of the loan portfolio. The Company principally uses its own loss experience in calculating its loan loss provision. However, in those instances where the Company's experience with certain types of lending is new or recent and therefore historical losses are less meaningful, management will consider such other factors as industry loss statistics, regulatory guidance, experience of other financial institutions operating in the same geographic area, and inherent risks associated with the borrower in determining the required allowance. In evaluating the adequacy of its allowance each quarter, management grades all loans in the commercial portfolio using a scale of one to ten. Loans graded in the three worst categories (substandard, doubtful and loss) generally are specifically reserved for. Loans graded as substandard would generally have reserves

that range between zero and 20% based on management's knowledge of the credit and other local factors. Substandard loans that have no reserves allocated to them generally exhibit negative financial characteristics, such as poor cash flow or declining sales, but have offsetting credit strengths, such as an abundance of collateral or the existence of a strong guarantor. Loans classified as doubtful are generally reserved at 50% and loans classified as loss are reserved at 100%, unless other facts and circumstances, such as strength of collateral or strength of guarantors warrant a different percentage. Management also engages a third-party to perform an independent loan review on a semi-annual basis. That third party reviews all loan relationships in excess of $250,000 and, among other things, challenges management's loan grades.

Loans charged-off are charged against the allowance when such loans meet the Company's established policy on loan charge-offs and the allowance itself is adjusted quarterly by recording a provision for loan losses. As such, actual losses and losses provided for should be approximately the same if the overall quality, composition and size of the portfolio remains static. To the extent that the portfolio grows at a rapid rate, such as the Company has experienced, or overall quality deteriorates, the provision generally will exceed charge-offs. 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, 2005, First Defiance's allowance for loan losses amounted to $13.7 million compared to $10.0 million at December 31, 2004. The following table sets forth the activity in First Defiance's allowance for loan losses during the periods indicated.

	Years Ended D		
	2005	2004	200
		(Dollars in	
Allowance at beginning of year	$ 9,956	$ 8,844	$ 7,
Provision for credit losses	1,442	1,549	1,
Allowance acquired in acquisitions	3,027	--	
Charge-offs:			
One to four family residential real estate	182	52	
Commercial real estate	226	58	
Commercial	267	390	
Consumer finance	354	186	
Home equity and improvement	25	--	
Total charge-offs	1,054	686	
Recoveries	302	249	

Net charge-offs	752	437	
Ending allowance	$ 13,673	$ 9,956	$ 8,
Allowance for loan losses to total non-performing loans at end of year	276.11%	525.94%	347
Allowance for loan losses to total loans at end of year	1.16%	1.12%	1
Allowance for loan losses to net charge-offs for the year	1,813.40%	2,278.26%	2,383
Net charge-offs for the year to average loans	0.07%	0.05%	0

The provision for credit losses has remained stable over the five-year period shown in the above table as the Company's loss experience has remained relatively low despite significant growth in the loan portfolios. The loan loss reserve increased significantly in 2005 because of reserves acquired in the acquisitions. The level of charge-offs increased in 2005 because of activity related primarily to acquired loans. Management anticipates that the level of charge-offs will remain higher than historical levels as non-performing loans acquired in the two acquisitions are charged off. Management also believes the level of loan loss reserves acquired in the acquisitions is sufficient to cover anticipated charge-offs of the acquired loans.

The percentage of the allowance for loan losses to total loans increased in 2005 because of the allowance recorded for the loan balances acquired was at a higher overall percentage than First Defiance's existing portfolio. Non-performing assets increased to $5.4 million at December 31, 2005 from $2.0 million at December 31, 2004, because of non-performing loans acquired in the acquisitions. Management believes all non-performing loans acquired had adequate allowance for loan losses allocations. No non-performing loans have been identified since the acquisition dates that were not adequately reserved for as of those dates. Historical trends are monitored by management on a quarterly basis and are considered in the establishment of the allowance for loan losses.

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."

	December 31					
	2005		2004		2003	
	Amount	Percent of total loans by category	Amount	Percent of total loans by category	Amount	Pe to by
Single family residential	$ 1,484	23.2%	$ 239	22.8%	$ 386	
Nonresidential and Multi-family residential real estate	8,965	46.4	6,538	46.3	6,265	
Other:						
Commercial loans	2,287	14.4	2,454	15.8	1,424	

Consumer and home equity and improvement loans	937	16.0	725	15.1	769
	$13,673	100.0%	$ 9,956	100.0%	$ 8,844

	December 31			
	2002		2001	
	Amount	Percent of total loans by category	Amount	Percent of total loans by category
	(Dollars in Thousands)			
Single family residential	$ 587	29.2%	$ 613	34.4%
Nonresidential and Multi-family residential real estate	4,293	38.5	2,847	34.1
Other:				
Commercial loans	1,729	17.6	1,734	16.4
Consumer and home equity and improvement loans	887	14.7	1,354	15.1
	$ 7,496	100.0%	$ 6,548	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 2005, First Defiance issued $20.0 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.

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, regular savings accounts, and term certificate accounts. Deposit account terms vary, with the principal differences being the minimum balance required, the time periods the funds must remain on deposit, and the interest rate.

To supplement its funding needs, First Defiance also utilizes brokered Certificates of Deposit. Such deposits, which were primarily acquired in prior years to fund operations now discontinued, have maturities ranging from three months to one year. The total balance of brokered certificates of deposit was

$37.0 million at December 31, 2005. Brokered CDs at December 31, 2004 totaled $61.2 million.

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

	Years Ended December 31					
	2005		2004		2003	
	Amount	Rate	Amount	Rate	Amount	Rate
	(Dollars in Thousands)					
Non-interest-bearing demand deposits	$ 86,741	--	$ 56,241	--	$ 47,505	--
Interest bearing demand deposits	273,502	1.19%	232,044	0.74%	198,039	0.74%
Savings deposits	87,708	0.27	53,247	0.25	47,047	0.36
Time deposits	570,826	3.00	413,796	2.68	387,948	3.04
Totals	$1,018,777	2.02%	$ 755,328	1.71%	$ 680,539	1.97%

The following table sets forth the maturities of First Defiance's certificates of deposit having principal amounts of $100,000 or more at December 31, 2005 (in thousands):

Certificates of deposit maturing in quarter ending:	
March 31, 2006	$ 47,167
June 30, 2006	42,996
September 30, 2006	35,927
December 31, 2006	20,012
After December 31, 2006	37,003
Total certificates of deposit with balances of $100,000 or more	$ 183,105

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

	2005	2004
	(In Thousands)	
Interest bearing demand deposits and money market accounts	$ 120	$ 58
Savings Accounts	--	--
Certificates	876	432
	$ 996	$ 490

For additional information regarding First Defiance's deposits see Note 10 to the financial statements.

Borrowings-- First Defiance may obtain advances from the FHLB of Cincinnati upon the security of the common stock it owns in that bank and certain of its residential mortgage loans, non-residential loans and investment securities provided certain standards related to creditworthiness have been met. Such advances are made pursuant to several credit programs, each of which has its own interest rate and range of maturities.

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

	December 31		
	2005	2004	2003
	(Dollars in Thousands)		
Long-term:			
FHLB advances	$ 152,460	$ 151,713	$ 153,522
Weighted average interest rate	4.65%	4.62%	4.60%
Short-term:			
FHLB advances	$ 28,500	$ 26,500	$ 11,000
Weighted average interest rate	3.65%	2.20%	1.12%
Revolving borrowings	--	3,000	--
Weighted average interest rate	--	2.25%	--
Securities sold under agreement to repurchase	$ 25,748	$ 11,804	$ 12,267
Weighted average interest rate	2.67%	1.57%	0.85%

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		
	2005	2004	2003
	(Dollars in Thousands)		
Long-term:			
FHLB advances:			
Maximum balance	$ 154,602	$ 153,373	$ 154,930
Average balance	153,267	152,547	152,939
Weighted average interest rate	4.63%	4.61%	4.78%
Term Borrowings:			
Maximum balance	--	--	$ 7
Average balance	--	--	1
Weighted average interest rate	--	--	7.50%

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

	2005	2004	2003
	(Dollars in Thousands)		
Short-term:			
FHLB advances:			
Maximum balance	$ 45,000	$ 28,500	$ 14,250
Average balance	14,313	15,577	2,296
Weighted average interest rate	3.79%	1.55%	1.31%
Revolving credit agreements:			
Maximum balance	$ 43,799	$ 3,000	$ --
Average balance	301	1,349	--
Weighted average interest rate	2.25%	2.20%	--
Securities sold under agreement to repurchase:			
Maximum balance	$ 25,748	$ 12,606	$ 12,860
Average balance	17,718	10,612	7,569
Weighted average interest rate	2.18%	1.08%	1.02%

First Defiance borrows funds under a variety of programs at the FHLB. As of December 31, 2005, there was $152.5 million outstanding under various long-term FHLB advance programs. First Defiance utilizes short-term advances from the FHLB to meet cash flow needs and for short-term investment purposes. There were $28.5 million and $26.5 million in short-term advances outstanding at December 31, 2005 and 2004, respectively. At December 31, 2005, $28.5 million was outstanding under First Defiance's REPO advance line of credit. The total available under the line is $100.0 million. Additionally, First Defiance has $15.0 million available under a Cash Management advance 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, non-mortgage loans, cash and investment securities. At December 31, 2005, irregardless of amounts available on the REPO and Cash Management line, First Federal's additional borrowing capacity with the FHLB was $24.1 million due to these collateral requirements.

As a member of the FHLB of Cincinnati, First Federal must maintain a minimum investment in the capital stock of that FHLB in an amount defined in the FHLB's regulations. First Federal is permitted to own stock in excess of the minimum requirement and is in compliance with the minimum requirement with an investment in stock of the FHLB of Cincinnati of $17.5 million at December 31, 2005.

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. All long-term advances by each FHLB must be made only to provide funds for residential housing finance.

For additional information regarding First Defiance's FHLB advances and other debt see Notes 11, 12 and 13 to the financial statements.

Subordinated Debentures - In October 2005, the Company formed an affiliated trust, First Defiance Statutory Trust I (the Trust Affiliate), that issued $20 million of Guaranteed Capital Trust Securities (Trust Preferred Securities). In connection with the transaction, the Company issued $20.6

million of Junior Subordinated Deferrable Interest Debentures (Subordinated Debentures) to the Trust Affiliate. The Trust Affiliate 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 the Trust Affiliate are the sole assets of the trust. Distributions on the Trust Preferred Securities issued by the Trust Affiliate are payable quarterly at a variable rate equal to the three-month LIBOR rate plus 1.38%, or 5.87% as of December 31, 2005.

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

Employees

First Defiance had 476 employees at December 31, 2005. None of these employees are represented by a collective bargaining agent, and First Defiance believes that it enjoys good relations with its personnel.

Competition

Competition in originating loans arises mainly from other savings associations, commercial banks, and mortgage companies. The distinction among market participants is based primarily on price and, to a lesser extent, 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 mortgage brokers and borrowers than is furnished by competitors. However, First Federal does have a significant market share of the lending markets in which it conducts operations.

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

Regulation

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

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

Regulatory Capital Requirements - First Federal is required by OTS regulations to meet certain minimum capital requirements. Current capital requirements call for tangible capital of 1.5% of adjusted total assets, core capital of 4.0% of adjusted total assets, except for associations with the highest examination rating and acceptable levels of risk, and risk-based capital of 8% of risk-weighted assets.

The following table sets forth the amount and percentage level of regulatory capital of First Federal at December 31, 2005, and the amount by which it exceeds the minimum capital requirements. Tangible and core capital are reflected as a percentage of adjusted total assets. Total (or risk-based) capital, which consists of core and supplementary capital, is reflected as a percentage of risk-weighted assets. Assets are weighted at percentage levels ranging from 0% to 100% depending on their relative risk.

	December 31, 2005	
	(In Thousands)	
Tangible Capital	$ 120,029	8.46%
Requirement	21,273	1.50
Excess	$ 98,756	6.96%
Core Capital	$ 120,029	8.46%
Requirement	56,729	4.00
Excess	$ 63,300	4.46%
Total risked-based capital	$ 133,636	11.84%
Risk-based requirement	90,323	8.00
Excess	$ 43,313	3.84%

First Federal's capital at December 31, 2005, meets the standards for a well-capitalized institution.

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 4350(h), including loans made by financial institutions in the ordinary course of business. All transactions between savings associations and their affiliates must comport with Sections 23A and 23B of the Federal Reserve Act (FRA) and the Federal Reserve Board'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 is an affiliate of First Federal.

Holding Company Regulation - First Defiance is a unitary thrift holding company and is subject to OTS 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 OTS, 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. If First Defiance were to acquire control of another savings institution, other than through a merger or other business combination with First Federal, First Defiance would become a multiple thrift holding company and its activities would thereafter be limited generally to those activities authorized by the FRB as permissible for bank holding companies.

Item 1A. Risk Factors

Interest Rate Risk

Our earnings and financial condition are dependent to a large degree upon net interest income, which is the difference between interest earned from loans and investments and interest paid on deposits and borrowings. The narrowing of the spread between interest earned on loans and investments and interest paid on deposits and borrowings could adversely affect our earnings and financial condition.

Interest rates are highly sensitive to many factors including:

- The rate of inflation;
- Economic conditions;
- Federal monetary policies;
- Stability of domestic and foreign markets.

Changes in market interest rates will also affect the level of prepayments on loans as well as the payments received on mortgage backed securities, requiring the reinvestment at lower rates than the loans or securities were paying.

First Federal Bank originates a significant amount of residential mortgage loans for sale and for our portfolio. The origination of residential mortgage loans is highly dependent on the local real estate market and the level of interest rates. Increasing interest rates tend to reduce the origination of loans for sale and consequently fee income, which we report 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, we may be required to write down the value of our mortgage servicing rights faster than anticipated, which will increase our expense and lower our earnings.

Credit Risk

Our earnings and financial condition may be adversely affected if we fail to adequately manage our credit risk. Our primary business is the origination and underwriting of loans. This business requires us to take "credit risk" which is the risk of losing principal and interest income because borrowers fail to repay their loans. The ability of borrowers to repay their loans and the value of collateral securing such loans may be affected by a number of factors including:

- A slowdown in the local economy of our market area or the national economy;
- A downturn in the business sector in which our loan customer operates;
- A rapid increase in interest rates.

Economy

We operate our banking and insurance business units within the geographic area comprised of the northwest corner of the state of Ohio and adjacent counties in Indiana and Michigan. Weaknesses in this geographic market area could be caused by such factors as an increase in the unemployment rate, a decrease in real estate values, or significant increases in interest rates. Any such weakness could have a negative impact on our earnings and financial condition because:

- Demand for our products and services may go down;
- Borrowers may be unable to make payments on their loans;
- The value of collateral securing loans may decline;
- The overall quality of the loan portfolio may decline.

Competition

Competition in our market area may reduce our ability to originate loans and attract and retain deposits. We face competition both in originating loans and attracting deposits. Competition is intense in the financial services industry. We compete in our market area by offering superior service and competitive rates and products. The type of institutions we compete 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 our competitors can offer a broader range of products and services than we offer. To stay competitive in our market area, we may need to adjust the interest rates on our products to match rates of our competition, which will have a negative impact on our net interest margin. Our continued profitability depends on our ability to continue to effectively compete in our market areas.

Government Regulation

Our business may be adversely affected by changes in the regulatory environment or by changes in government policies as a whole. The earnings of financial institutions such as First Defiance and First Federal are affected by the policies of the regulatory authorities, including the Federal Reserve Board, which regulates the money supply, and the Office of Thrift Supervision, which regulates unitary thrift holding companies such as First Defiance and savings banks such as First Federal.

Among the methods employed by the Federal Reserve Board are open market operations in U.S. Government securities, changes in the discount rate on member bank borrowings, and changes in the reserve requirement against member bank deposits. These tools are utilized by the Federal Reserve in varying combinations to influence overall growth and distribution of bank loans, investments and deposits and they have a significant impact on interest rates charged on loans and paid on deposits. The influence of the monetary policies of the Federal Reserve Board are expected to have a continuing and profound effect on the operating results of commercial and savings banks.

Policies, administration guidelines, and regulatory practices of the Office of Thrift Supervision and other banking regulators have a significant impact on the operations of First Federal and First Defiance. It is possible that certain of those regulations will negatively impact the Company's operating results or financial condition.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

At December 31, 2005, First Federal conducted its business from its main office at 601 Clinton Street, Defiance, Ohio, and eighteen other full service banking centers in northwestern Ohio. First Insurance conducted its business from leased office space at 419 5th Street, Suite 1200, Defiance, Ohio.

First Defiance maintains its headquarters in the main office of First Federal at 601 Clinton Street, Defiance, Ohio.

The following table sets forth certain information with respect to the office and other properties of the Company at December 31, 2005. See Note 9 to the Consolidated Financial Statements.

Description/address	Leased/ Owned	Net Book Value of Property	Deposits
		(Dollars in Thousands)	
Main Office, First Federal			
601 Clinton Street, Defiance, OH	Owned	$ 5,647	$ 237,278
Branch Offices, First Federal			
204 E. High Street, Bryan, OH	Owned	954	98,323
211 S. Fulton Street, Wauseon, OH	Owned	665	46,476
625 Scott Street, Napoleon, OH	Owned	1,387	65,682
1050 East Main Street, Montpelier, OH	Owned	494	29,677

926 East High Street, Bryan, OH	Owned	93	6,759
1333 Woodlawn, Napoleon, OH	Owned	44	17,766
1177 N. Clinton Street, Defiance, OH	Leased	1,261	24,700
905 N. Williams St., Paulding, OH	Owned	973	32,172
201 E. High St., Hicksville, OH	Owned	500	17,661
3900 N. Main St., Findlay, OH	Owned	1,268	40,817
11694 N. Countyline St., Fostoria, OH	Owned	813	21,153
1226 W. Wooster, Bowling Green, OH	Owned	1,236	51,392
301 S. Main St., Findlay, OH	Owned	1,126	31,801
405 E. Main St., Ottawa, OH	Owned	469	64,258
124 E. Main St., McComb, OH	Owned	257	19,648
7591 Patriot Dr., Findlay, OH	Owned	1,370	8,001
417 W Dussell Dr., Maumee, OH	Leased	1,159	27,915
230 E. Second St., Delphos, OH	Owned	1,331	96,089
105 S. Greenlawn Ave., Elida, OH	Owned	411	31,052
2600 Allentown Rd., Lima, OH	Owned	960	28,532
2285 N. Cole St., Lima, OH	Owned	496	9,337
22020 W. State Rt. 51, Genoa, OH	Owned	1,099	37,371
2760 Navarre Ave., Oregon, OH	Leased	273	16,332
1077 Louisiana Ave., Perrysburg, OH	Leased	99	9,309
First Insurance & Investments			
419 5th Street, Site 1200, Defiance, OH	Leased	193	N/A
		$ 24,578	$ 1,069,501

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Item 3. Legal Proceedings

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

Item 4. Submission of Matters to a Vote of Securities Holders

No matters were submitted to a vote of securities holders during the fourth quarter of 2005.

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PART II

Item 5. Market for Registrant's Common Stock and Related Stockholder Matters and Issuers Purchases of Common Stock

The Company's common stock trades on The Nasdaq Stock Market under the symbol "FDEF." As of March 3, 2006, the Company had approximately 2,170 shareholders of record. The table below shows the reported high and low sales prices of the common stock and cash dividends declared per share of common stock during the periods indicated in 2005 and 2004.

