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# Bank Mutual

C O R P O R A T I O N

**NOTICE OF 2013 ANNUAL MEETING OF SHAREHOLDERS**

**PROXY STATEMENT**

**2012 FORM 10-K ANNUAL REPORT**



**BANK MUTUAL CORPORATION**  
**4949 West Brown Deer Road**  
**Milwaukee, Wisconsin 53223**  
**(414) 354-1500**

March 8, 2013

Dear Fellow Shareholder,

We invite you to attend the Bank Mutual Corporation 2013 Annual Meeting of Shareholders, which will be held at the Four Points Sheraton Milwaukee North Hotel, 8900 N. Kildeer Court, Milwaukee, Wisconsin at 10:00 a.m., Central Time, on Monday, May 6, 2013.

Bank Mutual Corporation's Notice of Annual Meeting of Shareholders and Proxy Statement, which are enclosed, describe the business to be conducted at the Annual Meeting. If you plan to attend the Annual Meeting, please check the box on the proxy form so that we can plan for the appropriate number of people.

Also enclosed is a copy of Bank Mutual Corporation's Summary Annual Report and attached to this Proxy Statement is the Annual Report on Form 10-K for the year ended December 31, 2012.

**YOUR VOTE IS VERY IMPORTANT.** Whether or not you plan to attend the Annual Meeting, we urge you to **mark, sign, date and return your proxy form in the enclosed postage-paid envelope as soon as possible** to make sure that you are represented. Signing the proxy will not prevent you from voting in person at the Annual Meeting, but will ensure that your shares will be represented if you are unable to attend.

Sincerely,

**BANK MUTUAL CORPORATION**

*Michael T. Crowley, Jr.*

**MICHAEL T. CROWLEY, JR.**  
Chairman and Chief Executive Officer

## BANK MUTUAL CORPORATION

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### NOTICE OF ANNUAL MEETING OF SHAREHOLDERS TO BE HELD ON MAY 6, 2013

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To the Shareholders of Bank Mutual Corporation:

The 2013 annual meeting of shareholders of Bank Mutual Corporation will be held on Monday, May 6, 2013, at 10:00 a.m., Central Time, at the Four Points Sheraton Milwaukee North Hotel, 8900 N. Kildeer Court, Milwaukee, Wisconsin for the following purposes:

- (1) Electing three directors to serve for terms expiring in 2016;
- (2) Ratifying the selection of Deloitte & Touche LLP as our independent registered public accounting firm for 2013;
- (3) Holding an advisory vote to approve the compensation of the Company's named executive officers, as disclosed in "Compensation Discussion and Analysis" and "Executive Compensation" herein; and
- (4) Transacting such other business as may properly come before the annual meeting or any adjournment thereof.

**The board of directors recommends that shareholders vote FOR each of the board's director nominees, FOR the ratification of the selection of Deloitte & Touche LLP as our independent registered public accounting firm and FOR advisory approval of the compensation of the Company's named executive officers.**

The board of directors has fixed the close of business on March 1, 2013 as the record date for the determination of shareholders entitled to notice of and to vote at the annual meeting and any adjournment thereof. Only shareholders of record at the close of business on that date will be entitled to vote at the annual meeting.

We call your attention to the proxy statement accompanying this notice for a more complete statement regarding the matters to be acted upon at the annual meeting. Please read it carefully.

If you have questions or comments, please direct them to Bank Mutual Corporation, 4949 West Brown Deer Road, Milwaukee, Wisconsin 53223, Attention: Corporate Secretary. Please also contact the corporate secretary if you would like directions to the annual meeting. If you prefer, you may also e-mail questions, comments or requests for directions to [james.carter@bankmutual.com](mailto:james.carter@bankmutual.com).

By Order of the Board of Directors



James P. Carter  
Vice President and Secretary

Milwaukee, Wisconsin  
March 8, 2013

**Important Notice Regarding the Availability of Proxy Materials for the Annual Meeting of Shareholders to be Held on May 6, 2013: The Company's Proxy Statement, Annual Report on Form 10-K for the year ended December 31, 2012, and Summary Annual Report are available at: <http://www.bankmutualcorp.com> under the link "Annual Meeting Materials."**

To view this material, your browser must support the PDF file format. If your browser does not support PDF viewing, download and installation instructions are available at the above link.

**YOUR VOTE IS IMPORTANT**

**Your vote is important regardless of the number of shares you own. Whether or not you expect to attend the annual meeting, please indicate your voting directions, sign, date and promptly return the accompanying proxy, which is solicited by the Bank Mutual Corporation board of directors, using the enclosed self-addressed envelope, which requires no postage if mailed in the United States. If for any reason you should desire to revoke your proxy, you may do so at any time before it is voted at the annual meeting.**

## PROXY STATEMENT

**BANK MUTUAL CORPORATION**  
**4949 West Brown Deer Road**  
**Milwaukee, Wisconsin 53223**  
**(414) 354-1500**

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### SOLICITATION AND VOTING

This proxy statement and accompanying proxy are furnished to the shareholders of Bank Mutual Corporation ("Bank Mutual Corporation" or the "Company") in connection with the solicitation of proxies by Bank Mutual Corporation's board of directors for use at the annual meeting of Bank Mutual Corporation shareholders on Monday, May 6, 2013, and at any adjournment of that meeting. The 2012 summary annual report to shareholders, which accompanies this proxy statement, and the 2012 annual report on Form 10-K, attached hereto, contain financial statements and other information concerning the Company. The Company is mailing the proxy materials to shareholders beginning on or about March 11, 2013.

*Record Date and Meeting Information.* The board of directors has fixed the close of business on March 1, 2013 as the record date for the determination of shareholders entitled to notice of and to vote at the annual meeting and any adjournment thereof. Only holders of record of Company common stock, the only class of voting stock of Bank Mutual Corporation outstanding, on the record date are entitled to notice of and to vote at the annual meeting. Each share of common stock is entitled to one vote. At the record date, there were 46,420,084 shares of common stock validly issued and outstanding.

The board of directors of Bank Mutual Corporation knows of no matters to be acted upon at the annual meeting other than as set forth in the notice attached to this proxy statement. If any other matters properly come before the annual meeting, or any adjournment thereof, it is the intention of the persons named in the proxy to vote such proxies in accordance with their best judgment on such matters.

*Voting Your Shares.* Any shareholder entitled to vote at the annual meeting may vote either in person or by a properly executed proxy. Shares represented by properly executed proxies received by Bank Mutual Corporation will be voted at the annual meeting, or any adjournment thereof, in accordance with the terms of such proxies, unless revoked. If you own your shares directly and no voting instructions are given on a properly executed proxy, the shares will be voted by the persons named to vote the proxy FOR the election of the designated director nominees, FOR ratification of the selection of Deloitte & Touche LLP as the independent registered public accounting firm and FOR advisory approval of the compensation of the Company's named executive officers.

Brokers no longer have discretion to cast votes in the election of directors with respect to any shares held in street name for which they have not received voting directions from the beneficial owners. Therefore, if you hold your shares in street name, you must vote your proxy if you wish your shares to be voted in the election of directors, or on the advisory vote regarding executive compensation.

A shareholder may revoke a proxy at any time prior to the time it is voted by filing a written notice of revocation with the corporate secretary of the Company, by delivering a properly executed proxy bearing a later date or by voting in person at the annual meeting. Attendance at the annual meeting will not in itself constitute revocation of a proxy.

*Shares in Dividend Reinvestment or Employee Plans.* If a shareholder participates in the Company's Dividend Reinvestment and Stock Purchase Plan (the "DRP"), the proxy also will serve as voting instructions for the participant's shares held in the DRP. Participants' shares will be voted by the administrator of the DRP in accordance with those voting instructions. If a participant does not return a proxy, the DRP administrator will not vote that participant's shares held in the DRP.

Any shareholder who owns shares through an investment in the Company Common Stock Fund of the Bank Mutual Corporation 401(k) Plan (the "401(k) Plan") will receive a separate blue proxy card, marked "401k," to instruct the 401(k) Plan's administrator how to vote those shares. The administrator will vote shares in those participants' 401(k) Plan accounts in accordance with the voting instructions on the proxies. If a 401(k) Plan participant does not return a proxy, the administrator will vote that participant's shares in the 401(k) Plan in the same proportion as the voting of all shares in the 401(k) Plan for which voting instructions have been received.