Years Ending

	December 31, 2005			December 31, 2004		
	High	Low	Dividend	High	Low	Dividend
Quarter ended:						
March 31	$ 29.90	$ 26.00	$ .22	$ 29.00	$ 26.60	$ .20
June 30	30.46	25.29	.22	28.88	22.07	.20
September 30	31.44	26.21	.22	26.76	22.01	.20
December 31	30.06	25.56	.24	28.90	25.20	.22

The OTS imposes various restrictions or requirements on the ability of associations to make capital distributions. Capital distributions include, without limitation, payments of cash dividends, repurchases and certain other acquisitions by an association of its shares and payments to stockholders of another association in an acquisition of such other association.

An application must be submitted and approval from the OTS must be obtained by a subsidiary of a savings and loan holding company (i) if the proposed distribution would cause total distributions for the calendar year to exceed net income for that year to date plus the savings association's retained net income for the preceding two years; (ii) if the savings association will not be at least adequately capitalized following the capital distribution; or (iii) if the proposed distribution would violate a prohibition contained in any applicable statute, regulation or agreement between the savings association and the OTS (or the FDIC), or a condition imposed on the savings association in an OTS-approved application or notice. If a savings association subsidiary of a holding company is not required to file an application, it must file a notice of the proposed capital distribution with the OTS. First Federal paid $34.4 million in dividends to First Defiance during 2005 and $5.0 million during 2004.

First Defiance completed the following common stock repurchases during the fourth quarter and the year ended December 31, 2005:

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 that May Yet Be Purchased Under the Plans or Programs (a)
October 1, 2005 - October 31, 2005	3,216	$ 28.95	3,216	416,778
November 1, 2005 - November 30, 2005	--	n/a	n/a	416,778
December 1, 2005 - December 31, 2005	6,586(b)	$ 27.10	--	416,778
Total for 2005 Fourth Quarter	9,802	$ 27.71	3,216	416,778

(a) On July 18, 2003, First Defiance announced that its Board of Directors had authorized management to repurchase up to 10% of the Registrant's common stock through open market or in any private transaction. The authorization, which is for 639,828 shares, does not have an expiration date.

(b) Shares acquired upon exercise of stock options.

Item 6. Selected Financial Data

The following table sets forth certain summary consolidated financial data at or for the periods indicated. Results of operations associated with The Leader, including certain inter-company financing transactions, are reflected as discontinued operations for all periods presented. Continuing operations reflect the results of First Federal, First Insurance and First Defiance holding company expenses for all periods presented. This information should be read in conjunction with the Consolidated Financial Statements and notes thereto included herein. See "Item 8. Financial Statements and Supplementary Data."

	At or For Years Ended Dece		
	2005	2004	2003
	(Dollars in Thousands, Except Pe		
Selected Consolidated Financial Data:			
Total assets	$ 1,461,082	$ 1,126,667	$ 1,040,599
Assets of continuing operations	1,461,082	1,126,667	1,040,599
Loans held-to maturity, net	1,164,481	878,912	735,255
Loans held-for-sale	5,282	2,295	5,872
Allowance for loan losses	13,673	9,956	8,844
Nonperforming assets	5,356	1,990	2,949
Securities available-for-sale	113,079	137,003	168,259
Securities held-to maturity	1,775	2,255	2,776
Mortgage servicing rights	5,063	3,598	3,431
Deposits and borrowers' escrow balances	1,070,106	797,979	729,227
FHLB advances	180,960	178,213	164,522
Stockholders' equity	151,216	126,874	124,269
Selected Consolidated Operating Results:			
Interest income from continuing operations	$ 76,174	$ 54,731	$ 50,629
Interest expense from continuing operations	28,892	20,381	20,855
Net interest income from continuing operations	47,282	34,350	29,774
Provision for loan losses	1,442	1,548	1,719
Non-interest income	15,925	13,996	16,843
Non-interest expense	43,942	31,200	27,126
Income before income taxes	17,823	15,598	17,772
Income taxes	5,853	4,802	5,690
Income from continuing operations	11,970	10,796	12,082
Discontinued operations, net of tax	--	--	--
Cumulative effect of change in method of accounting for goodwill	--	--	--
Net income	11,970	10,796	12,082
Basic earnings per share from continuing operations	1.75	1.77	2.00
Basic earnings per share	1.75	1.77	2.00
Diluted earnings per share from continuing operations	1.69	1.69	1.91
Diluted earnings per share	1.69	1.69	1.91

Item 6. Selected Financial Data (continued)

	At or For Years Ended December 31			
	2005	2004	2003	2002
	(Dollars in Thousands, Except Per Share Da			
Performance Ratios:				
Return on average assets	0.88%	1.01%	1.24%	0.77%
Return on average equity	8.26%	8.57%	9.97%	5.39%
Interest rate spread (1)	3.63%	3.37%	3.13%	2.92%
Net interest margin (1)	3.87%	3.60%	3.42%	3.38%
Ratio of operating expense to Average total assets	3.22%	2.98%	2.91%	3.16%
Quality Ratios:				
Nonperforming assets to total assets at end of period (2)	0.37%	0.18%	0.28%	0.31%
Allowance for loan losses to nonperforming assets (2)	255.28%	500.30%	299.90%	274.48%
Allowance for loan losses to total loans receivable	1.16%	1.13%	1.19%	1.32%
Capital Ratios (3):				
Equity to total assets at end of period	10.35%	11.26%	11.94%	13.58%
Tangible equity to tangible assets at end of period	7.88%	9.74%	10.17%	13.23%
Average equity to average assets	10.62%	11.76%	12.43%	14.36%
Book value per share	$ 21.34	$ 20.20	$ 19.64	$ 18.73
Tangible book value per share	$ 15.81	$ 17.19	$ 16.39	$ 18.17
Ratio of average interest-earning assets to average interest-bearing liabilities	110.30%	112.25%	112.25%	115.57%
Stock Price and Dividend Information:				
High	$ 31.44	$ 29.00	$ 30.65	$ 21.44
Low	25.29	22.01	18.21	15.12
Close	27.09	28.85	25.90	18.90
Cash dividends declared per share	0.90	0.82	0.65	0.54
Dividend payout ratio (4)	51.43%	46.33%	32.50%	22.78%

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

(2) Nonperforming assets consist of non-accrual loans that are contractually past due 90 days or more; loans that are deemed impaired under the criteria of FASB Statement No. 114; and real estate, mobile homes and other assets acquired by foreclosure or deed-in-lieu thereof.

(3) Capital ratios are based on assets of continuing operations.

(4) Dividends payout ratio was calculated using basic earnings per share.

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

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

First Federal is a federally chartered savings bank that provides financial services to communities based in northwest Ohio where it operates 25 full service banking centers in 12 northwest Ohio counties. On January 21, 2005, First Defiance acquired ComBanc, Inc., headquartered in Delphos, Ohio in a transaction valued at $38.3 million including acquisition costs. ComBanc's subsidiary, the Commercial Bank, operated four banking offices in Delphos, Lima and Elida, Ohio. On April 8, 2005, First Defiance acquired The Genoa Savings and Loan Company (Genoa), in a $11.2 million transaction. Genoa operated offices in Genoa, Oregon, Perrysburg and Maumee Ohio. The acquired Maumee office was merged with First Federal's existing Maumee office. First Defiance acquired $117.5 million of loans and $163.7 million of deposits in the ComBanc acquisition and $66.9 million of loans and $76.8 million of deposits in the Genoa transaction. For more details on the ComBanc and Genoa acquisitions, see Note 3 - Acquisitions in the Notes to the Financial Statements.

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 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 and investment and annuity products. Insurance products are sold through First Insurance's office in Defiance, Ohio while investment and annuity products are sold through registered investment representatives located at four of First Federal's banking center locations.

During 2003, First Defiance acquired $166.7 million of deposits, $79.0 million of loans, and three banking center offices located in Findlay, Ottawa and McComb Ohio (the "RFC acquisition"). First Defiance successfully completed the RFC acquisition on June 6, 2003 and their results reflect the acquisition from that date forward. For more details on the RFC acquisition, see Note 3 - Acquisitions in the Notes to Consolidated Financial Statements.

Financial Condition

Assets at December 31, 2005 totaled $1.46 billion compared to $1.13 billion at December 31, 2004, an increase of $334 million or 29.7%. The increase was due primarily to the acquisition of ComBanc Inc. its subsidiary the Commercial Bank as of January 21, 2005 and the acquisition of the Genoa Savings and Loan Company as of April 8, 2005. ComBanc had assets of $196.0 million as of January 21, 2005 and Genoa had assets of $83.4 million as of April 8, 2005. The following table indicates what portion of the change in First Defiance's assets, liabilities and equity was due to the acquisitions. Fair value adjustments and purchase accounting entries that have been pushed down to ComBanc and Genoa are included with their respective acquisition column. Explanations of changes in individual categories follow the table.

	Balance at Dec. 31, 2004	ComBanc Acquisition Jan. 21, 2005	Genoa Savings Acquisition April 8, 2005
	(dollars in thousands		
Assets			
Cash and due from banks	$ 19,891	$ 3,360	$ (612)
Interest-bearing deposits	630	49,327	--
Securities	139,258	502	15
Loans held for sale	2,295	--	--
Loans	888,868	119,656	67,770
Less allowance for loan losses	(9,956)	(2,162)	(865)
Net loans	878,912	117,494	66,905
Federal Home Loan Bank stock	13,376	1,852	1,481
Premises and equipment, net	24,248	4,106	2,345
Core deposit and other intangibles	593	3,077	1,202
Goodwill	18,340	12,445	4,299
Other assets	29,124	2,533	1,230
Total Assets	$ 1,126,667	$ 194,696	$ 76,865
Liabilities			
Deposits			
Non-interest bearing checking	$ 62,450	$ 17,665	$ 4,993
Interest bearing checking and money market	258,797	33,190	20,369
Savings	52,132	32,665	11,249
Certificates of deposit	424,322	80,148	40,175
Total deposits	797,701	163,668	76,786
Securities sold under agreements to Repurchase and other borrowings	14,804	6,610	--
FHLB advances	178,213	3,253	--
Junior subordinated debentures	--	--	--
Other liabilities	9,075	2,061	79
Total Liabilities	999,793	175,592	76,865
Shareholders' Equity	126,874	19,104	--
Total Liabilities and Shareholders' equity	$ 1,126,667	$ 194,696	$ 76,865

Loans

Loans receivable increased by $292.2 million or 32.9% to $1.18 billion at December 31, 2005 from $888.9 million at December 31, 2004. The increase included $121.2 million in loans acquired in conjunction with the ComBanc acquisition and $68.6 million of loans acquired in the Genoa transaction. Excluding the acquisitions, First Federal's loans grew by $99.5 million, or 11.2% in 2005. The increases by type of loan included $88.9 million in 1-4 family residential real estate loans, $139.5 million in commercial real estate loans, $28.6 million in commercial loans and $22.2 million of home equity and improvement loans.

Of the $88.9 million increase in 1-4 family residential real estate loans, $33.1 million was acquired as part of the ComBanc acquisition and $36.3 million was acquired from Genoa Savings. Of the $139.5 million increase in commercial real estate loans, $57.2 million was acquired as part of the ComBanc acquisition and $7.5 million was acquired from Genoa Savings. Of the $28.6 million increase in commercial loans, $12.7 million was acquired as part of the ComBanc acquisition and $1.7 million was acquired from Genoa Savings. Of the $22.2 million increase in home equity and improvement loans, $4.6 million was acquired as part of the ComBanc acquisition and $13.4 million was acquired from Genoa Savings.

Allowance for Loan Losses

The allowance for loan losses represents management's assessment of the estimated probably credit losses in the loan portfolio at each balance sheet date. Lending activities contain risks of loan losses. Management analyzes the adequacy of the allowance for loan losses regularly through reviews of the performance of the loan portfolio. Consideration is given to economic conditions, changes in interest rates and the effect of such changes on collateral values and borrower's ability to pay, changes in the composition of the loan portfolio, and trends in past due and non-performing loan balances. The allowance for loan losses is a material estimate that is susceptible to significant fluctuation and is established through a provision for loan losses based on management's evaluation of the inherent risk in the loan portfolio. In addition to extensive in-house loan monitoring procedures, the Company utilizes an outside party to conduct an independent loan review of all commercial loan and commercial real estate loan relationships that exceed $250,000 of aggregate exposure. 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 this type of loans.

At December 31, 2005, the allowance for loan losses was $13.7 million compared to $10.0 million at December 31, 2004. Those balances represented 1.16% and 1.12% of outstanding loans as of December 31, 2005 and December 31, 2004 respectively. The allowances acquired in the ComBanc and Genoa acquisitions totaled $2.2 million and $865,000 respectively and they were the most significant factor in the year over year growth in the allowance balance

In determining the appropriate level for the allowance for loan losses, First Defiance evaluates all loans in its portfolio. While allowances are frequently required for loans classified as substandard, it is possible for a credit relationship to be graded as substandard based on the financial performance of the credit for which no allowance is required because of other factors such as value of collateral or creditworthiness of guarantors. At December 31, 2005, a total of $19.3 million of loans are classified as substandard for which some level of reserve ranging between 20% and 50% of the outstanding balance is required. A total of $31.8 million in additional credits were classified as substandard at December 31, 2005 for which no reserve is required. First Defiance also has classified $1.0 million as doubtful at December 31, 2005. First Defiance also utilizes a general reserve percentage for loans not otherwise classified which ranges from 0.025% for mortgage loans to 1.50% for consumer loans. General reserves for commercial and commercial real estate loans, the largest category in First Defiance's portfolio, are established at 1.10% of the outstanding balance. The reserve percentage utilized for these loans is based on both historical losses in the Company's portfolio, national statistics on loss percentages, regulatory guidance and empirical evidence regarding the strength of the economy in First Defiance's general market area.

First Defiance's ratio of allowance for loan losses to non-performing loans dropped from 525.9% at the end of 2004 to 276.1% at December 31, 2005, the result of substantial non-performing loans acquired as part of the two acquisitions. Through its due diligence prior to making the acquisitions, management was aware of the existence of non-performing loans in both portfolios. At December 31, 2005, First Defiance had total non-performing assets of $5.4 million. Of that, $3.3 million related to either the ComBanc or Genoa acquisitions. The balance of non-performing assets which either were originated by First Defiance or acquired in the 2003 RFC branch acquisition were $2.1 million compared to $2.0 million of non-performing assets at December 31, 2004. While the level of classified loans has increased, year over year, management believes that the current allowance for loan losses is appropriate and that the provision for loan losses recorded in 2005 is consistent with both charge-off experience and the strength of the overall credits in the portfolio.

First Defiance's non-performing assets at December 31, 2005 were just $5.4 million compared to $2.0 million at December 31, 2004 and $2.9 million at December 31, 2003. Non-performing assets include loans that are 90 days past due and all real estate owned and other foreclosed assets. Non-performing assets at December 31, 2005 and 2004 by category were as follows:

	December 31	
	2005	2004
	(In thousands)	
Non-performing loans:		
Single-family residential	$2,648	$ 419
Non-residential and multi-family residential real estate	1,917	1,013
Commercial	287	450
Consumer finance	100	10
Total non-performing loans	4,952	1,892
Real estate owned and repossessed assets	404	98
Total non-performing assets	$5,356	$1,990

Non-performing loans in the single-family residential, non-residential and multi-family residential real estate and commercial loan categories represent ..94%, .35% and .17% of the total loans in those categories respectively at December 31, 2005 compared to 0.22%, 0.24% and 0.32% respectively for the same categories at December 31, 2004. Management believes that the allowance for loan losses is adequate to cover any estimated losses from non-performing loans.

Loans Acquired with Impairment

Certain loans acquired in the ComBanc and Genoa acquisitions had evidence that the credit quality of the loan had deteriorated since its origination and in management's assessment at the acquisition date it was probable that the First Defiance would be unable to collect all contractually required payments due. In accordance with American Institute of Certified Public Accountants Statement of Position 03-3 - Accounting for Certain Loans or Debt Securities Acquired in a Transfer (SOP 03-3), these loans have been recorded based on management's estimate of the fair value of the loans. At the acquisition date of January 21, 2005, loans with a contractual receivable of $3.4 million were acquired from Combanc which were deemed impaired. Those loans were recorded at a net realizable value of $2.1 million. On April 8, 2005, loans with a contractual receivable of $1.5 million were acquired from Genoa which were deemed impaired. Those loans were recorded at a net realizable value of $735,000. As of December 31, 2005, the total contractual receivable for those loans was $4.6 million and the recorded value was $2.6 million.

In determining the fair value of these loans, management evaluated the likelihood of receiving full payment under the contractual terms. Because of the nature of the types of loans identified, estimates of specific cash flows are not readily determinable. The loans acquired that are within the scope of SOP 03-3 are not accounted for using the income recognition model of the SOP because the Company cannot reasonably estimate cash flows expected to be collected. See Note 7 in the financial statements.

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. Frist Federal usually requires residential mortgage loan borrowers whose loan-to-value is greater than 80% to purchase private mortgage insurance (PMI). First Federal does originate and retain 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. Mortgage loans whose balances when combined with applicable second mortgages exceed 80% of the appraised value with no PMI totaled $29.7 million at December 31, 2005. These loans are generally paying as agreed.

In addition to first mortgages that exceed 80% loan-to-value, First Defiance makes home equity loans which, when combined with first mortgage loans, held either by First Federal or by other lenders, have potential exposure in excess of 80%. First Defiance generally will not make home equity loans that exceed 90% loan-to-value and exceptions to that guideline must be approved by First Federal's senior loan committee. First Defiance's total exposure for home equity loans that exceed 80% is $6.2 million at December 31, 2005. 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.

Securities

The securities portfolio declined $24.4 million to $114.9 million at December 31, 2005. Only a minimal amount of securities were acquired in the acquisitions. The activity in the portfolio in 2005 included $30.3 million of purchases, $28.9 million of amortization and maturities, $24.2 million of sales and a net decrease of $3.3 million in market value. The decline in market value in 2005 was attributable primarily to rising interest rates and that decline is believed to be temporary. Management took advantage of the 2005 rate environment and sold a portion of the portfolio in order to realize gains totaling $1.2 million. Proceeds of those sales were used primarily to fund loan growth. In addition, management maintained approximately $8 million in overnight investments as of December 31, 2005.

Goodwill and Intangible Assets

Goodwill increased $16.7 million to $35.1 million at December 31, 2005. The ComBanc and Genoa acquisitions added $12.4 million and $4.3 million respectively to Goodwill for the year. No impairment of goodwill was recorded in 2005. Core deposit intangibles and other intangible assets increased $3.5 million during 2005 to $4.1 million from just $593,000 at the end of 2004, due to core deposit and customer relationship intangibles recorded in conjunction with the acquisitions.

Deposits

Total deposits at December 31 2005 were $1.07 billion compared to $797.7 million at December 31, 2004, an increase of 34.1%. The ComBanc acquisition added $163.7 million of deposits and Genoa added $76.8 million. The remaining activity was a net increase of $31.3 million. Non-interest bearing checking grew by $41.0 million while money market and interest bearing checking accounts grew by $17.8 million, savings by $30.6 million, and certificates of deposit by $182.4 million. Excluding the acquisitions, non-interest bearing accounts increased by $18.4 million during 2005 and certificates of deposit increased by $62.0 million while interest bearing checking and money market accounts declined by $35.8 million and savings accounts declined by $13.3. This swing is attributable to improved CD rates during 2005. Management periodically utilizes brokered certificates of deposit to supplement its funding needs. At

December 31, 2005 the balance of brokered CDs totaled $37.0 million, down from $49.5 million at December 31, 2004.