Any shareholder who owns shares through an allocation to that person's account under the Bank Mutual Corporation Employee Stock Ownership Plan (the "ESOP") will receive a separate green proxy card, marked "ESOP," to instruct the ESOP's administrator how to vote those shares. The ESOP administrator, which is Bank Mutual Corporation acting through its board, will vote shares allocated to those participants' ESOP accounts in accordance with the participant's voting instructions on the proxies. The ESOP administrator may vote, at its discretion, any ESOP shares that are not voted by the individuals to whom they are allocated. It is expected that those shares will be voted in accordance with the board's recommendations.

*Quorum and Required Vote.* A majority of the votes entitled to be cast by the shares entitled to vote, represented in person or by proxy, will constitute a quorum of shareholders at the annual meeting. Shares for which authority is withheld to vote for director nominees, abstentions and broker non-votes (i.e., proxies from brokers or nominees indicating that such persons have not received instructions from the beneficial owners or other persons entitled to vote shares as to a matter with respect to which the brokers or nominees do not have discretionary power to vote) will be considered present for purposes of establishing a quorum. The inspectors of election appointed by the board of directors will count the votes and ballots at the annual meeting.

Assuming a quorum is present, a plurality of the votes cast at the annual meeting by the holders of shares of common stock entitled to vote is required for the election of directors. In other words, the individuals who receive the largest number of votes are elected as directors up to the maximum number of directors in a class to be chosen at the annual meeting. With respect to the election of directors, any shares not voted, whether by withheld authority, broker non-vote or otherwise, will have no effect on the election of directors except to the extent that the failure to vote for an individual results in another individual receiving a comparatively larger number of votes.

Assuming that a quorum is present, the selection of Deloitte & Touche LLP will be deemed to have been ratified if more shares are voted in favor of ratification than are voted against ratification. Accordingly, any shares not voted on this matter, whether by abstention or otherwise, will have no effect on this matter.

Assuming a quorum is present, the advisory vote approving the compensation of the Company's named executive officers will be approved if the votes at the annual meeting by the holders of shares of common stock entitled to vote voting for approval exceed those voting against. Therefore, abstentions and broker non-votes will not affect this vote, except insofar as they reduce the number of shares that are voted.

*Expenses and Solicitation.* Expenses in connection with the solicitation of proxies will be paid by the Company. Proxies will be solicited principally by mail, but may also be solicited by the directors, officers and other employees of the Company in person or by telephone, facsimile or other means of communication. Those directors, officers and employees will receive no compensation therefor in addition to their regular compensation, but may be reimbursed for their related out-of-pocket expenses. Brokers, dealers, banks, or their nominees, who hold common stock on behalf of another will be asked to send proxy materials and related documents to the beneficial owners of such stock, and the Company will reimburse those persons for their reasonable expenses.

## SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS

The table below sets forth information regarding the beneficial ownership of Company common stock as of the March 1, 2013 record date by each director and nominee for director, by each executive officer named in the Summary Compensation Table below and by all directors and executive officers of the Company as a group. The table also includes information as to the only known 5% or greater shareholders of the Company.

<u>Name of Beneficial Owner</u>	<u>Number of Shares and Nature of Beneficial Ownership (1)(2)</u>	<u>Percent of Class</u>
P. Terry Anderegg .....	270,974	*
David A. Baumgarten.....	163,050	*
David C. Boerke.....	33,200	*
Richard A. Brown .....	39,200	*
Thomas H. Buestrin.....	186,372	*
Michael T. Crowley, Jr. (3).....	2,558,536	5.4%
Michael W. Dosland.....	145,842	*
Mark C. Herr .....	137,796	*
Gregory A. Larson.....	83,450	*
Thomas J. Lopina, Sr.....	229,941	*
Christopher L. Mayne.....	54,000	*
William J. Mielke.....	366,062	*
Robert B. Olson.....	318,623	*
J. Gus Swoboda.....	216,338	*
 All directors and executive officers as a group (16 persons) (4)(5) .....	 5,045,817	 10.5%
 BlackRock, Inc. (6) .....	 3,882,145	 8.4%

\* Less than 1.0%. Percentages are based on shares outstanding on the record date.

- (1) Unless otherwise noted, the specified persons have sole voting and dispositive power as to the shares. Includes the following shares that are allocated to individuals' ESOP accounts, for which individuals have sole voting power but no dispositive power (except that participants who have attained age 55 and have 10 years of plan participation may diversify up to 25% of their ESOP shares) over such shares: Mr. Anderegg – 35,869; Mr. Crowley Jr. – 40,703 (Messrs. Anderegg and Crowley Jr. have dispositive power over 25% of their shares); Mr. Dosland – 573; and all directors and executive officers as a group – 94,606. Includes the following shares that are allocated to individuals' accounts under the Benefits Restoration Plan related to the 401(k) Plan for which individuals have sole dispositive power but no voting power over such shares: Mr. Anderegg – 3,392; Mr. Crowley Jr. – 65,400; and all directors and executive officers as a group – 68,792. Includes the following shares for which beneficial ownership is shared: Mr. Buestrin – 32,029; Mr. Crowley Jr. – 129,368; Mr. Dosland – 6,800; Mr. Herr – 39,213; Mr. Lopina – 90,557; Mr. Mielke – 60,259; Mr. Olson – 229,623; and all directors and executive officers as a group – 708,705. See also notes (4) and (5) below.
- (2) Includes the following shares subject to options exercisable at or within 60 days of the record date: Mr. Anderegg – 110,000; Mr. Baumgarten – 48,000; Messrs. Boerke and Brown – 21,800 each; Messrs. Buestrin, Herr, Lopina, Mielke, Olson and Swoboda – 89,000 each; Mr. Crowley Jr. – 710,000; Mr. Dosland – 50,000; Mr. Larson – 24,000; Mr. Mayne – 24,000; and all directors and executive officers as a group – 1,561,500. As of December 31, 2012, Mr. Lopina had pledged 86,034 shares.
- (3) The information for Mr. Crowley Jr. is based in part on an amendment to Schedule 13G dated January 30, 2013 filed by him along with other information available to the Company. Mr. Crowley Jr.'s business address is c/o Bank Mutual Corporation, 4949 West Brown Deer Road, Milwaukee, WI 53223.

- (4) The total for the group (but not any individual) includes 90,104 shares held under the Benefit Restoration Plan related to the ESOP in which certain executive officers share beneficial ownership of shares held for the accounts of others. No ESOP shares remain unallocated.
- (5) Because the 401(k) Plan permits participants to vote shares and make investment decisions, except for certain takeover offers, shares held in the 401(k) Plan are included only if held in the accounts of named persons, even though certain of the officers are trustees or administrators of one of the plans. With respect to shares allocated to individuals' accounts under the Benefits Restoration Plan as related to the 401(k) Plan, the individuals whose accounts hold such shares have sole dispositive power but no voting power over such shares; such shares are included in the individuals' ownership in the table.
- (6) BlackRock, Inc. ("BlackRock") filed an amendment to Schedule 13G dated February 4, 2013 reporting sole voting and sole dispositive power as to 3,882,145 shares of common stock. BlackRock filed the report as a parent holding company; the report identifies the following subsidiaries as subsidiaries which hold or acquired the securities reported: BlackRock Advisors, LLC, BlackRock Investment Management, LLC, BlackRock Asset Management Australia Limited, BlackRock Asset Management Canada Limited, BlackRock Asset Management Ireland Limited, BlackRock Fund Advisors, BlackRock Institutional Trust Company, N.A. and BlackRock Japan Co. Ltd. The address of BlackRock is 40 East 52<sup>nd</sup> Street, New York, NY 10022.

The above beneficial ownership information is based on data furnished by the specified persons and is determined in accordance with Rule 13d-3 under the Securities Exchange Act, as required for purposes of this proxy statement. It is not necessarily to be construed as an admission of beneficial ownership for other purposes.