Borrowings

FHLB advances totaled $181.0 million at December 31, 2005 compared to $178.2 million at December 31, 2004. The balance at the end of 2005 includes $110.0 million of convertible advances with rates ranging from 4.07% to 5.84%. These advances are all callable by the FHLB, at which point they would convert to a three-month LIBOR advance if not paid off. Those advances have final maturity dates ranging from 2010 to 2013. In addition, First Defiance has advances totaling $27 million that are callable by the FHLB only if the three-month LIBOR rate exceeds a strike rate ranging from 7.5% to 8.0%. The rate on those advances ranges from 3.48% to 5.14%. First Defiance also has $14.3 million outstanding at the FHLB under a series of fixed-rate loans and $28.5 million borrowed on an overnight basis at December 31, 2005.

First Defiance also has $25.8 million of securities that have been sold at December 31, 2005 with agreements to repurchase, an increase of this type of funding of $14.0 million over December 31, 2004. The ComBanc acquisition accounted for approximately $6.6 million of that growth.

In October 2005, the Company issued $20.6 million of Subordinated Debentures. These debentures were issued to an unconsolidated affiliated trust that purchased them with the proceeds from a $20 million issued of trust preferred securities to an outside party. The proceeds of the Subordinated Debentures were used for general corporate purposes. The Subordinated Debentures have a rate equal to three-month LIBOR plus 1.38%.

Capital Resources

Total shareholders' equity increased $24.3 million to $151.2 million at

December 31, 2005. This increase is primarily comprised of $19.1 million of stock issued in conjunction with the ComBanc acquisition and $12.0 million for net income. Those increases were offset by $6.2 million of dividends ($0.90 per share declared), $2.2 million in after-tax market value adjustments to the available for sale securities portfolio and $1.5 million for treasury stock repurchases. The Company's board of directors authorized the repurchase of 640,000 shares in 2003. A total of 54,531 shares were repurchased in 2005 at an average cost of $28.37 and 416,778 shares remain to be purchased under the authorization. Equity also increased by $1.3 million to reflect the release of shares in the Employee Stock Ownership Plan and by $1.8 million as a result of stock option exercises and the related tax benefit of non-qualified option exercises.

Average Balances, Interest Rates and Yields

The following table presents for the periods indicated the total dollar amounts of interest from average interest-earning assets and the resultant yields, as well as the interest expense on average interest-bearing liabilities, expressed both in dollars and rates, and the net interest margin. The table does not reflect the effect of income taxes:

	Year Ended December 31,					
	2005			2004		
	Average Balance	Interest (1)	Yield/ Rate(2)	Average Balance	Interest (1)	Yiel Rate
				(Dollars in Thousands)		
Interest-Earning Assets:						
Loans receivable	$1,089,942	69,732	6.40%	$ 806,877	47,360	5.
Securities	121,510	5,873	4.88%	152,316	7,499	4.
Interest-earning deposits	10,410	364	3.50%	2,447	43	1.
Dividends on FHLB stock	16,352	829	5.07%	14,839	612	4.
Total interest-earning assets	1,238,214	76,798	6.20%	976,482	55,514	5.
Non-interest-earning assets	126,583			94,321		
Total Assets	$1,364,797			$1,070,803		
Interest-Bearing Liabilities:						
Interest-bearing deposits	$ 932,036	$20,615	2.21%	$ 699,087	$12,950	1.
FHLB advances	168,330	7,625	4.53%	169,463	7,317	4.
Other borrowings	18,736	451	2.41%	10,608	114	1.
Subordinated debentures	3,441	201	5.84%	--	--	
Total interest-bearing liabilities	1,122,543	28,892	2.57%	879,158	20,381	2.
Non-interest bearing demand deposits	86,741	--		56,241	--	
Total including non-interest- bearing						

demand deposits	1,209,284	28,892	2.39%	935,399	20,381	2.
Other non-interest liabilities	10,530			9,484		
Total Liabilities	1,219,814			935,399		
Stockholders' equity	144,983			125,920		
Total liabilities and stockholders' equity	$1,364,797			$1,070,803		
Net interest income; interest rate spread (3)		$47,906	3.63%		$35,133	3.
Net interest margin (4)			3.87%			3.
Average interest-earning assets to average interest-bearing liabilities			110.3%			104

(1) Interest on certain tax exempt loans (amounting to $47,000, $29,000 and $61,000 in 2005, 2004 and 2003 respectively) and tax-exempt securities ($1.2 million, $1.5 million and $1.4 million in 2005, 2004 and 2003) is not taxable for Federal income tax purposes. The average balance of such loans was $1.0 million, $722,000 and $870,000 in 2005, 2004 and 2003 while the average balance of such securities was $25.1 million, $32.8 million and $30.5 million in 2005, 2004 and 2003 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, 2005, the yields earned and rates paid were as follows: loans receivable, 6.69%; securities, 5.03%; FHLB stock, 5.75%; total interest-earning assets, 6.54%; deposits, 2.40%; FHLB advances, 4.57%; other borrowings, 2.68%; total interest-bearing liabilities, 2.72%; and interest rate spread, 3.82%.

(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.

Rate/Volume Analysis

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 interest income and 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.

	Year Ended December 31,				
	2005 vs. 2004			2004 vs.	
	Increase (decrease) due to rate	Increase (decrease) due to volume	Total increase (decrease)	Increase (decrease) due to rate	Incre (decre due volu
Interest-Earning Assets					
Loans	$ 4,567	$ 17,805	$ 22,372	$ (1,936)	$ 8,
Securities	(135)	(1,491)	(1,626)	2	(1,
Interest-earning deposits	75	246	321	182	(
FHLB stock	150	67	217	31	(
Total interest-earning assets	$ 4,657	$ 16,627	$ 21,284	$ (1,721)	$ 5,
Interest-Bearing Liabilities					
Deposits	$ 2,821	$ 4,844	$ 7,665	$ (2,702)	$ 2,
FHLB advances	357	(49)	308	516	(
Term notes	208	129	337	5	
Subordinated Debentures	--	201	201	--	
Total interest- bearing liabilities	$ 3,386	$ 5,125	$ 8,511	$ (2,181)	$ 1,
Increase in net interest income			$ 12,773		

Results of Operations

General -- First Defiance reported net income of $12.0 million for the year ended December 31, 2005 compared to $10.8 million and $12.1 million for the years ended December 31, 2004 and 2003 respectively. On a diluted per share basis, First Defiance earned $1.69 in 2005, $1.69 in 2004 and $1.91 in 2003.

The 2005 net income amount includes $3.5 million of acquisition related costs that were incurred as part of the ComBanc and Genoa acquisitions. These costs included such items as the expense to terminate data processing contracts, severance agreements with employees who were not retained, and other costs resulting from the acquisition or related transition efforts. After tax, these costs amounted to $2.3 million, or $.32 per share. The 2004 results included a $1.9 million pretax charge to reflect final settlement of certain contingent liabilities related to the sale of the Company's 2002 sale of the former Leader Mortgage subsidiary to US Bancorp. After tax, that amount was $1.25 million or $0.20 per diluted share. Excluding these non-operating items, core earnings were $14.2 million, $12.0 million and $12.1 million for the years ended December 31, 2005, 2004 and 2003 respectively. On a diluted per share basis, core earnings amounted to $2.01, $1.89 and $1.91 for those three periods. A reconciliation of GAAP earnings to core earnings is as follows:

	Year Ended December 31,		
	2005	2004	2003
	(in thousands)		
GAAP Net Income	$ 11,970	$ 10,796	$ 12,082
One-time acquisition related charges	3,476	--	--
Settlement of contingent liability	--	1,927	--
Tax effect	(1,217)	(674)	--
Core Operating Earnings	$ 14,229	$ 12,049	$ 12,082
Basic earnings per share:			
GAAP	$ 1.75	$ 1.77	$ 2.00
Core Operating Earnings	$ 2.08	$ 2.07	$ 2.00
Diluted earnings per share:			
GAAP	$ 1.69	$ 1.69	$ 1.91
Core Operating Earnings	$ 2.01	$ 1.89	$ 1.91

Net interest income was $47.3 million for the year ended December 31, 2005 compared to $35.1 million and $29.8 million for the years ended December 31, 2004 and 2003 respectively. The tax-equivalent net interest margin was 3.87%, 3.62% and 3.45% for the years ended December 31, 2005, 2004 and 2003 respectively. The increase in margin between 2004 and 2005 is due to an improved interest rate spread, which increased to 3.63% for the year ended December 31, 2005 compared to 3.39% for 2004. The improved spread resulted from a 51 basis point improvement in the yield on interest-earning assets to 6.20% in 2005 from 5.71% in 2004 while the cost of interest bearing liabilities between the two periods increased by just 26 basis points, from 2.32% in 2004 to 2.58% in 2005. Margin also improved in 2005 as a result of the improved mix between loans and investment securities, the $30.5 million increase in the average balance of non-interest bearing deposits and a $19.1 million increase in average equity for the year. The increase in the margin between 2003 and 2004 is due to an improved interest rate spread, which increased from 3.13% in 2003 to 3.37% in 2004, a result primarily due to a 30 basis point reduction the the

Company's overall cost of interest bearing liabilities (from 2.62% to 2.32%) compared to a drop of just six basis points on the yield of interest earning assets (from 5.75% in 2003 to 5.69% in 2004). Margin also improved in 2004 due to an $8.7 million increase in the average balance in non-interest bearing deposits and a $4.7 million increase in capital.

The 51 basis point improvement in asset yields in 2005 is due to 53 basis point improvement in the yield on loans and a $30.8 million decline in lower yielding securities that were replaced with higher yielding loans. Further yields improved on interest bearing deposits and on FHLB stock in 2005 compared to 2004. The decline in asset yields in 2004 compared to 2003 is the result of a 31 basis point decline in the yield on loans, which dropped to 5.87% in 2004 from 6.18% in 2003. That decline was partially offset by an improved asset mix as average loan balances increased from $667.2 million in 2003 to $806.9 million in 2004 while the average balance in securities declined from $186.6 million in 2003 to $152.3 million in 2004 and the average balance of interest bearing deposits declined from $22.1 million in 2003 to just $2.4 million in 2004.

The provision for loan losses totaled $1.4 million, $1.5 million and $1.7 million for 2005, 2004 and 2003 respectively while charge-offs were $1.1 million, $685,000 and $725,000 and recoveries were $302,000, $249,000 and $354,000 respectively in those same years. As a percentage of average loans, net charge-offs were 0.07% for the year ended December 31, 2005 compared to 0.05% and 0.06% for 2004 and 2003 respectively.

For the year ended December 31, 2005, non-interest income was $15.9 million compared to $14.0 million for 2004 and $16.8 million for 2003. Non-interest expense for the year ended December 31, 2005 was $43.9 million ($40.5 million excluding acquisition related charges) compared to $31.2 million for 2004 ($29.3 million excluding the settlement of a contingent liability) and $27.1 million for 2003.

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.

Total interest income increased by $21.4 million, or 39.2% to $76.2 million for the year ended December 31, 2005 from $54.7 million for the year ended December 31, 2004. The increase in income was due to an increase in the average balance in loans receivable, to $1.09 billion for the twelve months of 2005 compared to $806.9 million for 2004. During the same period the average balance of investment securities dropped to $121.5 million for all of 2005 from $152.3 million for the year ended December 31, 2004. In addition to the increase in loan balances, the yield on loans increased to 6.40% on average for 2005 compared to 5.87% in 2004, a 53 basis point improvement.

The increase in the average balance of loans resulted primarily from the acquisitions, where $190.0 million of loans were acquired. However, First Defiance continues to also have strong internal loan growth as average loan balances grew by an additional $93 million during 2005. For the year, First Defiance's commercial real estate loans grew by $139.5 million ($71.2 million excluding loans acquired in the acquisitions), one-to-four residential loans grew by $88.9 million ($13.1 million excluding the acquisitions), commercial loans grew by $28.6 million ($13.7 million excluding the acquisitions) and home equity and improvement loans grew by $22.2 million ($4.2 million excluding the acquisitions).

Interest income from the investment portfolio declined to $5.9 million in 2005 from $7.3 million in 2004. The decline is due to the decrease in the average balance from $152.3 million to $121.5 million between 2004 and 2005. As securities matured or were sold, the proceeds were generally used to fund loan

growth. The tax equivalent yield on the investment portfolio was 4.83% in 2005 compared to 5.08% in 2004 as several of the higher yielding securities in the portfolio were sold to take advantage of gain positions. First Defiance's balance in interest bearing deposits with other banks increased significantly following several of the securities sales. With recent increases in interest rates, the cost of carrying those liquid assets has declined relative to longer investment options.

Total interest income increased by $4.2 million, or 8.4% to $54.1 million for the year ended December 31, 2004 from $49.9 million for the year ended December 31, 2003. The increase in income was due to an increase in the average balance of loans receivable, to $806.9 million for the twelve months of 2004 compared to $667.2 million for 2003. During the same period, the average balance of lower yielding investment securities declined to $152.3 million in 2004 from $186.6 million in 2003 and funds held on deposit at other financial institutions dropped to an average of just $2.4 million in 2004 from $22.1 million in 2003. While loan yields between 2003 and 2004 dropped to 5.87% from 6.18%, that 31 basis point decline was more than offset by the change in the mix between loans and lower yielding assets. The increase in the average balance of loans receivable was due primarily to the growth in the Company's commercial real estate loans, which increased by $73.7 million or 21.6% between December 31, 2003 and December 31, 2004. In addition, balances in one-to-four family residential real estate loans, commercial loans and home equity loans increased by $22.1 million, $21.0 million and $20.8 million respectively from the beginning to the end of 2004. Interest income from the investment portfolio decreased to $6.7 million for 2004 from $8.5 million in 2003.

Interest expense increased by $8.5 million in 2005 compared to 2004, to $28.9 million from $20.4 million. This increase was due to a $232.9 million increase in the average balance of interest bearing deposits in 2005 compared to 2004 as well as a 36 basis point increase in the cost of those deposits. Total interest bearing deposits acquired in the acquisitions was $217.8 million. For the year, the actual balance of interest-bearing deposits increased by $230.8 from December 31, 2004 to December 31, 2005. Of that growth, $182.4 million was in certificates of deposit, which have a higher cost than transaction accounts. Interest expense on interest-bearing deposits was $20.6 million in 2005 and $12.9 million in 2004. Expenses on FHLB advances and other funding interest bearing funding sources was not significantly different between 2004 and 2005. First Defiance issued $20.6 million of junior subordinated debentures in conjunction with a trust preferred offering by an unconsolidated affiliated subsidiary. Interest expense recognized by the Company related to those subordinated debentures was $201,000 in 2005.

Interest expense declined by $474,000 in 2004 from 2003, to $20.4 million from $20.9 million. This decline was the result of a decline in interest rates paid on deposits and the utilization of overnight Federal Home Loan Bank advances to help short-term funding needs. Interest expense on interest bearing deposits was $12.95 million for 2004 compared to $13.4 million for 2003 despite the fact that the average balance of interest-bearing deposits increased to $699.1 million for 2004 from $633.0 million for 2003. The growth in the average balance of deposits occurred in both transaction accounts (savings accounts, money market accounts, and interest-bearing checking accounts which increased in total to $285.3 million at December 31, 2004 from $245.1 million at December 31, 2003) and in certificates of deposits (which increased to $413.8 million at December 31, 2004 from $387.9 million at December 31, 2003). The average cost of FHLB advances declined to 4.32% in 2004 from 4.73% in 2003 because of an increase in the average balance of over-night or short-term advances during the year. At December 31, 2004, FHLB advances included $26.5 million of overnight advances, compared to just $11.0 million at December 31, 2003. The average balance of short-term advances was $15.6 million for 2004 compared to $2.3 million for 2003. There was no change in the balance or rates paid on long-term advances during 2004.

As a result of the foregoing, First Defiance's net interest income was $47.3 million for the year ended December 31, 2005 compared to $34.3 million for the year ended December 31, 2004 and $29.8 million for the year ended December

31, 2003. Net interest margin from continuing operations calculated on a tax-equivalent basis was 3.87% for 2005 compared to 3.62% in 2004 and 3.45% in 2003. In addition to the factors cited above, net interest margin is also favorably impacted by an increase in non-interest bearing deposits, which increased to an average balance of $86.7 million in 2005 from an average of $56.2 million in 2004 and $47.5 million in 2003.

Provision for Loan Losses - First Defiance's provision for loan losses was $1.4 million for the year ended December 31, 2005 compared to $1.5 million and $1.7 million for the years ended December 31, 2004 and 2003 respectively.

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 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 assets, including loans which meet the FASB Statement No. 114 definition of impaired; the amount of assets 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 the Allowance for Loan Losses in Management's Discussion and Analysis and Note 7 to the audited financial statements.

Non-interest Income - Non-interest income increased by $1.9 million or 13.8% in 2005 to $15.9 million from $14.0 million for the year ended December 31, 2004. In 2003, $16.8 million of non-interest income was recognized. Most of the increase in 2005 was in service fees and other charges, which increased to $5.6 million for the year ended December 31, 2005 from $4.2 million for 2004, an increase of $1.4 million or 32.9%. Increased fees resulting from the larger account base following the acquisitions was the primary reason for the increase in service fees. Service fee income was $3.5 million in 2003

Mortgage banking income includes gains from the sale of mortgage loans, fees for servicing mortgage loans for others, and an offset for amortization of mortgage servicing rights, and adjustments for impairment in the value of mortgage servicing rights. Mortgage banking income totaled $3.3 million, $2.8 million and $6.8 million in 2005, 2004 and 2003 respectively. That $574,000 of growth in 2005 over 2004 was primarily attributable to the recapture of $417,000 of previously recorded mortgage servicing rights impairment and a $295,000 increase in mortgage servicing fees resulting from a $139 million increase in the portfolio of mortgage loans serviced for others. Gains from the sale of mortgage loans totaled $2.3 million for both 2005 and 2004. The higher level of mortgage banking income in 2003 was the result of significant mortgage loan origination activity, a result of the major mortgage refinancing wave which occurred in those periods. Gains from sale of loans in 2003 were $7.0 million. The higher level of gains in 2003 was offset somewhat by higher levels of mortgage servicing rights amortization ($2.0 million in 2003 compared to just $784,000 and $704,000 in 2005 and 2004 respectively). Also there have been significant fluctuations in the level of mortgage servicing rights impairment adjustments over the past three years, ranging from impairment expense of $717,000 and $1,000 in 2003 and 2004 respectively, to a recovery of previously recorded impairment of $417,000 in 2005. The balance of the impairment allowance stands at just $82,000 at the end of 2005 following the recording of a $108,000 permanent mortgage servicing rights write-down in 2005. See Note 8 to the financial statements.

First Defiance also realized $1.2 million of securities gains in 2005 compared to $1.4 million in 2004 and $1.6 million in 2003. In all three years, management took advantage of favorable prices in the bond portfolio as long-term interest rates stayed low. Generally as investments were sold out of the investment portfolio, the related proceeds were used to fund loan growth or they were reinvested in shorter-term securities in order to position the Company for an eventual overall rate increase.

Non-interest Expense -- Total non-interest expense for 2005 was $43.9 million compared to $31.2 million for the year ended December 31, 2004 and $27.1 million for the year ended December 31, 2003. The 2005 results include $3.5 million of acquisition related charges while the 2004 amount includes a charge of $1.9 million related to the final settlement of a contingent liability related to First Defiance's 2002 sale of its Leader Mortgage subsidiary. Non-interest expense, excluding the acquisition related charges in 2005 and the settlement of the contingency in 2004, was $40.4 million and $29.3 million respectively for those two years.

Compensation and benefits increased by $6.0 million in 2005 compared to 2004, to $23.4 million in 2005 from $17.4 million in 2004. Most of the increase in compensation was due to staffing increases resulting from the acquisitions, the addition of staff in central operations to service the larger branch network and continued increases in the cost of First Defiance's health insurance. The total number of full-time equivalent employees increased to 428 at the end of 2005 compared to 322 at the end of 2004. Also in 2005, occupancy costs increased to $4.7 million from $3.3 million in 2004, state franchise tax increased to $1.3 million from $868,000, and data processing increased to $3.2 million from $2.4 million. The majority of these increases were a result of the growth due to the acquisitions. Also in 2005, amortization of intangibles including core deposit intangibles and customer relationship intangibles increase to $755,000 from just $110,000 in 2004, a result of the amortization of intangibles acquired in the acquisitions. First Defiance's other non-interest expense category also increased to $6.9 million in 2005 from $5.2 million in 2004. Increases in that category resulted from higher levels of advertising (up $503,000), printing and office supplies (up $168,000), postage (up $223,000) and bad check charge-offs and other related deposit account losses (up $247,000).

The increase in non-interest expense in 2004 from 2003 was the primarily due to a $1.3 million increase in compensation and benefits expense. Occupancy costs and data processing costs also increased in 2004 by $254,000 and $522,000 respectively.

As noted, the 2005 non-interest expense included $3.5 million of acquisition related costs. Of these costs, $1.05 million related to the ComBanc acquisition and $2.45 related to the Genoa acquisition. For ComBanc, the most significant costs included $471,000 in severance and other termination payments to employees not retained, $222,000 related to the cancellation of certain contracts. For Genoa, the most significant costs included $1.3 million for the termination of a long-term data processing contract and other long-term contracts and lease arrangements and $364,000 for severance and other payments to employees not retained.

Income Taxes - Income taxes amounted to $5.9 million in 2005 compared to $4.8 million in 2004 and 5.7 million in 2003. The effective tax rates for those years were 32.8%, 30.8%, and 32.0% respectively. The tax rate is lower than the statutory 35% tax rate for the Company because of investments in tax-exempt securities and in BOLI. The earnings on such investments are not subject to federal income tax. The increase in the effective tax rate in 2005 compared to 2004 is primarily the result of lower levels of interest income from tax-exempt securities in 2005 compared to 2004 and a reduction in earnings from BOLI. See note 16 to the financial statements.

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 manner 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 market area. There are no 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 unused 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 $16.6 million, $16.3 million and $23.1 million in 2005, 2004 and 2003 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, ESOP expense related to the release of ESOP shares in accordance with AICPA SOP 93-6 and increases and decreases in other assets and liabilities.

In a typical year, 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 2005, First Defiance completed the acquisitions of ComBanc and Genoa. In the case of the ComBanc acquisition, which was purchased with a combination of stock and cash, First Defiance realized an increase in cash of $52.7 million after netting the cash that was acquired from ComBanc. ComBanc's cash level was high because they liquidated their investment portfolio in advance of the acquisition closing date. In the case of the Genoa acquisition, the acquisition resulted in a net reduction in cash of $612,000 after netting Genoa's cash balances against the purchase price. In 2003, First Defiance completed the RFC acquisition, which increased cash from investing activities by $70.1 million as deposits acquired exceeded the purchase price plus loans acquired.

In considering the more typical investing activities, during 2005, $27.9 million and $24.2 million was generated from the maturity or sale of available-for-sale investment securities, respectively, while $104.1 million was used fund loan growth and $30.3 million was used to purchase available-for-sale investment securities. During 2004, $42.8 million and $20.7 million was generated from the maturity of investment securities and sale of available-for-sale investment securities, respectively, while $144.7 million was used fund loan growth and $34.3 million was used to purchase available-for-sale investment securities. During 2003, $64.9 million and $22.2 million was realized from the maturity of investment securities and

sale of investment securities respectively while $97.4 million was used to fund loan growth and $48.9 million was used to purchase available for sale securities.

Principal financing activities include the gathering of deposits, the utilization of FHLB advances, the sale of securities under agreements to repurchase such securities and borrowings from other banks. In addition, First Defiance also purchased common stock for its treasury. For 2005, total deposits (excluding deposits acquired in the acquisitions) increased by $31.9 million, including $44.4 million of growth in retail deposit balances. The amount of deposits acquired from CD brokers or other out of market sources declined in 2005 by $12.5 million. For the year ended December 31, 2004, deposits increased by $69.1 million, including $58.6 million of growth in retail deposits generated by the First Federal Bank branch network, and $10.5 million in net growth in deposits acquired from CD brokers or other out of market sources. For the year ended December 31, 2003, deposits declined by $37.3 million, primarily do to the Company not replacing $32.0 million of maturing brokered certificates of deposit which were no longer needed. Also in 2005, First Defiance issued $20.6 million of subordinated debentures to an unconsolidated affiliated trust and that trust issued $20 million of trust preferred stock to outside investors. Also in 2005, Short-term advances from the FHLB increased by $2 million and borrowings on lines of credit from other banks of $3 million were paid off. Also securities sold under repurchase arrangements increased by $7.3 million. In 2004, First Defiance borrowed $15.5 million in short-term advances from the FHLB and $3.0 million on from other financial institutions under short-term lines of credit. In 2003, First Defiance borrowed $9 million from the FHLB under long-term advance agreements and an additional $8 million was borrowed on short-term advances. Also, the Company repurchased $1.5 million, $4.7 million, $4.4 million of common stock for treasury in 2005, 2004 and 2003 respectively. 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, 2005, First Defiance had the following commitments to fund deposit, advance and borrowing obligations:

	Maturity Dates by Period at December 31			
Contractual Obligations	Total	Less than 1 year	1-3 years	4-5 yea
			(In Thousands)	
Savings, checking and demand accounts	$ 462,822	$ 462,822	$ --	$
Certificates of deposit	606,679	451,010	151,439	3,3
FHLB overnight advances	28,500	28,500	--	
FHLB fixed advances including interest (1)	194,092	8,301	26,376	23,0
Subordinated debentures	20,619	--	--	
Securities sold under repurchase agreements	25,748	25,748	--	
Lease obligations	4,489	344	476	4

Total contractual cash obligations	$1,342,949	$ 976,725	$ 178,291	$ 26,8

(1) Includes principal payments of $152,298 and interest payments of $41,794

At December 31, 2005, First Defiance had the following commitments to fund loan or line of credit obligations:

		Amount of Commitment Expiration by Perio			
Commitments	Total Amounts Committed	Less than 1 year	1-3 years	4-5 years	Af y
		(In Thousands)			
Residential real estate loans in process	$ 44,998	$ 44,998	$ --	$ --	$
Commercial loans in process	8,629	8,629	--	--	
One-to-four family mortgage loan originations	12,097	6,757	4,974	--	
Multifamily originations	8,626	1,881	--	--	
Other real estate originations	48,310	12,550	11,556	10,914	1
Nonmortgage loan originations	3,024	182	2,067	475	
Consumer lines of credit	90,428	5,682	9,707	13,350	6
Commercial lines of credit	59,870	43,276	15,807	2	
Total loan commitments	275,982	123,955	44,111	24,741	8
Standby letters of credit	8,785	4,802	389	3,594	
Total Commitments	$284,767	$128,757	$ 44,500	$ 28,335	$ 8

In addition to the above commitments, at December 31, 2005 First Defiance had commitments to sell $8.5 million of loans held for sale to Freddie Mac.

To meet its obligations, management can adjust the rate of savings certificates to retain deposits in changing interest rate environments; it can sell or securitize mortgage and non-mortgage loans; and it can turn to other sources of financing including FHLB advances, the Federal Reserve Bank, bank lines and brokered certificates of deposit. At December 31, 2005 First Defiance had $64.1 million capacity under its agreements with the FHLB and other banks.

First Defiance is subject to various capital requirements of the Office of Thrift Supervision. At December 31, 2005, First Federal had capital ratios that exceeded the standard to be considered "well capitalized". For additional information about First Federal's capital requirements, see Note 15 to the Consolidated Financial Statements.

Critical Accounting Policies

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

Allowance for Loan Losses: First Defiance believes the allowance for loan losses is a critical accounting policy that requires the most significant judgments and estimates used in preparation of its consolidated financial statements. In determining the appropriate estimate for the allowance for loan losses, management considers a number of factors relative to both specific credits in the loan portfolio and macro-economic factors relative to the economy of the United States as a whole and the economy of the northwest Ohio region 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 than 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, the loss experience being reported by other financial institutions operating in the Company's market area, and other factors in providing for loan losses that have not been specifically classified. While management believes its allowance for loan losses is conservatively determined based on the above factors, it does not believe the allowances to be excessive or unnecessary. Refer to the section titled "Allowance for Loan Losses" and Note 2, Statement of Accounting Policies for a further description of the Company's estimation process and methodology related to the allowance for loan losses.

Valuation of Mortgage Servicing Rights: First Defiance believes the valuations of mortgage servicing rights is a critical accounting policy that requires significant estimates in preparation of its consolidated financial statements. First Defiance recognizes as separate assets the value of mortgage servicing rights, which are acquired through loan origination activities. First

Defiance does not purchase any mortgage servicing rights.

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

Forward Looking Information

Forward looking statements in this report are made in reliance upon the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. The statements in this report which are not historical fact are forward looking statements and they include, among other statements, projections about growth in the Financial Condition section, comments about the adequacy of the allowance for loan losses and projections about interest rate simulations included in the Asset/Liability Management section. Actual results may differ from expectations contained in such forward looking information as a result of factors including but not limited to the interest rate environment, economic policy or conditions, federal and state banking and tax regulations, and competitive factors in the marketplace. Each of these factors could affect estimates, assumptions, uncertainties and risks considered in the development of forward looking information and could cause actual results to differ materially from management's expectation regarding future performance.

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Item 7A. Quantitative and Qualitative Disclosure 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. The results of the simulation indicate that in an environment where interest rates rise 100 basis points over a 12 month period, First Defiance's net interest income would increase by just 1.75% over the base case scenario. Were interest rates to fall by 100 basis points during the same 12-month period, the simulation indicates that net interest income would decrease by only 1.72%. 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 Defiance's lending activities are in the non-residential real estate and commercial loan areas. While such loans carry higher credit risk than residential mortgage lending, they tend to be more rate sensitive than residential mortgage loans. The balance of First Defiance's non-residential and multi-family real estate loan portfolio was $552.0 million, which is split between $93.6 million of fixed-rate loans and $458.4 million of adjustable-rate loans at December 31, 2005. The commercial loan portfolio increased to $171.3 million, which is split between $70.2 million of fixed-rate loans and $101.1 million of adjustable-rate loans at December 31, 2005. Certain of the 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 7 years. First Defiance also has significant balances of consumer loans ($55.3 million at December 31, 2005) which tend to have a shorter duration than residential mortgage loans, and home equity and improvement loans ($113.0 million at December 31, 2005) which fluctuate with changes in the prime lending rate. Also, to limit its interest rate risk, (as well as to provide liquidity) First Federal sells a majority of its fixed-rate mortgage originations into the secondary market.

In addition to the simulation analysis, First Federal also prepares an "economic value of equity" ("EVE") analysis. This analysis calculates the net present value of First Federal's assets and liabilities in rate shock environments that range from -300 basis points to +300 basis points. The results of this analysis are reflected in the following table.

December 31, 2005

	Economic Value of Equity			Economic Value of Equity as % of Present Value of Assets	
Change in Rates	$ Amount (Dollars in Thousands)	$ Change	% Change	Ratio	Change
+ 300 bp	165,307	(21,390)	(11.46%)	12.04%	(84) bp
+ 200 bp	172,774	(13,923)	(7.46%)	12.36%	(52) bp
+ 100 bp	180,028	(6,669)	(3.57%)	12.65%	(23) bp
0 bp	186,697	--	--	12.88%	--
-100 bp	191,267	4,570	2.45%	12.98%	10 bp
-200 bp	193,131	6,434	3.45%	12.91%	3 bp
-300 bp	194,686	7,989	4.28%	12.83%	(5) bp

Based on the above analysis, in the event of a 200 basis point increase in interest rates as of December 31, 2005, First Federal would experience a 7.46%

decrease in its economic value of equity. If rates would fall by 200 basis points its economic value of equity would increase by 3.45%. 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 and the durations are fairly closely matched. The average duration of its assets at December 31, 2005 was 1.75 years while the average duration of its liabilities was 1.54 years.

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

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Item 8. Financial Statements and Supplementary Data

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

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

We have audited the accompanying consolidated statement of financial condition of First Defiance Financial Corp. as of December 31, 2005 and the related consolidated statements of income, stockholders' equity and cash flows for the year then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit. The consolidated financial statements of First Defiance Financial Corp. as of December 31, 2004 and for the years ended December 31, 2004 and 2003 were audited by other auditors whose report dated March 8, 2005 expressed an unqualified opinion on those statements.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of First Defiance Financial Corp. as of December 31, 2005, and the results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of the Company's internal control over financial reporting as of December 31, 2005, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) and our report dated March 10, 2006 expressed an unqualified opinion thereon.

/s/ Crowe Chizek and Company LLC

Crowe Chizek and Company LLC

Cleveland, Ohio
March 10, 2006

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Report of Independent Registered Public Accounting Firm
On Consolidated Financial Statements

The Board of Directors
First Defiance Financial Corp.

We have audited the accompanying consolidated statement of financial condition of First Defiance Financial Corp. and subsidiaries as of December 31, 2004, and the related consolidated statements of income, changes in stockholders' equity, and cash flows for each of the two years in the period ended December 31, 2004. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of First Defiance Financial Corp. and subsidiaries at December 31, 2004, and the consolidated results of their operations and their cash flows for each of the two years in the period ended December 31, 2004, in conformity with U.S. generally accepted accounting principles.

/s/ Ernst & Young LLP

Cleveland, Ohio
March 8, 2005

First Defiance Financial Corp.

Consolidated Statements of Financial Condition

	December 31 2005	December 31 2004
	(In Thousands)	
Assets		
Cash and cash equivalents:		
Cash and amounts due from depository institutions	$ 44,066	$ 19,891
Interest-bearing deposits	5,190	630
	49,256	20,521
Securities:		
Available-for-sale, carried at fair value	113,079	137,003
Held-to-maturity, carried at amortized cost (fair value $1,845 and $2,376 at December 31, 2005 and 2004, respectively)	1,775	2,255
	114,854	139,258
Loans receivable, net of allowance of $13,673 and $9,956 at December 31, 2005 and 2004, respectively	1,164,481	878,912
Loans held for sale	5,282	2,295
Mortgage servicing rights	5,063	3,598
Accrued interest receivable	6,207	4,653
Federal Home Loan Bank stock and other interest-earning assets	17,544	13,376
Bank owned life insurance	24,346	18,581
Premises and equipment	32,429	24,248
Real estate and other assets held for sale	404	98
Goodwill	35,084	18,340
Core deposit and other intangibles	4,117	593
Other assets	2,015	2,194
Total assets	$ 1,461,082	$ 1,126,667

	December 31 2005	December 31 2004
	(In Thousands)	
Liabilities and stockholders' equity		
Liabilities:		
Deposits	$ 1,069,501	$ 797,701
Advances from the Federal Home Loan Bank	180,960	178,213
Short term borrowings and other interest-bearing liabilities	25,748	14,804
Subordinated debentures	20,619	--
Advance payments by borrowers	605	278
Deferred taxes	795	934
Other liabilities	11,638	7,863
Total liabilities	1,309,866	999,793
Stockholders' equity:		
Preferred stock, no par value per share: 5,000 shares authorized; no shares issued		
Common stock, $.01 par value per share: 20,000 shares authorized; 11,701 and 10,982 shares issued and 7,085 and 6,280 shares outstanding, respectively	117	110
Additional paid-in capital	108,628	88,528
Stock acquired by ESOP	(1,053)	(1,479)
Deferred compensation	(2)	(4)
Accumulated other comprehensive income (loss), net of tax of $(13) and $1,148, respectively	(22)	2,131
Retained earnings	112,041	106,598
Treasury stock, at cost, 4,616 and 4,702 shares respectively	(68,493)	(69,010)
Total stockholders' equity	151,216	126,874
Total liabilities and stockholders' equity	$ 1,461,082	$ 1,126,667

See accompanying notes.

First Defiance Financial Corp.

Consolidated Statements of Income

	Years Ended December 31 2005	2004	2003
	(In Thousands, Except Per Share Amount)		
Interest income			
Loans	$ 69,708	$ 47,345	$ 41,165
Investment securities	5,273	6,731	8,491
Interest-bearing deposits	364	43	280
FHLB stock dividends	829	612	695

Total interest income	76,174	54,731	50,631
Interest expense			
Deposits	20,615	12,950	13,435
Federal Home Loan Bank advances and other	7,625	7,317	7,343
Subordinated debentures	201	--	--
Notes payable	451	114	77
Total interest expense	28,892	20,381	20,855
Net interest income	47,282	34,350	29,776
Provision for loan losses	1,442	1,548	1,719
Net interest income after provision for loan losses	45,840	32,802	28,057
Noninterest income			
Service fees and other charges	5,603	4,215	3,504
Mortgage banking income	3,345	2,771	6,771
Insurance commissions	4,185	4,052	3,712
Gain on sale of securities	1,222	1,426	1,575
Trust income	282	225	161
Income from bank owned life insurance	765	947	809
Other noninterest income	523	360	309
Total noninterest income	15,925	13,996	16,841
Noninterest expense			
Compensation and benefits	23,446	17,422	16,120
Occupancy	4,651	3,294	3,040
SAIF deposit insurance premiums	136	40	183
State franchise tax	1,285	868	1,118
Acquisition related charges	3,476	--	--
Data processing	3,247	2,363	1,841
Amortization of intangibles	755	110	70
Settlement of contingent liability	--	1,927	--
Other noninterest expense	6,946	5,176	4,754
Total noninterest expense	43,942	31,200	27,126
Income before income taxes	17,823	15,598	17,772
Federal income taxes	5,853	4,802	5,690
Net income	$ 11,970	$ 10,796	$ 12,082
Earnings per share:			
Basic	$ 1.75	$ 1.77	$ 2.00
Diluted	$ 1.69	$ 1.69	$ 1.91
Dividends declared per share	$ 0.90	$ 0.82	$ 0.65

See accompanying notes.

First Defiance Financial Corp.