#### **ELECTION OF DIRECTORS**

The bylaws provide that the number of directors of Bank Mutual Corporation shall be between seven and thirteen, as determined by the board of directors. At each annual meeting, the term of office of one class of directors expires and a class of directors is elected to serve for a term of three years or until their successors are elected and qualified. Under the bylaws, the board may appoint a new director to fill a vacancy that occurs between annual meetings, including a vacancy that would result from a later determination to increase the size of the board.

The board currently has ten directors. This year's board nominees for election for terms expiring at the 2016 annual meeting are Richard A. Brown, Mark C. Herr and J. Gus Swoboda.

It is the Company's policy that the board of directors should reflect a broad variety of experience and talents. When the Nominating and Governance Committee makes nominations for election to the board, it reviews the Company's director selection criteria and seeks to choose individuals who bring a variety of expertise to the board within these criteria. For further information about the criteria used to evaluate board membership, see "– Board Meetings and Committees–Nominating and Governance Committee" below.

Shares represented by proxies will be voted FOR the election of each of the nominees unless otherwise specified by the executing shareholder. If any nominee declines or is unable to act as a director, which the Company does not foresee, the board may name a replacement, in which case the shares represented by proxies will be voted FOR the substitute nominee.

Information regarding the nominees and the directors whose terms continue is set forth in the following table. For additional information regarding the specific attributes possessed by each of the current directors and nominees, which together with their specific business and personal experience listed in the following table, provide the bases for their nomination, see "–Director Attributes" below.

**The board of directors unanimously recommends that shareholders vote FOR the election of the director nominees listed in the following table.**

<u>Name and Age</u>	<u>Principal Occupation and Business Experience (1)</u>	<u>Director Since (2)</u>
<i>Nominees for terms expiring in 2016</i>		
Richard A. Brown, 64 (3)	Owner, Richard A. Brown, CPA, a firm providing CFO consulting services, since 2007; retired in 2006 as an audit partner, KPMG LLP, an international accounting firm; private equity investor and board member, Fortress Partners Capital Management, LTD	2007
Mark C. Herr, 60 (4)	Senior Partner, Plunkett Raysich Architects LLP	2001
J. Gus Swoboda, 77 (4) (5)	Retired; prior thereto, Senior Vice President, Human and Corporate Development, Wisconsin Public Service Corporation, electric and gas utility	1987
<i>Continuing Directors - Terms expire in 2014</i>		
David A. Baumgarten, 62 (6)	President of the Company and the Bank since 2010; previously Executive Vice President – Regional Banking of Associated Banc-Corp	2010
David C. Boerke, 67 (7) (8)	Principal and commercial real estate advisor, The Boerke Company, Inc., a member of the Cushman Wakefield Alliance, a commercial real estate company; president, Boerke Advocates, Inc., commercial real estate company; principal private equity investor, Antietam, LLC	2007
Thomas J. Lopina, Sr., 75 (8)	Associate, Spectrum Solutions, Inc., small business consulting firm	1979
Robert B. Olson, 75 (3) (8)	Retired as self-employed consultant in 2005; prior to 2000, an executive with Little Rapids Corporation, specialty paper producer	1997
<i>Continuing Directors - Terms expire in 2015</i>		
Thomas H. Buestrin, 76 (3) (4) (5) (7)	President of Buestrin, Allen & Associates Ltd., real estate investment, management and development	1995
Michael T. Crowley, Jr., 70 (5) (6)	Chairman and CEO of the Company and the Bank; President of both until 2010	1970
William J. Mielke, 65 (3) (4) (5) (8)	President and CEO of Ruekert & Mielke Inc., engineering consulting company	1988

- (1) Unless otherwise noted, all directors have been employed in their respective principal occupations listed for at least the past five years.
- (2) Indicates the date when director was first elected to the board of the Company, Bank Mutual (the "Bank") (the Bank is a subsidiary of the Company) or First Northern Savings Bank ("First Northern") (First Northern was acquired by the Company in 2000 and was merged into the Bank in 2003), as the case may be. Each person who became a Bank or First Northern director prior to 2000 became a director of the Company in 2000. Messrs. Brown and Boerke each became a director of the Company in 2008.
- (3) Member of the Audit Committee, of which Mr. Brown is Chairman.

- (4) Member of the Nominating and Governance Committee, of which Mr. Mielke is Chairman.
- (5) Member of the Executive Committee, of which Mr. Crowley Jr. is Chairman.
- (6) As previously announced, Mr. Crowley Jr. will retire as CEO of the Company and the Bank effective as of July 1, 2013, but will remain as non-executive Chairman of both. Mr. Baumgarten will become CEO of the Company and the Bank, effective upon Mr. Crowley Jr.'s retirement.
- (7) Messrs. Boerke and Buestrin are first cousins.
- (8) Member of the Compensation Committee, of which Mr. Mielke is Chairman.

#### **Director Attributes**

When making its decisions regarding who to nominate, or re-nominate, for the board, the Nominating and Governance Committee of the board of directors considers an individual's particular background and prior service with the Company, as summarized above, along with the general factors discussed in "Selection Criteria for Directors" and "Board Meetings and Committees--Nominating and Governance Committee" below.

As further discussed below, the board believes that, particularly in the context of a regulated industry, the Company generally benefits from retaining existing, long-term directors in office because of the knowledge of the industry and the Company that they can gain over the course of time. Thus, the Nominating and Governance Committee generally nominates incumbent directors for re-election to the board as long as those directors have performed, and are expected to continue to perform, in a satisfactory manner and the board maintains an acceptable overall balance of skills and experience. On the basis of their prior professional experience, their years of experience on the Company's board and their strong contributions as long-time directors, the Nominating and Governance Committee nominated Messrs. Brown, Herr and Swoboda for re-election at the 2013 annual meeting, and nominated Messrs. Baumgarten, Boerke, Buestrin, Crowley Jr., Lopina, Mielke and Olson for re-election at the prior two annual meetings, and that is also why the Nominating and Governance Committee has concluded, as of the date of the filing of this proxy statement, that each individual is qualified to serve on the board.

In addition, Mr. Crowley Jr. was re-nominated to the board in 2012 due to the practice of having the Company's chief executive officer serve on the board. Mr. Brown was initially nominated, and was nominated for re-election at the 2013 annual meeting, due to his extensive financial industry and accounting background, including over 36 years of public company auditing experience, focusing on the financial institutions industry, with KPMG LLP and his qualification as an "audit committee financial expert." Mr. Baumgarten was initially elected to the board in 2010, when he became President of the Company, and was re-nominated as a result of his important position and responsibilities within the Company and the Bank, as well as his significant prior experience and expertise for many years in the financial institutions industry.

#### **Selection Criteria for Directors**

The selection criteria for membership on Bank Mutual Corporation's board of directors, which were confirmed by the board in connection with the formation of the Nominating and Governance Committee and have been periodically reviewed thereafter, include: strength of character and judgment; honesty and integrity; a diversity of skill, education and experience with businesses and other organizations; interplay of the candidates' experience with the experience of other board members; and the extent to which the candidate would be a desirable addition to the board or its committees. Nominees must have a background that demonstrates an understanding of business and financial affairs, and should have a proven record of competence and accomplishments through leadership in industry, education, the professions or government. The Nominating and Governance Committee Charter identifies the following core areas that should be represented on the board: accounting and finance; business judgment; management; crisis response; industry knowledge; leadership; and strategic vision. A first-time nominee should be highly respected and active in his or her profession. A nominee must be a Company shareholder, and the willingness to hold a significant position in Company stock will be considered. A nominee must be capable and able to work well with other directors and management and be able to spend the time needed to function effectively as a director. To help assure that the director has the necessary time to effectively function as a director, the Nominating and Governance Committee Charter prohibits a director from serving on more than three boards of publicly-held companies in addition to the Company. The nominee must have a genuine interest in representing the interests of the Company and the shareholders overall, not any particular interest group. The nominee should not have conflicts of interest that would interfere with that person's duty of loyalty.

When considering directors for re-nomination, in addition to the above criteria, the Nominating and Governance Committee also heavily weights the existing director's record of service on the board by assessing and reviewing such director's contributions to the board and the Company. Assuming satisfactory performance, an existing director will generally be re-nominated absent specific need by the Company to change the mix of directors. Significant job or employment changes are also considered in determining whether to re-nominate an existing director. Further, the Nominating and Governance Committee Charter provides that if a director experiences a change in employment (other than a promotion or retirement), he or she must submit a resignation letter to the board; the board will decide to accept the resignation or not based on its determination of whether the change will adversely affect the board or the Company. The Company has not paid any third party fee to assist in the process of identifying or evaluating director nominees.