Consolidated Statements of Stockholders' Equity

(In Thousands)

				Stoc
	Common Stock	Treasury Stock	Additional Paid-In Capital	ESOP
Balance at January 1, 2003	$ 110	$ (63,782)	$ 86,255	$ (2,3
Comprehensive income:				
Net income	--	--	--	
Change in net unrealized gains and losses on available-for-sale securities, net of income taxes of $(1,314) (a)	--	--	--	
Total comprehensive income				
ESOP shares released	--	--	596	4
Amortization of deferred compensation of Management Recognition Plan, including income tax benefit of $31	--	--	31	
Shares issued under stock option plan, including income tax benefit of $236	--	1,931	236	
Acquisition of common stock for treasury	--	(4,406)	--	
Dividends declared	--		--	
Balance at December 31, 2003	110	(66,257)	87,118	(1,9
Comprehensive income:				
Net income	--	--	--	
Change in net unrealized gains and losses on available-for-sale securities, net of income taxes of ($1,015) (a)	--	--	--	
Total comprehensive income				
ESOP shares released	--	--	845	4
Amortization of deferred compensation of Management Recognition Plan, including income tax benefit of $12	--	--	12	
Shares issued under stock option plan, including income tax benefit of $553	--	1,938	553	
Acquisition of common stock for treasury	--	(4,691)	--	
Dividends declared	--	--	--	
Balance at December 31, 2004	110	(69,010)	88,528	(1,4
Comprehensive income:				
Net income	--	--	--	
Change in net unrealized gains and losses on available-for-sale securities, net of income taxes of ($1,015) (a)	--	--	--	
Total comprehensive income				
ESOP shares released	--	--	924	4
Shares issued to acquire ComBanc, Inc.	7	186	18,911	
Amortization of deferred compensation of Management Recognition Plan, including income tax benefit of $4	--	--	4	
Shares issued under stock option plan, including income tax benefit of $261	--	1,878	261	
Acquisition of common stock for treasury	--	(1,547)	--	

Dividends declared	--	--	--	
Balance at December 31, 2005	$ 117	$ (68,493)	$ 108,628	$ (1,0

	Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Total Stockholders' Equity
Balance at January 1, 2003	$ 6,455	$ 93,489	$ 120,110
Comprehensive income:			
Net income	--	12,082	12,082
Change in net unrealized gains and losses on available-for-sale securities, net of income taxes of $(1,314) (a)	(2,438)	--	(2,438)
Total comprehensive income			9,644
ESOP shares released	--	--	1,079
Amortization of deferred compensation of Management Recognition Plan, including income tax benefit of $31	--	--	50
Shares issued under stock option plan, including income tax benefit of $236	--	(436)	1,731
Acquisition of common stock for treasury	--	--	(4,406)
Dividends declared	--	(3,939)	(3,939)
Balance at December 31, 2003	4,017	101,196	124,269
Comprehensive income:			
Net income	--	10,796	10,796
Change in net unrealized gains and losses on available-for-sale securities, net of income taxes of ($1,015) (a)	(1,886)	--	(1,886)
Total comprehensive income			8,910
ESOP shares released	--	--	1,270
Amortization of deferred compensation of Management Recognition Plan, including income tax benefit of $12	--	--	19
Shares issued under stock option plan, including income tax benefit of $553	--	(383)	2,108
Acquisition of common stock for treasury	--	--	(4,691)
Dividends declared	--	(5,011)	(5,011)
Balance at December 31, 2004	2,131	106,598	126,874
Comprehensive income:			
Net income	--	11,970	11,970
Change in net unrealized gains and losses on available-for-sale securities, net of income taxes of ($1,015) (a)	(2,153)	--	(2,153)
Total comprehensive income			9,817
ESOP shares released	--	--	1,350
Shares issued to acquire ComBanc, Inc.	--	--	19,104
Amortization of deferred compensation of Management Recognition Plan, including income tax benefit of $4	--	--	6
Shares issued under stock option plan, including income tax benefit of $261	--	(317)	1,822

Acquisition of common stock for treasury	--	--	(1,547)
Dividends declared	--	(6,210)	(6,210)
Balance at December 31, 2005	$ (22)	$ 112,041	$ 151,216

(a) Net of reclassification adjustments. Reclassification adjustments represent net unrealized gains (losses) as of December 31 of the prior year on securities available-for-sale that were sold during the current year. The reclassification adjustment was $1.3 million ($844,000 after tax) in 2005, $1.82 million ($1.18 million after tax) in 2004 and$1.39 million ($905,000 after tax) in 2003.

See accompanying notes.

First Defiance Financial Corp.

Consolidated Statements of Cash Flows

	Years Ended December	
	2005	2004
		(In Thousands)
Operating activities		
Net income	$ 11,970	$ 10,796
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	1,442	1,548
Provision for depreciation	2,396	1,798
Net amortization of premium and discounts on loans, securities, deposits and debt obligations	1,152	564
Amortization of mortgage servicing rights	784	704
Net impairment (recovery) of mortgage servicing rights	(417)	1
Amortization of intangibles	755	110
Gain on sale of loans	(2,426)	(2,523)
Amortization of Management Recognition Plan deferred compensation	6	19
Gain on sale of property, plant and equipment	(116)	--
FHLB stock dividends	(835)	(610)
Release of ESOP shares	1,350	1,270
Gains on sales of securities	(1,222)	(1,426)
Deferred federal income tax	249	90
Proceeds from sale of loans	112,731	106,620
Origination of loans held for sale	(114,332)	(101,391)
Income from bank owned life insurance	(765)	(947)
Change in interest receivable and other assets	1,285	(136)
Change in accrued interest and other liabilities	2,574	(234)
Net cash provided by operating activities	16,581	16,253
Investing activities		
Proceeds from maturities of held-to-maturity securities	357	403
Proceeds from maturities of available-for-sale securities	27,882	42,850
Proceeds from sale of available-for-sale securities	24,160	20,747

Proceeds from sale of real estate and other assets held for sale	475	996
Proceeds from sale of office properties and equipment	1,286	2
Proceeds from sale of discontinued operations	--	--
Purchases of available-for-sale securities	(30,271)	(34,262)
Proceeds from sale of Federal Home Loan Bank stock	--	5,000
Purchases of office properties and equipment	(5,296)	(2,202)
Investment in bank owned life insurance	(5,000)	--
Proceed from insurance death benefit	--	318
Acquisition of banking center offices	--	--
Net cash received for acquisition of ComBanc, Inc.	52,687	--
Net cash paid for acquisition of Genoa Savings and Loan Co.	(612)	--
Net increase in loans receivable	(104,103)	(144,660)
Net cash (used in) provided by investing activities	(38,435)	(110,808)

First Defiance Financial Corp.

Consolidated Statements of Cash Flows (continued)

	Years Ended December	
	2005	2004
Financing activities		
Net increase (decrease) in deposits	31,931	69,090
Repayment of Federal Home Loan Bank long-term advances	(2,457)	(1,809)
Repayment of term notes payable	--	--
Net increase in Federal Home Loan Bank short-term advances	2,000	15,500
Net increase (decrease) in short-term line of credit	(3,000)	3,000
Proceeds from Federal Home Loan Bank long-term advances	--	--
Increase (decrease) in securities sold under repurchase agreements	7,334	(463)
Proceeds from issuance of subordinated debentures	20,619	--
Purchase of common stock for treasury	(1,547)	(4,691)
Cash dividends paid	(5,852)	(4,889)
Proceeds from exercise of stock options	1,561	1,555
Net cash provided by (used in) financing activities	50,589	77,293
Increase (decrease) in cash and cash equivalents	28,735	(17,262)
Cash and cash equivalents at beginning of period	20,521	37,783
Cash and cash equivalents at end of period	$ 49,256	$ 20,521
Supplemental cash flow information		
Interest paid	$ 28,327	$ 20,432
Income taxes paid	$ 5,053	$ 4,149
Transfers from loans to other real estate owned and other assets held for sale	$ 605	$ 690

First Defiance acquired all of the capital stock ComBanc Inc. and the Genoa Savings and Loan Company for $38.3 million and $11.2 million respectively in 2005. In conjunction with the acquisitions, liabilities were assumed as follows:

	ComBanc	Genoa	Total
Fair value of assets acquired	$ 213,927	$ 88,077	$ 302,004
Purchase price	(38,339)	(11,212)	(49,551)
Liabilities assumed	$ 175,588	$ 76,865	$ 252,453

In 2003, First Defiance acquired three banking center offices from another bank in a cash transaction. Liabilities assumed in that transaction, which consisted solely of deposits, totaled $166.7 million.

See accompanying notes.

First Defiance Financial Corp.

Notes to Consolidated Financial Statements

December 31, 2005, 2004 and 2003

1. Basis of Presentation

First Defiance Financial Corp. (First Defiance) is a holding company that conducts business through its two wholly owned subsidiaries, First Federal Bank of the Midwest, Defiance Ohio (First Federal) and First Insurance & Investments (First Insurance). 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 and trust services. First Insurance & Investments is an insurance agency that does business in the Defiance, Ohio area offering property and casualty, group health, and life insurance and investment and annuity products.

2. Statement of Accounting Policies

Use of Estimates

The preparation of consolidated financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates. Significant areas where First Defiance uses estimates are the determination of the allowance for loan losses, the valuation of mortgage servicing rights and goodwill, and the determination of post-retirement benefits.

Earnings Per Share

Earnings per share are based on the weighted average number of shares of common stock outstanding during the period. Basic earnings per share exclude any dilutive effects of options and unvested stock grants. Diluted earnings per common share includes the dilutive effect of additional potential common shares issuable under stock options and stock grants. Unreleased shares held by the Company's Employee Stock Ownership Plan are not included in average shares for purposes of calculating earnings per share. As shares are released for allocation, they are included in the average shares outstanding. Also see note 17.

Comprehensive Income

Comprehensive income consists of net income and other comprehensive income. Other comprehensive income includes unrealized gains and losses on securities available for sale.

Cash and Cash Equivalents

Cash and cash equivalents include amounts due from banks and overnight investments with the Federal Home Loan Bank (FHLB). Cash and amounts due from depository institutions includes required balances at the FHLB and Federal Reserve of approximately $175,000 and $100,000, respectively, at December 31, 2005. 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 a separate component of stockholders' equity until realized. Realized gains and losses, and unrealized losses judged to be other-than-temporary, are included in gains (losses) on securities. Realized gains and losses on securities sold is based on the specific identification method.

Currently, First Defiance invests in derivative securities as part of the overall asset and liability management process. Such derivative securities are disclosed in Note 5 and include agency step-up, REMIC and CMO investments. Such investments are not classified by management as high risk at December 31, 2005 and do not present risk significantly different than other mortgage-backed or agency securities.

FHLB Stock

As a member of the FHLB System, First Federal is required to own stock of the FHLB of Cincinnati in an amount principally equal to 0.15% of total assets plus an amount of at least 2% but no more than 4% of its non-grandfathered mission asset activity (as defined in the FHLB's regulations). First Federal is permitted to own stock in excess of the minimum requirement. FHLB stock is a restricted equity security that does not have a readily determinable fair value and is carried at cost.

Loans Receivable

Loans are reported at the principal amount outstanding, net of deferred loan fees and costs and the allowance for loan losses. Deferred fees net of deferred incremental loan origination costs, is amortized to interest income generally over the contractual life of the loan using the interest method.

2. Statement of Accounting Policies (continued)

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 cost or estimated fair value in the aggregate.

Interest receivable is accrued on loans and credited to income as earned. The accrual of interest on impaired loans is discontinued when, in management's opinion, the borrower may be unable to meet payments as they become due. When interest accrual is discontinued, all unpaid accrued interest is reversed. Interest income is subsequently recognized 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.

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 regulatory guidance and 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.

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 losses 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.

A loan is impaired when full payment under the loan terms is not expected. 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, at 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.

Acquired Loans

Valuation allowances for all acquired loans subject to SOP 03-3 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. Valuation allowances are established only subsequent to acquisition of the 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. 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.

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.

Marketing Costs

Marketing costs totaled $1.04 million, $592,000, and $524,000, in 2005, 2004, and 2003, respectively, and are expensed as incurred.

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 now are such matters that will have a material effect on the financial statements.

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First Defiance Financial Corp.

Notes to Consolidated Financial Statements (continued)

2. Statement of Accounting Policies (continued)

Dividend Restriction

Banking regulations require maintaining certain capital levels and may limit the dividends paid by the bank to the holding company. These restrictions pose no practical limit on the ability of the bank or holding company to pay dividends at historical levels. See Note 19.

Mortgage Servicing Rights

The total cost of loans originated or purchased is allocated between loans and servicing rights based on the relative fair values of each at the time of sale. The servicing rights capitalized are amortized in proportion to and over the period of estimated servicing income.

Mortgage servicing rights are periodically evaluated for impairment. For purposes of measuring impairment, mortgage servicing rights are stratified based on predominant risk characteristics of the underlying serviced loans. These risk characteristics include loan type (fixed or adjustable rate) and interest rate. Impairment represents the excess of amortized cost of an individual mortgage servicing rights stratum over its fair value, and is recognized through a valuation allowance.

Fair values for individual stratum are based on the present value of estimated future cash flows using a discount rate commensurate with the risks involved. Estimates of fair value include assumptions about prepayment, default and interest rates, and other factors which are subject to change over time. Changes in these underlying assumptions could cause the fair value of mortgage servicing rights, and the related valuation allowance, to change significantly in the future.

Real Estate and Other Assets Held for Sale

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

Premises and Equipment and Long Lived Assets

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 evaluated for impairment using the guidance provided by Statement of Financial Accounting Standards (SFAS) No. 144, Accounting for Long-Lived Assets to be Disposed of, relative to accounting for long-lived assets and accounting for long-lived assets to be disposed of either through sale, abandonment, exchange or a distribution to owners.

Income Taxes

Deferred income taxes reflect the temporary tax consequences on future years of differences between the tax basis and financial statement amounts of assets and liabilities at each year-end.

Deferred tax assets and liabilities are reflected at currently enacted income tax rates applicable to the period in which the deferred tax assets or liabilities are expected to be realized or settled. As changes in tax laws or rates are enacted, deferred tax assets and liabilities are adjusted through the provision for income taxes.

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.

Business Combinations

Business combinations, which have been accounted for under the purchase method of accounting, include the results of operations of the acquired business from the date of acquisition. Net assets of companies acquired are recorded at their estimated fair value as of the date of acquisition.

Goodwill and Other Intangibles

Core deposit intangibles are a measure of the value of checking and savings deposits acquired in business combinations accounted for under the purchase method. Core deposit intangibles are amortized on an accelerated basis over the estimated lives of the existing deposit relationships acquired, but not exceeding 10 years. Customer Relationship Intangibles are a measure of the value of customer relationships accounted for under the purchase method. The Customer Relationship Intangible is amortized over the estimated contractual life of the existing relationship and is limited to 10 years. Goodwill is the excess of the purchase price over the fair value of the assets and liabilities of companies acquired through business combinations accounted for under the purchase method. Goodwill is evaluated at the business unit level, which for First Defiance is First Federal Bank and First Insurance. At December 31, 2005 and December 31, 2004, goodwill at First Federal totaled $31.3 million and $14.5 million respectively, core deposit intangibles were $3.6 million and $593,000 respectively in 2005 and 2004 and customer relationship intangibles at December 31, 2005 were $512,000. At December 31, 2005 and 2004 goodwill totaled $3.8 million and $3.8 million respectively at First Insurance.

2. Statement of Accounting Policies (continued)

Core deposit intangibles are amortized over the life of the related deposits, not to exceed ten years. Amortization expense for core deposit intangibles was $693,000, $110,000 and $70,000 in 2005, 2004 and 2003 respectively. Customer relationship intangibles are amortized over the estimated live of the customer relationship, not to exceed 10 years. Amortization expense for customer relationship intangibles in 2005 was $62,000. Amortization of intangibles is expected to total $719,000, $573,000, $469,000, $410,000, and $402,000 in 2006, 2007, 2008, 2009 and 2010 respectively. Goodwill is not subject to amortization but its value is assessed annually to determine if there is any impairment of value.

Settlement of Contingent Liability

First Defiance sold its former Leader Mortgage subsidiary in 2002. During 2004, the Purchaser of that unit asserted certain claims against First Defiance under the Purchase and Sale Agreement. First Defiance settled all matters related to the sale of Leader Mortgage in the 2004 third quarter and it recognized a pre-tax charge of $1.9 million, which is included in the 2004 Consolidated Statement of Income.

Stock Compensation Plans

At December 31, 2005, the Company had four stock-based compensations plans, which are more fully described in Note 18. The Company accounts for those plans under recognition and measurement principles of Accounting Principles Board (APB) Opinion No. 25, Accounting for Stock Issued to Employees and related Interpretations. Under APB No. 25, because the exercise price of the Corporation's employee stock options equals the market price of the underlying stock on the date of the grant, no compensation expense is recognized.

Pro forma information regarding net income and earnings per share is required by SFAS No. 123, Accounting for Stock-Based Compensation and has been determined as if First Defiance had accounted for its employee stock-based compensation plans under the fair value method of that Statement. Under the fair-value based method, compensation cost is measured at the grant date based upon the value of the award and recognized over the service period. For purposes of the pro forma disclosures, the estimated fair value of the option is amortized to expense over the options' vesting period.

The following pro forma results of operations use a fair value method of accounting for stock options in accordance with SFAS No. 123. The estimated fair value of the options are amortized to expense over the option and vesting period. The fair value was estimated at the date of grant using a Black-Scholes option pricing model which was originally developed for use in estimating the fair value of traded options, which have different characteristics from the Company's employee stock options. The model is also sensitive to changes in assumptions, which can materially affect the fair value estimate. The following weighted-average assumptions were used to determine the fair value of options granted during the years presented on First Defiance common stock:

2. Statement of Accounting Policies (continued)

	December 31,		
	2005	2004	2003
Risk free interest rate	4.40%	4.73%	4.39%
Dividend yield	3.39%	2.96%	3.01%
Volatility factors of expected market price of stock	22.4%	22.9%	22.7%
Weighted average expected life	10 years	10 years	10 years
Weighted average grant date fair value of options granted	$ 5.67	$ 6.85	$ 4.97

Based upon the above assumptions, pro forma net income and earnings per share are as follows:

	Years Ended December 31		
	2005	2004	2003
Net income	$ 11,970	$ 10,796	$ 12,082
Stock-based compensation using the fair value method, net of tax	(268)	(222)	(186)
Pro forma net income	$ 11,702	$ 10,574	$ 11,896
Earnings per share as reported:			
Basic	$ 1.75	$ 1.77	$ 2.00
Diluted	$ 1.69	$ 1.69	$ 1.91
Pro forma earnings per share:			
Basic	$ 1.71	$ 1.74	$ 1.97
Diluted	$ 1.65	$ 1.66	$ 1.88

Company Owned Life Insurance

The Company has purchased life insurance policies on certain key executives. Company owned life insurance is recorded at its cash surrender value, or the amount that can be realized.

Fair Value of Financial Instruments

Fair values of financial instruments are estimated using relevant market information and other assumptions, as more fully disclosed in a separate note. 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.

2. Statement of Accounting Policies (continued)

Operating Segments

While the chief decision-makers monitor the revenue streams of the various products and services, the identifiable segments are not material and operations are managed and financial performance is evaluated on a Company-wide basis. Accordingly, all of the financial service operations are considered by management to be aggregated in one reportable segment.

Reclassifications

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

Recent Accounting Pronouncements

Accounting for Stock Compensation

In December 2004, the FASB revised SFAS 123, Accounting for Stock-Based Compensation. SFAS No. 123(R), Share-Based Payments which replaces SFAS No. 123 and supersedes APB Opinion No. 25 establishes accounting requirements for share-based compensation to employees and carries forward prior guidance on accounting for awards to non-employees. In 2005, the FASB issued further guidance on the classification and measurement of freestanding financial instruments originally issued for employee service and the application of grant date as defined in SFAS 123(R). First Defiance will be required to adopt this statement on January 1, 2006. The pro forma disclosures previously permitted under SFAS No. 123 no longer will be an alternative to financial statement recognition. Under SFAS No. 123(R), the Company must determine the appropriate fair value model to be used for valuing share-based payments, the amortization method for compensation cost and the transition method to be used at date of adoption.

The permitted transition methods include either retrospective or prospective adoption. Under the retrospective option, prior periods may be restated either as of the beginning of the year of adoption or for all periods presented. The prospective method requires that compensation expense be recorded for all unvested stock options at the beginning of the first quarter of adoption of SFAS No. 123R, while the retrospective methods would record compensation expense for all unvested stock options beginning with the first period presented. The Company plans to use the retrospective method and no prior periods will be adjusted. Management does not believe that the adoption of SFAS No. 123R will result in share-based expense amounts that are materially different than the current pro forma disclosures under SFAS No. 123 set forth above. See Note 18 for additional information regarding stock options outstanding at year-end.

First Defiance Financial Corp.

Notes to Consolidated Financial Statements (continued)

2. Statement of Accounting Policies (continued)

Meaning of Other Than Temporary Impairment

In November 2005, the Financial Accounting Standards Board (FASB) issued FASB Staff Position (FSP) 115-1, The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments. This FSP provides additional guidance on when an investment in a debt or equity securities should be considered impaired and when that impairment should be considered other-than-temporary and recognized as a loss in earnings. Specifically, the guidance clarifies that an investor should recognize an impairment loss no later than when the impairment is deemed other-than-temporary, even if a decision to sell has not been made. The FSP also requires certain disclosures about unrealized losses that have not been recognized as other-than-temporary impairments. Management has applied the guidance in this FSP in the 2005 financial statements.

Accounting Changes and Error Corrections

In May 2005, the FASB issued SFAS 154, Accounting Changes and Error Corrections, which changes the accounting for and reporting of a change in accounting principle. This statement applies to all voluntary changes in accounting principle and changes required by an accounting pronouncement in the unusual instance that the pronouncement does not include specific transition provisions. This statement requires retrospective application to prior period financial statements of changes in accounting principle, unless it is impractical to determine either the period-specific or cumulative effects of the change. SFAS 154 is effective for accounting changes made in fiscal years beginning after December 15, 2005. The adoption of this standard is not expected to have a material effect on financial condition, results of operations, or liquidity of the Company.

Accounting For Certain Loans or Debt Securities Acquired in a Transfer

In December 2003, the American Institute of Certified Public Accountants issued Statement of Position (SOP) 03-3, Accounting for Certain Loans or Debt Securities Acquired in a Transfer. SOP 03-3 requires acquired loans, including debt securities, to be recorded at the amount of the purchaser's initial investment and prohibits carrying over valuation allowances from the seller for those individually evaluated loans that have evidence of deterioration in credit quality since origination, and it is probable all contractual cash flows on the loan will be unable to be collected. SOP 03-3 also requires the excess of all undiscounted cash flows expected to be collected at acquisition over the purchaser's initial investment to be recognized as interest income on a level-yield basis over the life of the loan. Subsequent increases in cash flows expected to be collected are recognized prospectively through an adjustment of the loan's yield over its remaining life, while subsequent decreases are recognized as impairment. Loans carried at fair value, mortgage loans held for sale, and loans to borrowers in good standing under revolving credit agreements are excluded from the scope of SOP 03-3. The Corporation adopted the provisions of SOP 03-03 effective January 1, 2005. See Note 7 for further details.

First Defiance Financial Corp.

Notes to Consolidated Financial Statements (continued)

3. Acquisitions

On April 8, 2005, The Company acquired the Genoa Savings and Loan Company ("Genoa"), a savings and loan headquartered in Genoa, Ohio for a total purchase price of $11.2 million including direct acquisition costs of $220,000. Genoa shareholders received cash of $11.0 million in the all-cash transaction.

On January 21, 2005, First Defiance acquired ComBanc, Inc. ("ComBanc"), a bank-holding company and its wholly-owned subsidiary, the Commercial Bank by acquiring all of the outstanding capital stock of ComBanc for an aggregate purchase price of $38.3 million, including direct acquisition costs of $542,000. ComBanc shareholders received 733,775 shares of First Defiance stock and cash of $18.7 million.

The acquisitions enhance First Defiance's community bank operations by giving them a larger presence in the Toledo, Ohio market area following the Genoa acquisition and allowing them to expand into the Allen County, Ohio area, which is adjacent to existing markets, following the ComBanc acquisition. The value of the common stock issued for the ComBanc acquisition was determined based on an average of the closing price for two days before and after the date the final exchange terms were determined. The following table presents the allocation of the purchase price, including direct acquisition costs, for the Genoa and ComBanc acquisitions to assets acquired and liabilities assumed, based on their fair values:

	Genoa	ComBanc
	(in thousands)	
Assets		
Cash and cash equivalents	$ 10,600	$ 71,915
Investment securities	15	502
Loans, net of allowances for loan losses	66,905	117,494
Premises and equipment	2,345	4,106
Goodwill and other intangibles	5,501	15,522
Other assets	2,711	4,388
Total assets acquired	88,077	213,927
Liabilities		
Deposits	76,786	163,668
Borrowings	--	9,863
Other liabilities	79	2,057
Total liabilities acquired	76,865	175,588
Net assets acquired	$ 11,212	$ 38,339

First Defiance Financial Corp.

Notes to Consolidated Financial Statements (continued)

3. Acquisitions (continued)

	Genoa	ComBanc
	(in thousands)	
Purchase price	$ 11,212	$ 38,339
Carrying value of net assets acquired	(6,737)	(22,615)
Excess of purchase price over carrying value of net assets acquired	4,475	15,724
Purchase accounting adjustments:		
Portfolio loans	978	1,668
Investment securities	--	9
Premises and equipment	(1,620)	651
Mortgage servicing rights	116	49
Deposits	(301)	(322)
Borrowings	--	(211)
Deferred tax liabilities	(199)	(1,642)
Total net tangible assets	(1,026)	202
Core deposit and customer relationship intangibles	1,202	3,077
Goodwill	$ 4,299	$ 12,445

The following (unaudited) pro forma consolidated results of operations have been prepared as if the acquisitions of ComBanc and Genoa occurred as of the beginning of each period presented.

	December 31	
	2005	2004
	(in thousands, except per share amounts)	
Net interest income	$ 48,542	$ 44,085
Net income	$ 13,775	$ 10,057
Net income per share - basic	$ 2.00	$ 1.47
Net income per share - Diluted	$ 1.93	$ 1.42

3. Acquisitions (continued)

The pro forma results include amortization of fair value adjustments on loans, deposits and FHLB advances, amortization of newly created intangibles, and post-merger acquisition related charges. The pro forma average common shares outstanding used to compute the pro forma basic and diluted income per share includes adjustments for shares issued for the ComBanc acquisition. The pro forma results presented do not include $3.5 million of acquisition related costs included in First Defiance's 2005 income statement, nor do they reflect cost savings or revenue enhancements anticipated from the acquisitions. These pro forma results are not necessarily indicative of what actually would have occurred if the acquisitions had been completed as of the beginning of each period presented, nor are they necessarily indicative of future results.

On February 22, 2003, First Defiance entered into a purchase and assumption agreement with RFC Banking Company and its parent Rurban Financial Corp. to acquire banking center offices located in Findlay, Ottawa and McComb, Ohio and related deposit liabilities, certain loans and other assets associated with the business of those branches. On June 6, 2003, First Defiance completed the purchase of the banking center offices and the reported results include the operations of these acquired banking centers assets and liabilities from that acquisition date and thereafter. Total deposits acquired through the acquisition were $166.7 million. Additionally, loan balances acquired by First Defiance in the transaction were approximately $79 million, which included $35.4 million of non-residential real estate loans, $16.8 million of commercial loans, $3.6 million of consumer loans, $1.8 million of home equity loans and $21.4 million of residential mortgages. Other assets acquired included $2.0 million of premises and equipment and $443,000 of interest receivable and other assets. Cash received, net of the premium paid, was $70.1 million. Total consideration for the acquisition was 10.5% of acquired non-brokered deposits plus an agreed upon amount for all furnishings and equipment.

As of the final closing, First Defiance paid a net premium of $12.5 million and recorded fair value increases (reductions) on acquired loans of ($1.2) million and acquired deposits of $2.3 million to record them at fair value and recorded transaction costs and other adjustments of approximately $900,000. These items resulted in total intangibles of $16.9 million including goodwill of $16.1 million and a core deposit intangible of $772,000. During 2004, First Defiance recorded adjustments to the original purchase price, reducing goodwill balances by $1.6 million. The core deposit is being amortized over 10 years and goodwill was recorded in accordance with SFAS No. 142 and accordingly is not subject to amortization. All intangible assets acquired as part of this acquisition are deductible for Federal income tax purposes over 15 years.

4. Earnings Per Share

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

	2005	2004	2003
	(In Thousands, Except Per Share Amounts)		
Numerator for basic and diluted earnings per share-net income	$ 11,970	$ 10,796	$ 12,082
Denominator:			
Denominator for basic earnings per share-weighted-average shares	6,843	6,094	6,036
Effect of dilutive securities:			
Employee stock options	252	275	277
Unvested Management Recognition Plan stock	1	2	6

Dilutive potential common shares	253	277	283
Denominator for diluted earnings per share-adjusted weighted-average shares	7,096	6,371	6,319
Basic earnings per share	$ 1.75	$ 1.77	$ 2.00
Diluted earnings per share	$ 1.69	$ 1.69	$ 1.91

First Defiance Financial Corp.

Notes to Consolidated Financial Statements (continued)

5. Investment Securities

The following is a summary of available-for-sale and held-to-maturity securities:

	December 31, 2005			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fai Val
	(In Thousands)			
Available-for-sale securities:				
U.S. treasury securities and obligations of U.S. government corporations and agencies	$ 41,173	$ 217	$ (325)	$ 4
Mortgage-backed securities	19,959	35	(263)	1
REMICs	998	--	(7)	
Collateralized mortgage obligations	20,002	1	(330)	1
Trust preferred stock	7,725	76	--	
Obligations of state and political subdivisions	23,257	574	(13)	2
Totals	$ 113,114	$ 903	$ (938)	$ 11
Held-to-maturity securities:				
FHLMC certificates	$ 333	$ 11	$ --	$
FNMA certificates	756	4	(3)	
GNMA certificates	241	--	(1)	
Obligations of states and political subdivisions	445	59	--	
Totals	$ 1,775	$ 74	$ (4)	$

First Defiance Financial Corp.

Notes to Consolidated Financial Statements (continued)

5. Investment Securities (continued)

	December 31, 2004		
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses
	(In Thousands)		
Available-for-sale securities:			
U.S. treasury securities and obligations of U.S. government corporations and agencies	$ 48,913	$ 1,461	$ (61)
Corporate bonds	6,158	310	--
Mortgage-backed securities	16,645	151	(16)
REMICs	4,902	--	(26)
Collateralized mortgage obligations	20,027	136	(54)
Trust preferred stock	6,228	64	--
Equity securities	69	4	--
Obligations of state and political subdivisions	30,781	1,313	(2)
Totals	$ 133,723	$ 3,439	$ 159
Held-to-maturity securities:			
FHLMC certificates	$ 459	$ 21	$ (1)
FNMA certificates	960	12	(4)
GNMA certificates	306	4	(1)
Obligations of states and political subdivisions	530	90	--
Totals	$ 2,255	$ 127	$ (6)

The amortized cost and fair value of securities at December 31, 2005 by contractual maturity are shown below. Expected maturities will differ from contractual maturities because borrowers 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 the underlying collateral. The mortgage-backed securities may mature earlier than their weighted-average contractual maturities because of principal prepayments.

5. Investment Securities (continued)

	Available-for-Sale		Held-to-Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
	(In Thousands)			
Due in one year or less	$ 14,200	$ 14,027	$ 449	$ 455
Due after one year through five years	60,715	60,516	923	959
Due after five years through ten years	17,200	17,244	357	384
Due after ten years	20,999	21,292	46	47
	113,114	113,079	1,775	1,845

Investment securities with carrying amounts of $82.3 million and $91.9 million at December 31, 2005 and 2004, respectively, were pledged as collateral on public deposits, securities sold under repurchase agreements and FHLB advances and for other purposes required or permitted by law.

First Defiance Financial Corp.

Notes to Consolidated Financial Statements (continued)

5. Investment Securities (continued)

The following table summarizes First Defiance's securities that were in an unrealized loss position at December 31, 2005 and December 31, 2004:

	Duration of Unrealized Loss Position			
	Less than 12 Months		12 Month or Longer	
	Fair Value	Gross Unrealized Loss	Fair Value	Gross Unreali Loss
			(In Thousands)	
At December 31, 2005				
Available-for-sale securities:				
U.S. treasury securities and obligations of U.S. government corps and agencies	$ 16,873	$ (173)	$ 8,845	$ (15
Mortgage-backed securities	9,488	(151)	4,352	(11
Collateralized mortgage obligations and REMICs	5,780	(62)	11,687	(27
Obligations of state and political				

subdivisions	1,368	(13)	20	-
Held to maturity securities:				
Agency certificates	320	(1)	177	(
Total temporarily impaired securities	$ 33,829	$ (400)	$ 25,081	$ (54
At December 31, 2004				
Available-for-sale securities:				
U.S. treasury securities and obligations of U.S. government corps and agencies	$ 16,817	$ (61)	$ --	$ -
Mortgage-backed securities	3,312	(6)	759	(1
Collateralized mortgage obligations and REMICs	11,601	(80)	--	-
Obligations of state and political subdivisions	510	(1)	158	(
Held to maturity securities:				
Agency certificates	124	(2)	253	(
Total temporarily impaired securities	$ 32,364	$ (150)	$ 1,170	$ (1

The above securities all have fixed interest rates and 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. Realized gains from the sale of investment securities totaled $1.2 million, $1.4 million and $1.6 million in 2005, 2004 and 2003 respectively. Realized losses from securities transactions were $5,000 in 2005 and $65,000 in 2003. There were no realized losses during 2004.

6. Commitments and Contingent Liabilities

Loan Commitments

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

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

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

	2005	2004

Loan commitments	$ 275,982	$ 186,404
Standby letters of credit	8,785	9,921
Total	$ 284,767	$ 196,325

Lease Agreements

The Company has entered into lease agreements covering First Insurance's main office, one banking center location and the land on which one banking center was constructed and numerous stand-alone Automated Teller Machine sites with varying terms and options to renew.

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

2006	$ 344
2007	269
2008	207
2009	214
2010	192
Thereafter	3,263
Total	$ 4,489

Rentals under operating leases and data processing costs amounted to $329,000, $237,000, and $195,000, in 2005, 2004, and 2003, respectively.

7. Loans Receivable

	December 31	
	2005	2004
	(In Thousands)	
Loans receivable consist of the following at December 31:		
Real estate loans:		
Secured by single family residential	$ 275,497	$ 187,775
Secured by multi-family residential	50,040	39,049
Secured by non-residential real estate	501,943	376,115
Construction	21,173	15,507
	848,653	618,446
Other loans:		
Automobile	37,584	34,391
Commercial	171,289	141,644
Home equity and improvement	113,000	90,839
Other	17,713	11,121

	339,586	277,995
Total loans	1,188,239	896,441
Deduct:		
Undisbursed loan funds	(8,782)	(6,341)
Net deferred loan origination fees and costs	(1,303)	(1,232)
Allowance for loan losses	(13,673)	(9,956)
Totals	$ 1,164,481	$ 878,912

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First Defiance Financial Corp.

Notes to Consolidated Financial Statements (continued)

7. Loans Receivable (continued)

Changes in the allowance for loan losses were as follows:

	Years Ended December 31		
	2005	2004	2003
	(In Thousands)		
Allowance at beginning of year	$ 9,956	$ 8,844	$ 7,496
Provision for credit losses	1,442	1,548	1,719
Acquired in acquisitions	3,027	--	--
Charge-offs	1,054	685	725
Recoveries	302	249	354
Net charge-offs	752	436	371
Ending allowance	$ 13,673	$ 9,956	$ 8,844

Unpaid balances of loans with contractual payments delinquent 90 days or more totaled $5.0 million at December 31, 2005 and $1.9 million at December 31, 2004.

Impaired loans having recorded investments of $822,000 at December 31, 2005 and $505,000 at December 31, 2004, have been recognized in conformity with FASB Statement No. 114, as amended by FASB Statement No. 118. The average recorded investment in impaired loans during 2005, 2004 and 2003 was $1.1 million, $732,000, and $892,000 respectively. The total allowance for loan losses related to these loans was $380,000 and $253,000 at December 31, 2005 and 2004. There was $61,000, $36,000 and $29,000 of interest received and recorded in income during 2005, 2004 and 2003 respectively on impaired loans during the impairment period. Loans having carrying values of $605,000 and $690,000 were transferred to real estate and other assets held for sale in 2005 and 2004, respectively. At December 31, 2005 and December 31, 2004, non-performing loans were $5.0 million and $1.9 million respectively. There was no accrued interest recorded on impaired or non-performing loans at December 31, 2005 or 2004. Also there were no loans deemed impaired for which there was no allowance for loan loss allocation at December 31, 2005 or 2004.

First Defiance is not committed to lend additional funds to debtors whose loans have been modified.

7. Loans Receivable (continued)

Certain loans acquired in the ComBanc and Genoa acquisitions had evidence that the credit quality of the loan had deteriorated since its origination and in management's assessment at the acquisition date it was probable that the First Defiance would be unable to collect all contractually required payments due. In accordance with American Institute of Certified Public Accountants Statement of Position 03-3 - Accounting for Certain Loans or Debt Securities Acquired in a Transfer (SOP 03-3), these loans have been recorded based on management's estimate of the fair value of the loans. Detail of these loans are as follows:

	Contractual Amount Receivable	Impairment Discount	Recorded Loan Receivable
	(in thousands)		
Amounts recorded in acquisition:			
Genoa	$ 1,547	$ 812	$ 735
ComBanc	3,426	1,376	2,050
Total acquired	4,973	2,188	2,785
Principal payments received	(175)	--	(175)
Loans written down	(169)	(169)	--
Loan accretion recorded	--	--	--
Balance at December 31, 2005	$ 4,629	$ 2,019	$ 2,610

In determining the fair value of these loans, management evaluated the likelihood of receiving full payment under the contractual terms. Because of the nature of the types of loans identified, estimates of specific cash flows are not readily determinable. The loans acquired that are within the scope of SOP 03-3 are not accounted for using the income recognition model of the SOP because the Company cannot reasonably estimate cash flows expected to be collected.

Interest income on loans is as follows:

	Years Ended December 31		
	2005	2004	2003
	(In Thousands)		
Commercial and non-residential real-estate loans	$ 49,869	$ 34,506	$ 28,145
Mortgage loans	9,549	6,272	7,144
Other loans	10,290	6,567	5,876
Totals	$ 69,708	$ 47,345	$ 41,165

There are no industry concentrations (exceeding 10% of gross loans) in First

Federal's non-residential real estate and commercial loan portfolios. The Company's loans receivable are primarily to borrowers in the Northwest Ohio, Northeast Indiana or Southeast Michigan areas.

Outstanding loan balances at December 31, 2005 and 2004 include loans to executive officers and directors and their affiliates totaling $5.25 million and $5.30 million respectively. All such loans are paying as agreed.

8. Mortgage Banking

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

	Years Ended December 31		
	2005	2004	2003
	(In Thousands)		
Gain from sale of mortgage loans	$ 2,291	$ 2,350	$ 7,047
Mortgage loan servicing revenue (expense):			
Mortgage loan servicing revenue	1,421	1,126	976
Amortization of mortgage servicing rights	(784)	(704)	(1,998)
Mortgage servicing rights valuation adjustments	417	(1)	746
	1,054	421	(276)
Net revenue from sale and servicing of mortgage loans	$ 3,345	$ 2,771	$ 6,771

The unpaid principal balance of residential mortgage loans serviced for third parties was $602.5 million at December 31, 2005 compared to $463.8 million at December 31, 2004.

	Years Ended December 31		
	2005	2004	2003
	(In Thousands)		
Mortgage servicing assets:			
Balance at beginning of period	$ 4,205	$ 4,037	$ 3,442
Loans sold, servicing retained	906	872	2,593
NBV of servicing assets acquired	926	--	--
Impairment deemed permanent	(108)	--	--
Amortization	(784)	(704)	(1,998)
Carrying value before valuation allowance			

at end of period	5,145	4,205	4,037
Valuation allowance:			
Balance at beginning of period	(607)	(606)	(1,352)
Impairment recovery (charges)	417	(1)	746
Impairment deemed permanent	108	--	--
Balance at end of period	(82)	(607)	(606)
Net carrying value of MSRs at end of period	$ 5,063	$ 3,598	$ 3,431
Fair value of MSRs at end of period	$ 6,471	$ 3,743	$ 3,573

First Defiance Financial Corp.