While the board does not have a separate formal diversity policy, it is the Company's and the board's policy to identify qualified potential candidates without regard to any candidate's race, color, disability, gender, national origin, religion or creed, and the Company seeks to ensure the fair representation of shareholder interests on the board through the criteria set forth above. The board believes that the use of the Nominating and Governance Committee's general criteria, along with non-discriminatory policies, will best result in a board that shows diversity in many respects. The board believes that it currently maintains that diversity.

### **Board Meetings and Committees**

The Bank Mutual Corporation board of directors met five times during 2012. Messrs. Boerke, Brown, Buestrin, Herr, Lopina, Mielke, Olson and Swoboda are considered "independent" under The Nasdaq Stock Market rules; all members of the Audit, Compensation and Nominating and Governance Committees are "independent." As part of the board meetings, independent directors regularly met without management or non-independent directors present. Mr. Mielke informally chairs those executive sessions. Each director attended at least 75% of the total of the number of meetings of the board and the number of meetings of all committees of the board on which such director served during the year.

When making its determinations regarding director independence, the board of directors considers The Nasdaq Stock Market rules and also reviews other transactions and relationships involving the Company, which are described, or of the types described, in "Certain Transactions and Relationships with the Company." The board has not considered ordinary course of business banking transactions with the Bank such as a banking relationship with a trust for Mr. Buestrin's daughter to be an impediment to independence, so long as the transactions meet the standards described in "Certain Transactions and Relationships with the Company," since such transactions are in the ordinary course of the Bank's regular business.

*Board Leadership Structure.* Mr. Crowley Jr. currently serves as Chairman and Chief Executive Officer of the Company and the Bank; however, as previously announced, he will retire as Chief Executive Officer effective as of July 1, 2013, but will remain as non-executive Chairman. Historically, the Company has combined the positions of Chairman and Chief Executive Officer because it believed that, based on the highly-regulated nature of the financial institutions industry and the increased frequency of interactions with the regulators in recent periods, it was important that the Chairman be very familiar with the industry and the Company's operations. In addition, the Company has historically believed that, among other things, having an executive officer such as Mr. Crowley Jr. serve in both roles allowed him to use his substantial experience and information gained from those roles to effectively lead the Company, to keep the non-management board members apprised of recent developments regarding the day-to-day operations of the Company and the industry and to act as a unified spokesperson on behalf of the Company.

From time to time, the Company re-evaluates whether to combine or separate the Chairman and Chief Executive Officer positions. One such occasion for doing so was the recent announcement that Mr. Crowley Jr. intends to retire as Chief Executive Officer in 2013. Given Mr. Crowley Jr.'s long history of leadership within the Company and experience in the financial institutions industry, the Company believes that it is appropriate for Mr. Crowley Jr. to continue to serve as Chairman and, therefore, decided that it will separate the Chairman and Chief Executive Officer positions following Mr. Crowley Jr.'s retirement. Although Mr. Crowley Jr. will not be an "independent" Chairman under Nasdaq and federal securities rules (by virtue of his prior employment with the Company), the board currently believes that having a non-independent Chairman is appropriately counter-balanced

by the fact that all but one of the other directors are independent and that the independent directors meet in executive session at each board meeting. While the board has not formally appointed an independent lead director, Mr. Mielke has traditionally served as the independent directors' designee for relaying information from the independent directors of the board to management and effectively has undertaken many of the same responsibilities that an independent lead director would have.

*Audit Committee.* The Audit Committee is responsible for, among other things, assisting the board in: fulfilling its fiduciary responsibilities as to the Company's accounting policies, reporting practices and controls and the sufficiency of auditing relating thereto; assuring the independence and qualifications of the outside auditors, the integrity of management and the adequacy of disclosures to shareholders; evaluating the performance of the Company's independent registered public accounting firm; and reviewing related party transactions and potential conflict of interest situations.

The Audit Committee met four times in 2012. On behalf of the Audit Committee, Mr. Brown, its chair, also regularly consulted with the independent registered public accounting firm about the Company's periodic public financial disclosures, and participated in eight calls relating to SEC-filed documents and financial disclosures. See also "Report of the Audit Committee" and "Independent Registered Public Accounting Firm" for other information pertaining to the Audit Committee.

The current members of the Audit Committee are Messrs. Brown (Chairman), Buestrin, Mielke and Olson. The board believes that all of the members of the Audit Committee have sufficient experience, knowledge and other personal qualities to be "financially literate" and be active, effective and contributing members of the Audit Committee. In addition, the board has determined that Mr. Brown meets the SEC's definition of "audit committee financial expert." The board's determination was based on Mr. Brown's 36 years of employment and public company auditing experience with KPMG LLP, an international public accounting firm. The board has also determined that Messrs. Buestrin, Mielke and Olson are "financially sophisticated" within The Nasdaq Stock Market rules. Mr. Buestrin was for seven years a member of the board of directors of the Federal Home Loan Bank of Chicago, and served for several years on its audit committee and, at its request, on the boards of several savings institutions. Both Messrs. Buestrin and Mielke have served as executive officers of their companies, and in those positions have regularly had responsibility for their companies' financial affairs as well as financial matters for projects undertaken by their companies. Mr. Olson has served as an executive officer of a manufacturing company, and for many years was the chief operating officer of one of its divisions. As such, Mr. Olson had primary responsibility for financial performance and reporting of that division.

*Compensation Committee.* The current members of the Compensation Committee are Messrs. Mielke (Chairman), Boerke, Lopina and Olson. The Compensation Committee held four meetings during 2012. The Compensation Committee reviews, and either establishes or recommends to the board: compensation policies and plans; salaries, bonuses and benefits for all officers; salary and benefit levels for employees; determinations with respect to stock options and restricted stock awards; and other personnel policies and procedures. See also "Compensation Discussion and Analysis" for other information pertaining to the Compensation Committee, including information about the Compensation Committee's policies and procedures.

*Compensation Committee Interlocks and Insider Participation.* None of the members of the Compensation Committee served as an officer or employee of the Company, the Bank or a Bank subsidiary, nor did any of them have any other reportable interlock. For a description of the Company's policies with respect to loans to and other banking transactions with officers, directors and employees, see "Certain Transactions and Relationships with the Company."

*Nominating and Governance Committee.* The current members of the Nominating and Governance Committee are Messrs. Mielke (Chairman), Buestrin, Herr and Swoboda. The Nominating and Governance Committee held one meeting in 2012. The Nominating and Governance Committee considers nominees for director positions and also evaluates and oversees other corporate governance and related issues. The Nominating and Governance Committee will identify nominees based upon suggestions by outside directors, management members and/or shareholders and evaluate them in accordance with its established criteria. See "Director Attributes" and "Selection Criteria for Directors" above.

The Nominating and Governance Committee will consider proposed nominees whose names are submitted to it by shareholders, and it would evaluate proposed nominees from shareholders the same regardless of who has made the proposal. If a shareholder wishes to suggest a name for the Nominating and Governance Committee to consider for a director position, the name of that nominee and related personal information should be forwarded to the Nominating and Governance Committee, in care of the corporate secretary, at least five months before the next annual meeting to assure time for meaningful consideration by the Nominating and Governance Committee or should be submitted to the corporate secretary in accordance with the procedures set forth in the Company's bylaws. The Nominating and Governance Committee believes that such this process for considering shareholder nominations is adequate given the lack of suggestions received from shareholders in the past. The Nominating and Governance Committee reviews periodically whether additional policies should be adopted. See also "Shareholder Proposals and Notices" for bylaw requirements for nominations. The Company has not received any proposed nominees who have been suggested by eligible 5%-or-greater security holders contemplated by relevant SEC disclosure requirements, or rejected any such nominees.

*Executive Committee.* The current members of the Executive Committee are Messrs. Crowley Jr. (Chairman), Buestrin, Mielke and Swoboda. The Executive Committee did not meet in 2012. The Executive Committee may act on most matters on behalf of the entire board when action is necessary or appropriate on short notice between board meetings.

*Committee Charters.* The board of directors has adopted charters for the Audit, Compensation and Nominating and Governance Committees. The Company will continue to respond to and comply with SEC and The Nasdaq Stock Market proposals relating to board committees as they are finalized, adopted and become effective. The Company posts copies of the charters for its Audit, Compensation and Nominating and Governance Committees (including director selection criteria) and other corporate governance documents on its website, at [www.bankmutualcorp.com](http://www.bankmutualcorp.com), under the link "Corporate Governance." If any of those documents are changed, or related documents adopted, those changes and new documents will be posted on the Company's corporate website at the internet address above.

### **Other Board and Corporate Governance Matters**

*Communications between Shareholders and the Board.* Any shareholder communication that is sent to the board in care of the chief executive officer, the corporate secretary or another corporate officer is forwarded to the board, unless the communication relates specifically to a customer inquiry or complaint for which shareholder status is not relevant. The chief executive officer and the corporate secretary have been given the authority to conduct that screening process and make that determination. The procedure has been unanimously approved by the board, and was specifically approved by its independent members. Unless and until any other more specific procedures are developed and posted on the Company's website, any communications to the board of directors should be sent to it in care of the chief executive officer or the corporate secretary.

*Director Attendance at Annual Shareholders' Meeting.* Bank Mutual Corporation expects all of its directors to attend the annual meeting of shareholders. A board meeting is also held immediately after the annual shareholders' meeting to facilitate directors' attendance at both. All directors attended the 2012 annual meeting of shareholders.

*Code of Ethics and Code of Conduct.* As a long-standing part of the Company's and the Bank's corporate governance practices, the Bank has had for many years a code of ethics and a code of conduct. Bank Mutual Corporation has built on these codes to reflect current circumstances and SEC and Nasdaq definitions for such codes, and currently has a vision statement, a code of ethics and a code of conduct for itself, the Bank and other subsidiaries. Among other things, the code of ethics and code of conduct include provisions regarding honest and ethical conduct, conflicts of interest, full and fair disclosure, compliance with law, and reporting of and sanctions for violations. The codes apply to all directors, officers and employees of Bank Mutual Corporation and subsidiaries. The Company has posted copies of its vision statement, code of ethics and code of conduct on its corporate website, at [www.bankmutualcorp.com](http://www.bankmutualcorp.com), under the link "Corporate Governance." If further matters are documented, or if those documents (including the code of ethics and the code of conduct) are changed, waivers from the code of ethics or the code of conduct are granted, or new procedures are adopted, those new documents, changes and/or waivers will be posted on the corporate website at the internet address above.

*Board Role in Risk Oversight.* The board believes that long-term, sustainable value creation and preservation is attainable through the prudent assumption and management of both risks and potential rewards, and the Company's board as a whole takes a leading role in overseeing the Company's overall risk tolerances. Eight of the ten members currently serving on the Company's board also comprise the Bank's board and, therefore, are aware of and can report to the entire Company board regarding the Bank's risk-related policies, and help implement oversight by the Company's board. The financial institutions industry is highly-regulated; the board of the Bank maintains and considers compliance with various extensive formal policies that are reviewed and approved annually to ensure that the Bank and its policies comply with those regulations. The policies include, among other matters, those related to interest rate risk, business continuity risk, lending and underwriting, regulatory compliance, environmental risks, insider trading, codes of ethics and conduct, internal controls, information security and information technology risk management.

In addition, the Compensation Committee of the Company's board of directors also considers risk when making compensation determinations so as not to encourage excessive risk-taking. See "Risk Management and Compensation" below.

## **DIRECTORS' COMPENSATION**

### **Meeting Fees**

*The Company.* In 2012, Bank Mutual Corporation's directors who are not officers received a \$14,000 annual retainer for serving as a member of the board of directors. Each director also received a fee of \$1,600 per board meeting attended, the Chairman of the Audit Committee received \$1,000 for each Audit Committee meeting and each other non-officer director received \$600 for each meeting attended of a committee of which the director is a member. For purposes of determining fees, meetings include conference calls in which committee chairs and/or other representatives participate to review Company disclosures and filings. The same fees remain in effect for 2013. Some directors of the Company also serve as a director of the Bank; compensation for service on the Bank's board of directors is described below.

*The Bank.* The Bank does not pay a retainer fee to its directors. Each director received a \$1,400 fee for each board meeting attended and each non-officer director received a \$1,500 fee for attending an executive committee meeting. The same fees remain in effect for 2013.

Messrs. Baumgarten, Boerke, Brown, Buestrin, Crowley Jr., Herr, Mielke and Olson were directors of the Bank in 2012. Messrs. Baumgarten, Boerke, Buestrin, Crowley Jr. and Olson were members of the Bank's executive committee in 2012. Each individual who served as a director of the Bank or as a member of its executive committee in 2012 is expected to continue as such in 2013.

### **Stock Incentive Plans**

Bank Mutual Corporation directors are eligible to participate in the Company's 2004 Stock Incentive Plan ("2004 Stock Plan"). The options and restricted stock grants vest 20% per year, becoming fully vested after five years, subject to accelerated vesting in the event of a change in control of the Company, death or disability. Other than grants to Messrs. Boerke and Brown in 2008 when they joined the Company's board, no options or awards of restricted stock were granted to non-employee directors under either plan from 2005 through 2010. However, to recognize the additional responsibilities placed on directors as a consequence of recent legislation, the more stringent regulatory climate and the challenges in the weak economy, the Compensation Committee granted options to purchase 15,000 shares to each non-employee director in each of January 2011 and January 2012. Such options were granted at the average of the high and low trading prices on the grant date (which was \$3.39 for the 2012 grants), and vest over a five-year period. Similarly, the Compensation Committee granted options to purchase 11,000 shares to each non-officer director on January 22, 2013. Such options were granted at \$4.82 per share, the average of the high and low trading prices on that date, and vest over a five-year period. The Compensation Committee will consider in the future whether to continue annual grants, to revert to prior practices or to adopt a different approach.

### Deferred Plans for Directors

The Company maintains a deferred retirement plan for its non-officer directors (other than Messrs. Lopina, Olson and Swoboda who are covered by the First Northern plan described below). Non-officer directors who have provided at least five years of service will be paid \$1,167 per month for 10 years (or, if less, the number of years of service on the board) after their retirement from the Bank board or age 65, whichever is later. As of December 31, 2012, all of the existing eligible non-officer directors' benefits have vested. In the event a director dies prior to completion of these payments, payments will go to the director's heirs. The Company has funded these arrangements through "rabbi trust" arrangements and, based on actuarial analyses, believes these obligations are adequately funded. The plan may be amended by the Company's board of directors, although a plan amendment generally may not impair the rights of persons who are receiving benefits under the plan.

A similar deferred retirement plan of First Northern established prior to its acquisition by the Company in 2000 terminated upon First Northern's merger into the Bank in 2003. Messrs. Lopina, Olson and Swoboda have vested benefits under that plan, but do not accrue further benefits. That plan provides for monthly payments of \$1,000 for 180 months after the end of board service or until the director's death if earlier. Payments under that plan to Messrs. Lopina, Olson and Swoboda began in 2003 as a consequence of the merger of First Northern into the Bank and are continuing.

### Directors' Compensation Table

Set forth below is a summary of the compensation paid to each person who served as non-officer director in fiscal 2012:

**Directors' Compensation Table  
2012**

Name	Fees Earned or Paid in Cash (\$) (1)	Stock Awards (\$) (2)	Option Awards (\$) (2)	All Other Compensation (\$) (3)	Total (\$)
Mr. Boerke	76,000	0	12,900	14,000	103,500
Mr. Brown	47,600	0	12,900	14,000	74,500
Mr. Buestrin	77,800	0	12,900	0	90,700
Mr. Herr	39,400	0	12,900	0	52,300
Mr. Lopina	23,800	0	12,900	12,000	48,700
Mr. Mielke	43,600	0	12,900	0	56,500
Mr. Olson	77,500	0	12,900	12,000	102,400
Mr. Swoboda	22,600	0	12,900	12,000	47,500

- (1) Includes annual retainer, meeting, committee and chairmanship fees for services on the board of the Company and, when applicable, the Bank. For director fees paid to Messrs. Crowley Jr. and Baumgarten, see the "Summary Compensation Table" below.
- (2) As discussed above, on January 17, 2012, each non-officer director received options to purchase 15,000 shares of Company common stock. Such options were granted at \$3.39 per share, the average of the high and low trading prices on that date, and vest over a five-year period. The amounts shown reflect the grant date fair value computed in accordance with ASC 718 for grants and awards under the 2004 Stock Plan. ASC 718 requires the Company to recognize compensation expense for stock options and other stock-related awards granted to employees and directors based on the estimated fair value under ASC 718 of the

equity instrument at the time of grant. The assumptions used to determine the valuation of the awards are discussed in Note 11 to the consolidated financial statements. See the following table for information regarding all outstanding awards to non-officer directors.