Notes to Consolidated Financial Statements (continued)

8. Mortgage Banking (continued)

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

	December 31			
	2005		2004	
Investor	Number of Loans	Principal Outstanding	Number of Loans	Principal Outstanding
		(Dollars in Thousands)		
Fannie Mae	601	$ 39,094	562	$ 34,351
Freddie Mac	6,858	562,199	5,148	429,439
Other	52	1,218	--	--
Totals	7,511	$ 602,511	5,710	$ 463,790

Significant assumptions at December 31, 2005 used in determining the value of MSRs include a weighted average prepayment rate of 189 PSA and a weighted average discount rate of 8.95%.

A sensitivity analysis of the current fair value to immediate 10% and 20% adverse changes in those assumptions as of December 31, 2005 is presented below. These sensitivities are hypothetical. Changes in fair value based on a 10% 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

	(Dollars in Thousands)	
Assumption:		
Decline in fair value from increase in prepayment rate	$ 255	$ 490
Declines in fair value from increase in discount rate	201	394

9. Premises and Equipment

Premises and equipment are summarized as follows:

	December 31 2005	2004
	(In Thousands)	
Cost:		
Land	$ 5,071	$ 3,913
Buildings	25,764	20,401
Leasehold improvements	416	539
Furniture, fixtures and equipment	15,649	12,205
Construction in process	1,020	850
	47,920	37,908
Less allowances for depreciation and amortization	15,491	13,660
	$ 32,429	$ 24,248

Depreciation expense was $2.4 million, $1.8 million and $1.6 million for the years ended December 31, 2005, 2004 and 2003 respectively.

10. Deposits

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

	Years Ended December 31 2005	2004	2003
	(In Thousands)		
Checking and money market accounts	$ 3,264	$ 1,722	$ 1,466
Savings accounts	239	134	169
Certificates of deposit	17,119	11,100	11,810
	20,622	12,956	13,445
Less interest capitalized	(7)	(6)	(10)
Totals	$ 20,615	$ 12,950	$ 13,435

At December 31, 2005, accrued interest payable on deposit accounts amounted to $996,000, which was comprised of $876,000 and $120,000 for certificates of deposit and checking and money market accounts respectively.

First Defiance Financial Corp.

Notes to Consolidated Financial Statements (continued)

10. Deposits (continued)

A summary of deposit balances is as follows:

	December 31	
	2005	2004
	(In Thousands)	
Non-interest bearing checking accounts	$ 103,498	$ 62,450
Interest bearing checking and money market accounts	276,558	258,797
Savings deposits	82,766	52,132
Retail certificates of deposit less than $100,000	408,384	272,098
Retail certificates of deposit greater than $100,000	161,305	102,750
Brokered or national certificates of deposit	36,990	49,474
	$ 1,069,501	$ 797,701

Scheduled maturities of certificates of deposit at December 31, 2005 are as follows (in thousands):

2006	$ 451,010
2007	137,332
2008	14,107
2009	1,716
2010	1,669
2011 and thereafter	845
Total	$ 606,679

At December 31, 2005 and 2004, deposits of $303.3 million and $214.6 million, respectively, were in excess of the $100,000 Federal Deposit Insurance Corporation insurance limit. At December 31, 2005 and 2004, $42.4 million and $57.0 million, respectively, in investment securities were pledged as collateral against public deposits for certificates in excess of $100,000 and an additional $38.7 million and $1.3 million of securities were pledged at December 31, 2005 and December 31, 2004, respectively as collateral against deposits from private entities in excess of $100,000. Also, First Federal has pledged $7.8 of cash on deposit at the FHLB as collateral against public deposits at December 31, 2005 and it also holds $13,700,000 in depository bonds at December 31, 2005 with governmental entities, which can be pledged as collateral against public deposits in excess of $100,000.

First Defiance Financial Corp.

Notes to Consolidated Financial Statements (continued)

11. 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 and certain multi-family or non-residential real estate loans as security for these advances. Advances secured by investment securities must have collateral of at least 105% of the borrowing. Advances secured by residential mortgages must have collateral of at least 125% of the borrowings. Advances secured by multi-family or non-residential real estate loans securities must have 300% collateral coverage. The total level of borrowing is also limited to 50% of total assets and at least 50% of the borrowings must be secured by either one-to-four family residential mortgages or investment securities. Total loans pledged to the FHLB at December 31, 2005 were $465.9 million. First Federal has a maximum potential to acquire advances of approximately $205.6 million from the FHLB at December 31, 2005.

As of December 31, 2005, the FHLB has made a series of advances totaling $111.0 million to First Defiance that have fixed maturity dates but are callable at the option of the FHLB on a specified date and quarterly thereafter. The terms of these advances are as follows (in thousands):

Balance	Fixed Interest Rate	Call Date	Maturity Date
$ 15,000	5.44%	01/26/06	10/23/13
10,000	5.84%	03/01/06	09/01/10
20,000	4.61%	01/20/06	10/21/13
10,000	4.71%	02/07/06	11/07/13
15,000	4.52%	01/10/06	01/10/11
10,000	4.76%	01/10/06	01/10/11
10,000	4.93%	02/02/06	02/02/11
20,000	4.07%	03/08/06	03/08/11
1,000	4.56%	03/11/06	12/11/08

The FHLB has made advances totaling $27.0 million to First Defiance that have fixed maturity dates but which are callable after the call date only when three-month LIBOR rates exceed the agreed upon strike rate in the advance contract. The terms of these advances are as follows (in thousands):

Balance	Fixed Interest Rate	Call Date	Maturity Date	LIBOR "Strike" Rate
$ 10,000	5.14%	03/08/06	03/08/11	7.5%
7,000	3.54%	01/15/06	10/15/12	8.0%
5,000	3.85%	02/02/06	11/06/12	8.0%
5,000	3.48%	02/25/06	02/25/13	7.5%

When called, First Defiance has the option of paying off these advances, or converting them to variable rate advances priced at the three month LIBOR rate.

First Defiance Financial Corp.

Notes to Consolidated Financial Statements (continued)

11. Advances from Federal Home Loan Bank (continued)

First Defiance has an additional $14.3 million outstanding on a series of fixed rate long-term advances. Of this amount, $1.1 million is a fixed rate advance under the FHLB Affordable Housing Program in 1995. The total FHLB long-term advances including all convertible advances bear a weighted average interest rate of 4.65 % at December 31, 2005.

Future minimum payments by fiscal year based on maturity date are as follows (in thousands):

2006	$ 8,301
2007	8,018
2008	18,358
2009	6,625
2010	16,431
Thereafter	136,359
Total minimum payments	194,092
Less amounts representing interest	41,794
Totals	$ 152,298

First Defiance also utilizes short-term advances from the FHLB to meet cash flow needs and for short-term investment purposes. There were $28.5 million in short-term advances outstanding at December 31, 2005 at an interest rate of 4.12% and $26.5 million at December 31, 2004 at an interest rate of 2.20%. First Defiance borrows short-term advances under a variety of programs at FHLB. At December 31, 2005, $28.5 million was outstanding under First Defiance's REPO Advance line of credit. The total available under the REPO Advance line is $100.0 million. In addition, First Defiance has $15.0 million available under a Cash Management Advance line of credit and there were no borrowings against that line at December 31, 2004 or 2005. Amounts are generally borrowed under the Cash Management and REPO lines on an overnight basis. Other advances may be borrowed under the FHLB's short-term fixed or LIBOR based programs. Information concerning short-term advances is summarized as follows:

	Years Ended December 31	
	2005	2004
	(In Thousands, Except Percentages)	
Average daily balance during the year	$ 14,313	$ 15,577
Maximum month-end balance during the year	45,000	28,500
Average interest rate during the year	3.79%	1.55%

First Defiance Financial Corp.

Notes to Consolidated Financial Statements (continued)

12. Junior Subordinated Debentures Owed to Unconsolidated Subsidiary Trust

In October 2005, the Company formed an affiliated trust, First Defiance Statutory Trust I (the Trust Affiliate), that issued $20 million of Guaranteed

Capital Trust Securities (Trust Preferred Securities). In connection with the transaction, the Company issued $20.6 million of Junior Subordinated Deferrable Interest Debentures (Subordinated Debentures) to the Trust Affiliate. The Trust Affiliate 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 the Trust Affiliate are the sole assets of the trust. Distributions on the Trust Preferred Securities issued by the Trust Affiliate are payable quarterly at a variable rate equal to the three-month LIBOR rate plus 1.38%, or 5.87% as of December 31, 2005.

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

First Defiance Financial Corp.

Notes to Consolidated Financial Statements (continued)

13. Notes Payable and Other Short-term Borrowings

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

	Dece
	2005
	(In Th
Securities sold under agreement to repurchase (rate of 2.68% and 1.57% at December 31, 2005 and 2004, respectively)	$ 25,748
Revolving line of credit facility to financial institution, unsecured, at fed funds rate	--
Total other short-term borrowings	$ 25,748

	Years Ended
	2005
	(In Thousands, E
Securities sold under agreement to repurchase	
Average daily balance during year	$ 17,718
Maximum month-end balance during the year	25,748
Average interest rate during the year	2.18%
Revolving line of credit facilities to financial institutions	
Average daily balance during year	$ 301
Maximum month-end balance during the year	43,799
Average interest rate during the year	2.25%

As of December 31, 2005, First Defiance had the following line of credit facilities available for short-term borrowing purposes:

A $15 million revolving line of credit facility with a financial institution. The facility is unsecured and has an interest rate of fed funds rate plus 0.45%. There were no amounts outstanding on the line at December 31, 2005 or 2004. The maximum borrowed at any point in time under the line was $4.0 million and $15.0 million in 2005 and 2004, respectively. The average balance outstanding for the year was $67,000 and $244,000 in 2005 and 2004, respectively.

A $20 million fed funds line of credit with a financial institution. The line is unsecured and has an interest rate of the institution's fed funds rate. There were no amounts outstanding on the line at December 31, 2005 and 2004. The maximum borrowed at any point in time under the line was $20.0 million in both 2005 and 2004, and the average balance outstanding was $554,000 and $228,000 in 2005 and 2004, respectively.

A $5.0 million revolving line of credit with a financial institution. There was no amount outstanding on the line at December 31, 2005. The line is secured by the stock of First Federal Bank and the interest rate is either the lender's prime rate or LIBOR plus 1.75%, whichever is selected by First Defiance. The maximum borrowed in 2005 under the line was $3.0 million and the average outstanding balance for 2005 was $1.3 million. The Company had a $10.0 revolving line of credit available under similar terms in 2004 and it was not used.

14. Postretirement Benefits

First Defiance sponsors a defined benefit postretirement plan that is intended to supplement Medicare coverage for certain retirees who meet minimum age requirements. First Federal employees who retired prior to April 1, 1997 who completed 20 years of service after age 40 receive full medical coverage at no cost. Such coverage continues for surviving spouses of those participants for one year, after which coverage may be continued provided the spouse pays 50% of the average cost. First Federal employees retiring after April 1, 1997 are provided medical benefits at a cost based on their combined age and years of service at retirement. Surviving spouses are also eligible for continued coverage after the retiree is deceased at a subsidy level that is 10% less than what the retiree is eligible for. First Federal employees retiring before July 1, 1997 receive dental and vision care in addition to medical coverage. First Federal employees who retire after July 1, 1997 are not eligible for dental or vision care, but those retirees and their spouses each receive up to $200 annually in a medical spending account. Funds in that account may be used for payment of uninsured medical expenses. First Federal employees who were born after December 31, 1950 are not eligible for the medical coverage described above at retirement. Rather, a medical spending account of up to $10,000 (based on the participant's age and years of service) will be established to reimburse medical expenses for those individuals. First Insurance employees who were born before December 31, 1950 can continue coverage until they reach age 65, or in lieu of continuing coverage, can elect the medical spending account option, subject to eligibility requirements. Employees hired or acquired after January 1, 2003 are eligible only for the medical spending account option.

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	
	2005	20
	(In Thousands)	
Change in benefit obligation:		
Benefit obligation at beginning of year	$ 1,630	$ 1,
Service cost	49	
Interest cost	97	
Participant contribution	34	
Plan amendments	38	
Actuarial gains	(141)	
Benefits paid	(126)	(
Benefit obligation at end of year	1,581	1,
Change in fair value of plan assets:		
Balance at beginning of measurement period	--	
Employer contribution	92	
Participant contribution	34	
Benefits paid	(126)	(
Balance at end of measurement period	--	
Funded status	(1,581)	(1,
Unrecognized prior service cost	77	
Unrecognized net loss	317	
Accrued postretirement benefit obligation included in other liabilities in consolidated statement of financial condition	$ (1,187)	$ (1,

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First Defiance Financial Corp.

Notes to Consolidated Financial Statements (continued)

14. Postretirement Benefits (continued)

Net periodic postretirement benefit cost includes the following components:

	Years Ended December 31		
	2005	2004	2003
	(In Thousands)		
Service cost-benefits attributable to service during the period	$ 49	$ 48	$ 36
Interest cost on accumulated postretirement benefit obligation	97	97	83
Net amortization and deferral	25	23	14
Net periodic postretirement benefit cost	$ 171	$ 168	$ 133

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

	2005	2004
Weighted average discount rates:		
Used to determine benefit obligations at December 31	5.75%	6.00%
Used to determine net periodic postretirement benefit cost for years ended December 31	6.00%	6.00%
Assumed health care cost trend rates at December 31:		
Health care cost trend rate assumed for next year	8.00%	8.50%
Rate to which the cost trend rate is assumed to decline (the ultimate trend rate)	4.00%	4.00%
Year that rate reaches ultimate trend rate	2014	2014

The following benefits are expected to be paid over the next five years and in aggregate for the next five years thereafter. The Company has elected to opt for the Federal subsidy approach in lieu of coverage under Medicare Part D. These amounts include an estimate of that tax-free Federal subsidy:

	Before Reflecting Medicate Part D Subsidy	Impact of Medicare Part D Subsidy	After Reflecting Medicare Part D Subsidy
		(In Thousands)	
2006	$ 100	$ (19)	$ 81
2007	104	(19)	85
2008	113	(21)	92
2009	115	(26)	89
20010	126	(28)	98
2011 through 2015	708	(192)	516

14. Postretirement Benefits (continued)

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 (in thousands):

	One-Percentage-Point Increase	One-Percentage-Po Decrease

Effect on total of service and interest cost	$ 19	$ (16)
Effect on postretirement benefit obligation	197	(166)

15. Regulatory Matters

First Federal is subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the consolidated financial statements. Under capital guidelines and the regulatory framework for prompt corrective action, First Federal must meet specific capital guidelines that involve quantitative measures of First Federal's assets, liabilities and certain off-balance-sheet items as calculated under regulatory accounting practices. First Federal's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

Quantitative measures established by regulation to ensure capital adequacy require First Federal to maintain minimum amounts and ratios of Tier I and total capital to risk-weighted assets and of Tier I capital to average assets. As of December 31, 2005 and 2004, First Federal meets all capital adequacy requirements to which it is subject and the most recent notification from the Office of Thrift Supervision (OTS) categorized First Federal as well capitalized under the regulatory framework. The following schedule presents First Federal's regulatory capital ratios:

	Actual		Required for Capital Adequacy Purposes	
	Amount	Ratio	Amount	Ratio
As of December 31, 2005				
Tangible Capital	$ 120,029	8.46%	$ 21,273	1.50%
Tier 1 (Core) Capital	120,029	8.46%	56,729	4.00%
Tier 1 Capital to risk-weighted assets	120,029	10.63%	45,161	4.00%
Risk-Based Capital	133,636	11.84%	90,323	8.00%
As of December 31, 2004				
Tangible Capital	$ 102,342	9.29%	$ 16,533	1.50%
Tier 1 (Core) Capital	102,342	9.29%	44,089	4.00%
Tier 1 Capital to risk-weighted assets	102,342	11.59%	35,326	4.00%
Risk-Based Capital	112,267	12.71%	70,653	8.00%

First Defiance is a unitary thrift holding company and is regulated by the OTS. The OTS does not have defined capital requirements for unitary thrift holding companies.

16. Income Taxes

The components of income tax expense for continuing operations (credit) are as follows:

	Years Ended December 31		
	2005	2004	2003
	(In Thousands)		
Current:			
Federal	$ 5,367	$ 4,677	$ 4,783
State and local	7	35	33
Deferred	479	90	874
	$ 5,853	$ 4,802	$ 5,690

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

	Years Ended December 31		
	2005	2004	2003
	(In Thousands)		
Tax expense at statutory rate (35%)	$ 6,238	$ 5,457	$ 6,220
Increases (decreases) in taxes from:			
ESOP adjustments	193	83	29
State income tax - net of federal tax benefit	--	23	21
Tax exempt interest income	(394)	(498)	(468)
Bank owned life insurance	(268)	(332)	(283)
Other	84	69	171
Totals	$ 5,853	$ 4,802	$ 5,690

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.

16. Income Taxes (continued)

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

	December 31	
	2005	2004
	(In Thousands)	

Deferred federal income tax assets:		
Allowance for loan losses	$ 4,565	$ 3,477
Impaired loans	706	--
Deferred compensation and management recognition plans	547	337
Postretirement benefit costs	415	365
Accrued Vacation	259	186
Deposit and FHLB advance mark to market	150	--
Net unrealized losses on available-for-sale securities	13	--
Other	532	43
Total deferred federal income tax assets	7,187	4,408
Deferred federal income tax liabilities:		
Net unrealized gains on available-for-sale securities	--	1,147
FHLB stock dividends	2,585	1,868
Fixed assets	1,277	967
Mortgage servicing rights	1,207	587
Core Deposit Intangible	1,265	--
Goodwill	1,084	685
Loan mark to market	564	--
Other	--	88
Total deferred federal income tax liabilities	7,982	5,342
Net deferred federal income tax liability	$ (795)	$ (934)

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. 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, 2005.

Retained earnings at December 31, 2005 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 bse 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, 2005 was approximately $3.85 million.

17. Employee Benefit Plans

Employees of First Defiance are eligible to participate in the First Defiance Financial Corp. 401(k) Employee Savings Plan (First Defiance 401(k)) if they meet certain age and service requirements. Under the First Defiance 401(k), First Defiance matches 50% of the participants' contributions, to a maximum of 3% 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 $333,000, $293,000 and $258,000 for the years ended December 31, 2005, 2004 and 2003 respectively. There were no discretionary contributions in any of those years.

First Defiance also has established an Employee Stock Ownership Plan (ESOP) covering all employees of First Defiance age 21 or older who have at least one year of credited service. Contributions to the ESOP are made by First Defiance and are determined by First Defiance's Board of Directors at their discretion. The contributions may be made in the form of cash or First Defiance common stock. The annual contributions may not be greater than the amount deductible for federal income tax purposes and cannot cause First Federal to violate regulatory capital requirements.

To fund the plan, the ESOP borrowed funds from First Defiance for the purpose of purchasing shares of First Defiance common stock. The ESOP acquired a total of 863,596 shares in 1993 and 1995. The loan outstanding at December 31, 2005 was $1,722,000. Principal and interest payments on the loan are due in equal quarterly installments through June of 2008. The loan is collateralized by the shares of First Defiance's common stock and is repaid by the ESOP with funds from the Company's contributions to the ESOP, dividends on unallocated shares and earnings on ESOP assets.