The ultimate value of the options will depend on the future market price of Company common stock, which the Company cannot forecast. The actual value, if any, that an optionee would realize upon exercise of an option depends on the market value of Company common stock as compared to the exercise price when the option is exercised.

- (3) Represents, in the case of Messrs. Lopina, Olson and Swoboda, payments under the First Northern directors' deferred retirement plan. In the case of Messrs. Boerke and Brown, it represents benefits accrued during the fiscal year under the Company's deferred retirement plan for directors, based on one additional year of service. The deferred compensation payments for the non-officer directors have fully vested as of December 31, 2012. No further benefits are being accrued nor do any earnings accrue thereon.

\* \* \*

Each non-officer director who served as a director in 2012 had the following equity awards outstanding as of the end of fiscal 2012. For information regarding options and restricted stock held by Messrs. Baumgarten and Crowley Jr., see the "Outstanding Equity Awards at Fiscal Year-End" table below.

Name	Option Awards	Stock Awards
	Number of Securities Underlying Unexercised Options (#) (1) (2)	Number of Shares of Stock That Have Not Vested (#) (2)
Mr. Boerke	46,000	1,280
Mr. Brown	46,000	1,280
Mr. Buestrin	110,000	0
Mr. Herr	110,000	0
Mr. Lopina	110,000	0
Mr. Mielke	110,000	0
Mr. Olson	110,000	0
Mr. Swoboda	110,000	0

- (1) The options generally expire upon on the earlier of (i) 10 years from the date of grant or (ii) termination of service as a director, except that directors and executive officers have: (x) one year after death or termination due to disability to exercise options, whether or not exercisable at the time of such death or termination, or (y) one year upon a termination other than for cause to exercise options that were exercisable at the time of such termination.
- (2) Options and the restricted shares vest 20% per year in each of the five years after the grant date, or earlier in the event of a change in control of the Company, death or disability. The following option shares had vested as of December 31, 2012: Messrs. Brown and Boerke – 15,800 each; and Messrs. Buestrin, Herr, Lopina, Mielke, Olson and Swoboda – 83,000 each.

**Other**

See "Executive Compensation" for compensation paid to, and other compensatory agreements with, Messrs. Crowley Jr. and Baumgarten as executive officers and employees of Bank Mutual Corporation and the Bank. See also "Certain Transactions and Relationships with the Company" for information on amounts paid to Michael T. Crowley Sr., a former director and the father of Mr. Crowley Jr.

**SECTION 16(a) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE**

Under the federal securities laws, the Company's directors, executive officers and any person holding more than 10% of Company common stock are required to report their initial ownership of the common stock and any change in that ownership to the Securities and Exchange Commission ("SEC"). Specific due dates for these reports have been established and the Company is required to disclose in this proxy statement any failure to file such reports by these dates during the last year.

The Company believes that all of these filing requirements were satisfied on a timely basis for the year ended December 31, 2012. In making these disclosures, the Company has relied solely on written representations of its directors and executive officers and copies of the reports that they have filed with the SEC.

## EXECUTIVE OFFICERS

The following table lists the executive officers of the Company and the Bank as of March 1, 2013.

<u>Name and Age</u>	<u>Offices and Positions with the Company and the Bank (1)</u>	<u>Executive Officer Since</u>
Michael T. Crowley, Jr., 70	Chairman and Chief Executive Officer of the Company and the Bank (2)	1968
David A. Baumgarten, 62	President of the Company and the Bank since 2010; previously, Executive Vice President – Regional Banking of Associated Banc-Corp (2)	2010
Michael W. Dosland, 53	Senior Vice President and Chief Financial Officer of the Company and the Bank since 2008; former President and Chief Executive Officer of Vantus Bank and First Federal Bankshares from 2006 to August 2008; Lieutenant Colonel and Infantry Battalion Commander, United States Army, Iraq Theater of Operations prior thereto (3)	2008
P. Terry Anderegg, 62	Senior Vice President – Retail Banking of the Bank	1993 (4)
James P. Carter, 55	Vice President and Secretary of the Company since 2009; Vice President Corporate Counsel of the Bank since 1991	2009
Gregory A. Larson, 58	Senior Vice President – Director of Commercial Banking of the Bank since 2010; previously, Senior Vice President/Group Manager – Commercial Banking of Associated Bank, N.A.	2011 (5)
Christopher L. Mayne, 48	Senior Vice President – Chief Credit Officer of the Bank since 2011; previously, Senior Vice President – Senior Credit Officer for Middle Market Lending of Associated Bank, N.A.	2011 (5)
Richard L. Schroeder, 55	Vice President – Controller and Principal Accounting Officer of the Company since 2009, Vice President – Controller of the Bank since 2008; formerly Vice President – Finance of Guaranty Bank from 1995 to 2008	2009

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- (1) Excluding directorships and excluding positions with Bank subsidiaries. Those positions do not constitute a substantial part of the officers' duties. Includes other positions held in the past five years, if the individuals have not held their current positions for that entire period.
  - (2) Mr. Crowley Jr. became an executive officer of the Company in 2000; Mr. Crowley Jr. was also President of the Company and the Bank until 2010. As previously announced, Mr. Crowley Jr. will retire as Chief Executive Officer of the Company and the Bank effective as of July 1, 2013, but will remain as non-executive Chairman of both. Mr. Baumgarten will become Chief Executive Officer of the Company and the Bank, effective upon Mr. Crowley Jr.'s retirement.
  - (3) In September 2009, Vantus Bank was closed by the Office of Thrift Supervision, and the Federal Deposit Insurance Corporation was appointed as Vantus' receiver. Those events occurred more than one year after Mr. Dosland left his positions with Vantus Bank.
  - (4) This position has been considered to be an executive officer position of the Company since 2003.
  - (5) This position has been considered to be an executive officer position of the Company since 2011.

## COMPENSATION DISCUSSION AND ANALYSIS

**Summary.** The board's Compensation Committee (for purposes of this Compensation Discussion and Analysis, the "Compensation Committee" or the "Committee") makes decisions relating to Company compensation consistent with an intent to use compensation to attract and retain talented and highly-experienced personnel and to provide incentives for that personnel to maximize corporate performance. The major elements of compensation that the Committee uses to achieve these goals are driven by competitive market pressures and include:

- fixed salaries, which are intended to provide the Company's executive officers with a predictable stream of income for their living expenses, in an amount commensurate with their duties and responsibilities and which is competitive with peer companies;
- possible annual cash incentive bonuses, which tie potential additional cash compensation to specified objective Company financial goals and specific individual performance goals;
- stock-based compensation, which is intended to further align the interests of executive officers and shareholders and incent executive officers by providing economic rewards tied to increases in shareholder value; and
- longer-term compensation, including retirement benefits and protections in the event of a change in control, which are intended to retain executives and reward long-term service to the Company and provide a degree of security to executive officers to assist their focus on corporate goals.

In addressing these elements, the Company is aware that there is a high degree of competition for the services of talented employees, particularly those with significant experience in the financial institutions industry. The Committee particularly focuses on obtaining and retaining the services of highly-experienced personnel, especially those with a long-term commitment to the Company.

**Committee Composition.** The Bank Mutual Corporation board of directors has established a Compensation Committee to determine salaries of executive officers and make other compensation and benefit plan decisions. The Committee made compensation determinations for 2012, and expects to continue in that role going forward. All members of the Committee are independent directors.