As principal and interest payments on the loan are paid, shares are released from collateral and committed for allocation to active employees, based on the proportion of debt service paid in the year. Shares held by the ESOP which have not been released for allocation are reported as stock acquired by the ESOP plan in the statement of financial condition. As shares are released, First Defiance records compensation expense equal to the average fair value of the shares over the period in which the shares were earned. Also, the shares released for allocation are included in the average shares outstanding for earnings per share computations. Dividends on allocated shares are recorded as a reduction of retained earnings and dividends on unallocated shares are recorded as additional ESOP expense. ESOP compensation expense was $976,000, $956,000, and $802,000, for 2005, 2004 and 2003, respectively. As of December 31, 2005, 743,385 ESOP shares have been released for allocation of which 731,187 were allocated to participants, compared to 694,594 released and 682,397 allocated at December 31, 2004. The 120,211 unreleased shares have a fair value of $3.3 million at December 31, 2005, while the fair value of 169,002 unreleased shares at December 31, 2004 was $5.9 million. A total of $532,000 and $487,000 of dividends in 2005 and 2004, respectively, were used for debt service.

18. Stock Option Plans

First Defiance has established incentive stock option plans for its directors and its employees and has reserved 1,727,485 shares of common stock for issuance under the plans. A total of 1,467,204 shares are reserved for employees and 260,281 shares are reserved for directors. As of December 31, 2005, 569,099 options (545,912 for employees and 23,187 for directors) have been granted and remain outstanding at option prices based on the market value of the underlying shares on the date the options were granted. There are 50,186 options granted under the 1993 plan that are currently exercisable, 232,863 options granted under the 1996 plan that vest at 20% per year beginning in 1997 of which 224,910 are fully vested and currently exercisable, 247,500 options granted under the 2001 plan which vest at 20% per year beginning in 2002, of which 129,150 are fully vested and currently exercisable and 38,550 options granted under the 2005 plan which vest at 20% per year beginning in 2006. All options expire ten years from date of grant. Vested options of retirees expire on the earlier of the scheduled expiration date or five years after the retirement date for the 1993, 2001 and 2005 plans and on the earlier of the scheduled expiration date or twelve months after the retirement date for the 1996 plan.

The following table summarizes stock option activity for 2005, 2004, and 2003:

	Options Outstanding	Weighted Average Option Prices
Balance at January 1, 2003	808,320	12.12
Granted	57,000	20.47
Exercised or cashed out	(136,537)	10.95
Expired or canceled	(1,050)	15.32
Balance at December 31, 2003	727,733	$ 12.99
Granted	48,750	27.03
Exercised	(135,390)	11.49
Expired or canceled	(1,500)	18.40
Balance at December 31, 2004	639,593	$ 14.36
Granted	61,253	25.98
Exercised	(127,197)	12.27
Expired or canceled	(4,550)	24.25
Balance at December 31, 2005	569,099	$ 16.00

As of December 31, 2005 and 2004, 314,050 and 19,753 shares, respectively, were available for grant under the Company's stock option plans.

First Defiance Financial Corp.

Notes to Consolidated Financial Statements (continued)

18. Stock Option Plans (continued)

Information about stock options outstanding is as follows:

Range of Exercise Prices	Outstanding	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (in years)	Exercisable	We A Exer
$8.25 - $12.99	173,252	$ 10.64	0.86	173,252	$
$13.00 - $17.99	230,044	14.11	4.15	196,644	
$18.00 - $22.99	52,450	19.42	7.18	22,000	
$23.00 - $27.70	113,353	26.45	8.80	12,350	
Total at 12/31/05	569,099	$ 16.00	4.35	404,246	$

Total at 12/31/04	639,593	$ 14.36	4.37	475,954	$
Total at 12/31/03	727,733	$ 12.99	4.65	555,427	$

19. Parent Company and Regulatory Restrictions

Dividends paid by First Federal to First Defiance are subject to various regulatory restrictions. In accordance with these restrictions, First Federal can initiate dividend payments in 2006 only equal to or less than 2006 net profits. However, First Federal can request OTS approval to pay a dividend in excess of 2006 net profits.

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

Statements of Financial Condition	December 31 2005	2004
	(In Thousands)	
Assets		
Cash and cash equivalents	$ 9,406	$ 466
Investment securities, available for sale, carried at fair value	1,494	1,073
Investment in subsidiaries	160,035	124,179
Loan receivable from First Defiance Employee Stock Ownership Plan	1,760	2,312
Other assets	668	83
Total assets	$ 173,363	$ 128,113
Liabilities and stockholders' equity:		
Subordinated debentures	$ 20,619	$ --
Accrued liabilities	1,528	1,239
Stockholders' equity	151,216	126,874
Total liabilities and stockholders' equity	$ 173,363	$ 128,113

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First Defiance Financial Corp.

Notes to Consolidated Financial Statements (continued)

19. Parent Company and Regulatory Restrictions (continued)

Statements of Income	Years Ended Decembe 2005	2004
		(In Thousands)

Interest on loan to ESOP	$ 169	$ 214
Interest expense	(275)	(3)
Other income	102	45
Noninterest expense	(637)	(470)
Loss before income taxes and equity in earnings of subsidiaries	(641)	(214)
Income tax (credit)	(212)	(56)
Loss before equity in earnings of subsidiaries	(429)	(158)
Equity in earnings of subsidiaries	12,399	10,954
Net income	$ 11,970	$ 10,796

	Years Ended Decembe	
Statements of Cash Flows	2005	2004
	(In Thousands)	
Operating activities:		
Net income	$ 11,970	$ 10,796
Adjustments to reconcile net income to net cash (used in) provided by operating activities:		
Equity in earnings of subsidiaries	(12,399)	(10,954)
Dividends received from subsidiary	34,415	5,500
Change in other assets and liabilities	232	699
Net cash (used in) provided by operating activities	34,218	6,041
Investing activities:		
Investment in unconsolidated trust subsidiary	(619)	--
Cash paid for ComBanc, Inc.,	(18,693)	--
Cash paid for Genoa Savings and Loan Company	(10,869)	--
Principal payments received on ESOP loan	552	505
Purchase of available-for-sale securities	(500)	--
Sale of available-for-sale securities	70	
Net cash (used in) provided by investing activities	(30,059)	505
Financing activities:		
Proceeds from issuance of subordinated debt securities	20,619	--
Capital contribution to subsidiary	(10,000)	--
Stock options exercised	1,561	1,556
Purchase of common stock for treasury	(1,547)	(4,691)
Cash dividends paid	(5,852)	(5,011)
Net cash used in financing activities	4,781	(8,146)
Net increase (decrease) in cash and cash equivalents	8,940	(1,600)
Cash and cash equivalents at beginning of year	466	2,066
Cash and cash equivalents at end of year	$ 9,406	$ 466

Notes to Consolidated Financial Statements (continued)

20. Fair Value Statement of Consolidated Financial Condition

The following is a comparative condensed consolidated statement of financial condition based on carrying and estimated fair values of financial instruments as of December 31, 2005 and 2004. FASB Statement No. 107, Disclosures about Fair Value of Financial Instruments excludes certain financial instruments and all nonfinancial instruments from its disclosure requirements. Accordingly, the aggregate fair value amounts presented do not represent the underlying value of First Defiance Financial Corp.

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, warehouse and 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.

For investment securities, fair value has been based or current market quotations. If market prices are not available, fair value has been estimated based upon the quoted price of similar instruments.

The fair value of loans which 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. The allowance for loan losses is considered to be a reasonable adjustment for credit risk.

SFAS No. 107 requires that the fair value of demand, savings, NOW and certain money market accounts be equal to their carrying amount. The Company believes that the fair value of these deposits may be greater or less than that prescribed by SFAS No. 107.

The carrying amount of Subordinated Debentures is considered to be equal to fair value as a result of their interest rate structure. For deposits with fixed maturities, fair value is estimated based on interest rates currently being offered on deposits with similar characteristics and maturities.

20. Fair Value Statement of Consolidated Financial Condition (continued)

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. The cost or value of any call or put options are based on the estimated cost to settle the option at December 31, 2005.

	December 31, 2005	
	Carrying Value	Estimated Fair Values
	(In Tho	
Assets:		
Cash and cash equivalents	$ 49,256	$ 49,256
Investment securities	114,854	114,924
Loans, net, including loans held for sale	1,169,763	1,165,508
	1,333,873	$ 1,329,688
Other assets	127,209	
Total assets	$ 1,461,082	
Liabilities and stockholders' equity:		
Deposits	$ 1,069,501	$ 1,067,279
Advances from Federal Home Loan Bank	180,960	179,435
Subordinated debentures	20,619	20,619
Short term borrowings and other interest bearing liabilities	25,748	25,748
Advance payments by borrowers for taxes and insurance	605	605
	1,297,433	$ 1,293,686
Other liabilities	12,433	
Total liabilities	1,309,866	
Stockholders' equity	151,216	
Total liabilities and stockholders' equity	$ 1,461,082	

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First Defiance Financial Corp.

Notes to Consolidated Financial Statements (continued)

21. 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
	(In Thousands, Except Per Share		

2005			
Interest income	$ 16,436	$ 18,669	$ 19,932
Interest expense	5,826	6,816	7,715
Net interest income	10,610	11,853	12,217
Provision for loan losses	347	349	368
Net interest income after provision for loan losses	10,263	11,504	11,849
Gain on sale of securities	621	515	86
Noninterest income	3,640	3,365	3,930
Noninterest expense	10,244	12,518	10,496
Income before income taxes	4,280	2,866	5,369
Income taxes	1,409	838	1,742
Net income	$ 2,871	$ 2,028	$ 3,627
Earnings per share:			
Basic	$ 0.43	$ 0.30	$ 0.53
Diluted	$ 0.41	$ 0.28	$ 0.51
Average shares outstanding:			
Basic	6,668	6,869	6,908
Diluted	6,945	7,119	7,159

* - The significant increase in noninterest expense and resulting decline in net income for the quarters ended March 31 and June 30, 2005 was primarily due to $884,000 and $2.5 million in those quarters respectively of acquisition related charges associated with the previously disclosed 2005 acquisitions.

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First Defiance Financial Corp.

Notes to Consolidated Financial Statements (continued)

22. Quarterly Consolidated Results of Operations (Unaudited) (continued)

	Three Months Ended		
	March 31	June 30	September
	(In Thousands, Except Per Share		
2004			
Interest income	$ 13,002	$ 13,163	$ 13,97
Interest expense	4,806	4,881	5,25
Net interest income	8,196	8,282	8,72
Provision for loan losses	379	490	37
Net interest income after provision for loan losses	7,817	7,792	8,34
Gain on sale of securities	98	293	30
Noninterest income	2,738	3,976	2,64

Noninterest expense	7,055	7,425	9,00
Income before income taxes	3,598	4,636	2,28
Income taxes	1,105	1,492	60
Net income	$ 2,493	$ 3,144	$ 1,68
Earnings per share:			
Basic	$ 0.41	$ 0.51	$ 0.2
Diluted	$ 0.39	$ 0.49	$ 0.2
Average shares outstanding:			
Basic	6,113	6,125	6,08
Diluted	6,427	6,385	6,34

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 the design and operation 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, 2005, pursuant to Exchange Act Rule 13a-15. 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, 2005, are effective in timely alerting them to material information relating to First Defiance Financial Corp. (including its consolidated subsidiaries) required to be included in First Defiance's periodic filings under the Exchange Act.

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. First Defiance's internal control over financial reporting is a process designed under the supervision of First Defiance's chief executive officer and chief financial officer to provide reasonable assurance regarding the reliability of financial reporting and the preparation of First Defiance's financial statements for external reporting purposes in accordance with U.S. generally accepted accounting principles.

First Defiance's management assessed the effectiveness of its internal control over financial reporting as of December 31, 2005 based on the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission in "Internal Control-Integrated Framework." Based on the assessment, management determined that, as of December 31, 2005, First Defiance's internal control over financial reporting is effective based on those criteria. Management's assessment of the effectiveness of First Defiance's internal control over financial reporting as of December 31, 2005 has been audited by Crowe Chizek and Company LLC, an independent registered public accounting firm, as stated in their report appearing on page 103.

/s/ William J. Small	/s/ John C. Wahl
William J. Small Chairman, President and Chief Executive Officer	John C. Wahl Executive Vice President and Chief Financial Officer

Changes in Internal Control over Financial Reporting

There were no changes in First Defiance's internal control over financial reporting during the quarter ended December 31, 2005 that have materially affected, or are reasonably likely to materially affect First Defiance's internal control over financial reporting.

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

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

We have audited management's assertion, included in the accompanying Management's Report on Internal Control over Financial Reporting, that First Defiance Financial Corp. (the Company) maintained effective internal control over financial reporting as of December 31, 2005, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management's assessment and an opinion on the effectiveness of the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

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

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

In our opinion, management's assessment that First Defiance Financial Corp. maintained effective internal control over financial reporting as of December 31, 2005, is fairly stated, in all material respects, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring

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Organizations of the Treadway Commission (COSO). Also in our opinion, First Defiance Financial Corp. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2005 based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO)

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated statement of financial condition of First Defiance Financial Corp. as of December 31, 2005, and the related consolidated statements of income, stockholders' equity and cash flows for the year then ended and our report dated March 10, 2006 expressed an unqualified opinion on those consolidated financial statements.

/s/ Crowe Chizek and Company LLC

Crowe Chizek and Company LLC

Cleveland, Ohio
March 10, 2006

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Item 9b. Other Information

None.

PART III

Item 10. Directors and Executive Officers of the Registrant

The information required herein is incorporated by reference from the section captioned "Information Regarding Directors and Executive Officers" of the definitive proxy statement dated March 17, 2006.

Item 11. Executive Compensation

The information required herein is incorporated by reference from the sections captioned "Board Fees", "Executive Compensation", "Compensation Committee Report on Executive Compensation", "Stock Options", "Employment Agreements", and "Performance Graph" of the definitive proxy statement dated March 17, 2006.

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

The information required herein is incorporated by reference from the section captioned "Beneficial Ownership" of the definitive proxy statement dated March 17, 2006.

First Defiance maintains the 1993 Stock Incentive Plan, the 1993 Directors' Stock Option plan, the 1996 Stock Option Plan, the 2001 Stock Option and Incentive Plan and the 2005 Stock Option and Inventive Plan (collectively, the "Plans") and the 1996 Management Recognition Plan and Trust ("MRP") under which it may issue equity securities to its directors, officers and employees in exchange for goods and services. All of the Plans and the MRP were approved by the shareholders of First Defiance.

The following table shows, as of December 31, 2005, the number of common shares issuable upon the exercise of outstanding stock options, the weighted average exercise price of those stock options, and the number of common shares remaining for future issuance under the Plans and the MRP, excluding shares issuable upon exercise of outstanding stock options.

Equity Compensation Plan Information

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 remaining av future issu equity compen (excluding reflected in
	(a)	(b)	(c
1993 Stock Incentive Plan	50,186	$ 12.14	
1996 Stock Option Plan	232,863	$ 12.42	
2001 Stock Option and Incentive Plan	247,500	$ 18.62	1,
2005 Stock Option and Incentive Plan	38,550	$ 25.89	312,
1996 Management Recognition Plan and Trust	N/A	N/A	

Item 13. Certain Relationships and Related Transactions

The information required herein is incorporated by reference from the section captioned "Indebtedness of Management" of the definitive proxy statement dated March 17, 2006.

Item 14. Principal Accountant Fees and Services

The information required by this item is incorporated herein by reference under the section captioned "Independent Registered Public Accounting Firm" of the definitive proxy statement dated March 17, 2006.

PART IV

Item 15. Exhibits and Financial Statement Schedules

(a) (1) Financial Statements

The following consolidated financial statements are filed as a part of this document under "Item 8. Financial Statements and Supplementary Data."

Reports of Independent Registered Public Accounting Firms

Consolidated Statements of Financial Condition as of December 31, 2005 and 2004

Consolidated Statements of Income for the years ended December 31, 2005, 2004, and 2003

Consolidated Statements of Stockholders' Equity for the years ended December 31, 2005, 2004, and 2003

Consolidated Statements of Cash Flows for the years ended December 31, 2005, 2004, and 2003

Notes to Consolidated Financial Statements

(a) (2) Financial Statement Schedules

All schedules for which provision is made in the applicable accounting regulations of the Securities and Exchange Commission are not required under the related instructions or are included in the Notes to Consolidated Financial Statements incorporated herein by reference and therefore have been omitted.

(a) (3) Exhibits

The following exhibits are either filed as a part of this report or are incorporated herein by reference to documents previously filed as indicated below:

Exhibit Number	Description	
3.1	Articles of Incorporation	(1)
3.2	Code of Regulations	(1)
3.2	Bylaws	(1)
10.1	1996 Stock Option Plan	(2)
10.2	Form of Incentive Stock Option Award Agreement	(3)
10.3	Form of Nonqualified Stock Option Award Agreement	(3)
10.4	1996 Management Recognition Plan and Trust	(2)
10.5	2001 Stock Option and Incentive Plan	(5)
10.6	1993 Stock Incentive Plan	(1)
10.7	Employment Agreement with William J. Small	(6)

10.8	Employment Agreement with James L. Rohrs	(2)
10.9	Employment Agreement with John C. Wahl	(2)
10.10	Employment Agreement with Gregory R. Allen	(7)
10.11	Description of Annual Bonus	(4)
10.12	2005 Stock Option and Incentive Plan	(8)
13	Annual Report to Shareholders and Notice of Annual Meeting of Shareholders and Proxy Statement	(4)
14	Code of Ethics	(4)
21	List of Subsidiaries of the Company	(4)
23.1	Consent of Crowe Chizek and Company LLC	(4)
23.2	Consent of Ernst & Young LLP	(4)
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	(4)
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	(4)
32.1	Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	(4)

(1) Incorporated herein by reference to the like numbered exhibit in the Registrant's Form S-1 (File No. 33-93354).

(2) Incorporated herein by reference to like numbered exhibit in Registrant's 2001 Form 10-K

(3) Incorporated herein by reference to like numbered exhibit in Registrant's 2004 Form 10-K

(4) Included herein

(5) Incorporated herein by reference to Appendix B to the 2001 Proxy Statement

(6) Incorporated herein by reference to like numbered exhibit in Registrant's 2000 Form 10-K

(7) Incorporated herein by reference to like numbered exhibit in Registrant's 2002 Form 10-K

(8) Incorporated herein by reference to Appendix A to the 2005 Proxy Statement

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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.

March 10, 2006 By: /s/ John C. Wahl

John C. Wahl, Exec.V.P, 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 March 10, 2006.

Signature	Title

/s/ William J. Small William J. Small	Chairman of the Board, President and Chief Executive Officer
/s/ John C. Wahl John C. Wahl	Executive Vice President and Chief Financial Officer
/s/ James L. Rohrs James L. Rohrs	Director, Executive Vice President
/s/ Stephen L. Boomer Stephen L. Boomer	Director, Vice Chairman
/s/ John L. Bookmyer John L. Bookmyer	Director
/s/ Dr. Douglas A. Burgei Dr. Douglas A. Burgei	Director
/s/ Peter A. Diehl Peter A. Diehl	Director
/s/ Dr. John U. Fauster, III Dr. John U. Fauster, III	Director
/s/ Dwain I. Metzger Dwain I. Metzger	Director
/s/ Gerald W. Monnin Gerald W. Monnin	Director
/s/ Samuel S. Strausbaugh Samuel S. Strausbaugh	Director
/s/ Thomas A. Voigt Thomas A. Voigt	Director

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