**Compensation Philosophy.** In determining compensation, the Committee has recognized that the Company must provide its executive officers and key employees a market-competitive compensation package in order to attract and retain talented and highly-experienced personnel. The Committee has sought to offer compensation which it believes is in line with compensation paid by other similarly situated institutions, including banks, savings banks and savings associations, so as to be neither unduly generous nor lagging behind other institutions. In making its decisions, the Committee has also noted that, as a mutual institution, the Bank previously could not provide stock-based incentive compensation, as could publicly-held institutions, and noted the effect on prior compensation when going forward. In particular, and in part because of the years as a mutual institution, the Committee has sought to especially recognize and reward service to the Company over an extended period of time; the Committee believes that the Company greatly benefits from such continuity of experience.

The Committee has the ultimate authority within the Company to make fundamental decisions as to the types of compensation plans offered by the Company to its executive officers, as well as determining compensation levels under those plans. From time to time, the Committee uses outside consultants or advisors to assist it in analyzing the Company's compensation programs and determining appropriate levels of compensation and benefits. The Committee has full discretion as to whether to use compensation consultants or other third party services, as well as the identity and compensation of such persons or entities.

In making its determinations (including for fiscal 2012 and 2013), the Committee has utilized compensation summaries involving comparably-sized Midwestern financial institutions. While the Committee reviews these studies and uses them as a resource, it does not formally or numerically benchmark Company

compensation as compared to other companies or aim for any particular compensation level compared to those other companies. In 2012, these studies were prepared for the Committee by RP Financial, LC. (“RP Financial”), which also advises the Company and its management on certain other financial matters. Since the analyses by RP Financial have generally involved objective criteria and summarization, the Committee believes that RP Financial is sufficiently independent to make an appropriate review and that its relationship with RP Financial has not given rise to any conflict of interest, even though the Company utilizes RP Financial’s services for other purposes. RP Financial does not make recommendations to the Committee or management or otherwise act as a “compensation consultant.”

From time to time, the Company may also use other third-party compiled compensation information to assist in making compensation decisions. For example, in 2012, the Committee utilized the services of Milliman Inc. (“Milliman”), a provider of actuary services to the Company, to perform calculations to help with analyzing various potential changes to the Company’s pension plan. Prior to engaging Milliman to perform these calculations, the Committee considered the relevant factors set forth in the final SEC and proposed Nasdaq rules and determined that Milliman is sufficiently independent to appropriately advise the Committee on such matters and that its relationship with Milliman does not give rise to any conflict of interest. The Company is also considering whether to obtain additional consulting assistance in further evaluating its retirement plans.

As a federally-regulated savings bank holding company, the Company is subject to various laws and regulations that govern the compensatory plans, programs, agreements and arrangements established by the Company and the Bank. The Committee therefore establishes compensation in a manner intended to conform with those laws and regulations. Because the Company and the Bank have not received a federal capital infusion under the U.S. Treasury’s Troubled Assets Relief Program (“TARP”), the Company and the Bank are not subject to the specific compensation limits which apply to institutions receiving TARP funds or funds under other similar federal programs; however, given the number of recent legislative and regulatory proposals, the Company may become subject to additional compensation requirements or other limits in the future. In addition, compensation decisions, like all others, must be made with the safety and soundness of the regulated institutions in mind. See also “Risk Management and Compensation” below.

The Committee also considers the results of advisory “say-on-pay” shareholder votes when making compensation decisions. The Company holds such votes annually, and the Company’s shareholders have voted to approve the compensation of the Company’s executive officers at each previous annual meeting for which there was such an advisory vote.

In addition, upon request, other personnel of the Company (including from time to time executive officers) compile and summarize additional information and prepare tally sheets for the Committee. In 2012, Messrs. Crowley Jr. and Dosland provided these services. In addition, Messrs. Crowley Jr. and Baumgarten participated in discussions of, and made recommendations regarding, other executive officers’ compensation for 2012 and 2013, but not in discussions of their own.

***Elements of Compensation.*** The Company, with the review of the Committee, offers various types of compensation for its executive officers and, in most cases, other employees in order to achieve and balance various corporate goals and remain competitive with other financial institutions. The Company’s corporate compensation goals include attracting and retaining highly-qualified employees, motivating those employees to achieve improved corporate results without encouraging unnecessary risk taking, and connecting employees’ interests with shareholders’ interests in order to induce long-term commitment to the Company through the provision of financial security in retirement and, in the case of executive officers, in the event of a change in control of the Company.

***Salary.*** The Company provides a significant portion of compensation through a fixed salary. The Committee believes that providing competitive base salary levels is important in attracting and retaining talent, as salary levels are often the initial point of consideration in a compensation package. The Committee also believes salary is important to provide officers with a steady and predictable source of income for them and for their families’ basic living needs. Salaries are intended to be commensurate with their duties and responsibilities and market competitiveness.

*Cash Bonus/Incentives.* The Committee considers it important to offer financial incentives to achieve corporate performance goals that are measured by specific financial metrics. Therefore, the Company provides annual cash incentives through its Management Incentive Compensation Plan (the "Management Incentive Plan"). Under the Management Incentive Plan, the Committee establishes Company financial performance criteria upon which cash incentives depend. The Committee believes it is important to align performance criteria with specific incentives to promote achievement of corporate financial goals. These goals are particularly targeted to the Company's goals and results, and do not depend upon stock market performance, which can be heavily influenced by factors outside of the Company's control and its own financial performance. The Committee believes that this creates further incentive for employees to achieve corporate goals and aims to establish goals that are reasonably achievable but do not encourage unnecessary risk taking.

Individual goals are also set for the executive officers (other than the CEO and the President, whose bonuses solely depend on corporate performance) and employees, and a portion of their bonuses depend upon the achievement of these goals. The Committee believes that it is important to particularize some portion of the bonuses for these individuals to incent personal performance. However, in the case of executive officers, to recognize the importance of the Company-wide goals, these plan bonuses may be earned only if the Company also meets its corporate financial performance thresholds.

In addition, the Committee may from time to time award discretionary bonuses based on various factors and achievements, including for example, the successful completion of a specific project, achievement of meaningful business development or increased profitability, responding to adverse economic conditions, promotion to a new position or increased responsibilities and case-by-case increases driven by competitive pressures and market conditions.

*Stock-Based Plans.* Historically, the Company and the Committee have provided incentives that link executive officers' compensation to the returns experienced by Company shareholders. To accomplish that, the Committee maintains a stock incentive plan (and, in prior years, utilized an employee stock ownership plan) to provide awards of Company common stock.

Under the Company's 2004 Stock Incentive Plan ("2004 Stock Plan"), the Committee may grant stock options and make management recognition awards of shares of restricted stock. Stock options, which are awarded at the average market value (average of the high and low trading prices) on the date of grant, are intended to reward option holders in the event of increases in market price of that stock over time. Restricted stock grants are intended to provide an additional equity stake in the Company with the goal of helping grantees further identify with other shareholders of the Company. Both options and restricted stock vest over five-year periods, both to comply with the Office of the Comptroller of the Currency ("OCC") regulations and to incent long-term employment with the Company.

The 2004 Stock Plan and a similar predecessor plan were established in connection with the Company's conversion from a mutual institution to a fully shareholder-owned institution. The Company's and the Bank's primary regulator at the time of the conversion, the Office of Thrift Supervision ("OTS"), had regulations that significantly controlled the types and provisions of plans that could be adopted shortly after conversion. Because the 2004 Stock Plan and its predecessor plan were adopted during those periods, they were limited by those regulations. In light of the OTS regulations and in recognition of the fact that periods of conversion from a mutual form of organization create insecurity for management and other employees, the Committee did not believe it was appropriate to impose further limitations upon the stock plans. Therefore, for example, the Company chose to implement plans that provide for time vesting (rather than performance vesting) for the awards. In addition, through 2010, the Company historically has made relatively large option grants only after the two conversion transactions and in connection with new hires, rather than making annual grants, because it believed that this practice would recognize the past service of key employees, best recognize long-term service to the Company and attract key employees to join, and incent them to remain with, the Company.

The Committee regularly considers how frequently to make equity grants. As a result of those reviews and other relevant factors, in January 2011, the Committee granted certain officers and key employees an aggregate of options to purchase 318,500 shares of common stock. Similarly, in January 2012, the Committee granted an aggregate of options to purchase 282,500 shares of common stock and awarded an aggregate of 97,500 shares of

restricted stock to certain officers and key employees, including 20,000 option shares and 10,000 shares of restricted stock to Mr. Crowley Jr., 40,000 option shares and 20,000 shares of restricted stock to Mr. Baumgarten and 20,000 option shares and 10,000 shares of restricted stock to each of Messrs. Dosland, Anderegg, Larson and Mayne. Such options were granted at \$3.39 per share, the average of the high and low trading prices on that date, and vest over a five-year period. The Committee also considers and makes additional grants in connection with new hiring and significant promotions.

Given the Company's improved financial performance in 2012 and in order to further align the interests of certain key employees with the interests of the Company's shareholders, on January 22, 2013, the Committee granted certain officers and key employees an aggregate of options to purchase 214,000 shares of common stock and awarded an aggregate of 93,600 shares of restricted stock to them, including 12,000 option shares and 13,100 shares of restricted stock to Mr. Crowley Jr., 24,000 option shares and 20,500 shares of restricted stock to Mr. Baumgarten and 12,000 option shares and 10,000 shares of restricted stock to each of Messrs. Dosland, Anderegg, Larson and Mayne. Such options were granted at \$4.82 per share, the average of the high and low trading prices on that date, and vest over a five-year period. The Committee will consider in the future whether to continue annual grants, to revert to prior practices or to adopt a different approach. The form of option agreement currently used by the Company provides for clawbacks in the event of violations of post-employment covenants.

The 2004 Stock Plan expires in February 2014 and no more awards can be granted under the 2004 Stock Plan after that date. Therefore, in 2013, the Committee will consider when and whether to adopt a new equity and/or incentive plan and, if it decides to pursue a new plan, will seek shareholder approval of the plan as appropriate.

In addition, at the time of the 2000 initial conversion transaction, the Company established an Employee Stock Ownership Plan ("ESOP") to provide further equity ownership of the Company generally throughout the Company's employee base. The ESOP was intended to increase the depth of share ownership among employees and to align employees' interests with those of the shareholders. After giving effect to 2010 service, all of the shares available under the ESOP had been allocated to participants' accounts and no unallocated shares remain. The Company does not currently have plans to allocate additional shares to the ESOP, although that decision may be reconsidered at some time in the future.

*Retirement and Post-Employment Compensation.* The Company maintains the Bank Mutual Corporation Pension Plan (the "Pension Plan"), a defined benefit plan, and the Company's 401(k) Retirement Plan (the "401(k) Plan"), a defined contribution plan that also allows voluntary employee contributions. In connection with these plans, the Company also maintains a supplemental retirement plan (the "Supplemental Plan"), in which Mr. Crowley Jr. and Mr. Baumgarten participate. The Company has also adopted a Benefit Restoration Plan (the "Restoration Plan") relating to the 401(k) Plan in order to provide the equivalent of full participation by any Company employee whose compensation is above Internal Revenue Code (the "Code") limitations. The Company believes that maintaining the Restoration Plan is appropriate so that the persons covered by the Restoration Plan can receive benefits similar to other Company employees, so as not to dis-incent the highest-paid personnel.

The Company and its predecessors have maintained the Pension Plan for over 45 years. Under the Pension Plan, which is supplemented by the Supplemental Plan, benefits are determined by a matrix depending upon final average compensation (salary and bonus) and years of credited service to the Company. It is Company policy to evaluate the Pension Plan periodically to help ensure that it is adequately funded and determine whether other changes are necessary. The Committee has historically believed that it is appropriate to offer a defined benefit retirement plan because the Company's employees have, over the course of many years, come to depend upon the Pension Plan as a source of income to provide security in retirement and because the years of service provisions of the Pension Plan incent employees to remain with the Company over time, thus helping to provide the Company with a stable and experienced employee base.

The Company's 401(k) Plan permits supplemental employee contributions, with a minimal Company match. The Committee maintains the 401(k) Plan to provide employees an additional vehicle under which they can further save for retirement. Under the 401(k) Plan, the Company makes matching contributions up to a stated percentage of the participating employee's salary because it believes that this modest incentive assists with

employee morale and long-term employee well-being. During 2012, the Company matched participating employees' contributions up to 1% of their salary.

As a result of the rising costs to the Company of maintaining the defined benefit Pension Plan, which were caused in part by the increase in recent years in the actuarial present value of benefits under the Pension Plan (which includes the effects of the low discount rates in recent years used to calculate the present value), in 2012, the Committee utilized the services of Milliman to perform calculations to help with analyzing various potential changes to the Company's Pension Plan. After reviewing those calculations and considering the increasing costs to the Company, the Committee closed the qualified defined benefit Pension Plan to employees not eligible to participate as of January 1, 2013, as well as any employees hired after that date. In addition, effective for service performed after March 1, 2013, the Committee reduced certain future benefits formerly provided under the Pension Plan and the Supplemental Plan, but did not reduce all future benefits. The Committee also contemplates that the 401(k) Plan be amended such that, for employees who are not eligible to participate in the Pension Plan, the Company will match \$0.50 for each \$1.00 of employee salary deferral up to a maximum of 3% of the employee's base salary plus incentive compensation and the Company match will vest over three one-year periods. The Company match under the 401(k) Plan for employees who are eligible to participate in the Pension Plan would remain the same (i.e., up to 1% of the employee's base salary). The Committee believed that, due to the closing of the Pension Plan to certain employees, it would be appropriate to provide a more generous match to those employees under the 401(k) Plan to remain competitive in the marketplace and make up for some of the lost pension benefit. The Committee will continue to regularly review the Company's retirement benefit programs and will continue to consider changes when and if appropriate.

The Restoration Plan and the Supplemental Plan are intended to provide benefits equivalent to those under the Pension Plan and 401(k) Plan for certain individuals whose benefits otherwise are limited with respect to qualified tax treatment under the Code as a result of income or payment limitations. The Committee has continued to maintain the Restoration Plan and the Supplemental Plan because it has believed that it is not appropriate to provide these individuals with a benefit that is proportionately less than other employees simply due to the Code's limits on covered salary and/or years of service that may be considered in a tax-qualified retirement plan. In essence, these additional plans only retain the same percentage level of benefit that would have applied but for the Code's limits. As with the Company's other retirement benefit programs, the Committee regularly reviews the Restoration Plan and Supplemental Plan and will continue to consider changes when and if appropriate.

*Employment Agreements.* The Company has employment agreements with Messrs. Crowley Jr., Baumgarten, Dosland, Anderegg, Larson and Mayne. These agreements include change in control provisions. The Committee believes it is important to have agreements, including change in control provisions, to provide security to the executive officers in view of their long-term dedication to the Company, which the Company, in turn, believes will facilitate those officers' commitment and dedication to the Company, especially in cases where Company interests may diverge from a personal interest. The Committee believes this is particularly important in the case of a potential acquisition. The change in control provisions utilize a "double trigger" before benefits are payable because the Committee did not believe it was appropriate to provide benefits simply upon the change in control if employment is not affected.

*Other Benefits.* Executive officers qualify for the same group health, life and disability insurance benefits as other full-time salaried employees of the Company. The Committee believes that these insurance benefits are generally important to address market conditions and attract and retain qualified employees. In addition, the Company reimburses officers and other high-level employees for approved memberships in certain civic and industry groups, appropriate attendance at related functions and, in the case of Messrs. Crowley Jr. and Baumgarten, the cost of club memberships used exclusively for appropriate business entertaining. However, because these expenses are reimbursed only if and to the extent they are specifically incurred for business purposes, these are not considered by the Committee to be "perquisites" or personal benefits to these persons. The Committee seeks to minimize any benefits or "perquisites" for executive officers which are not on the same terms and conditions as other salaried employees; however, certain executives receive use of a business automobile and/or a car allowance, which is not on the same terms as other salaried employees due to their significant business travel.

**2012 Annual Compensation Determinations.** The Committee makes determinations of salary and cash bonus incentives, and decisions relating to awards of stock-based incentives, on an annual basis. The following paragraphs discuss the Committee's determinations for 2012, and include the results under the annual cash incentive plan for 2012.

**Base Salary.** In determining the base salary of executive officers for 2012, the Committee reviewed, among other things, peer group information gathered by Committee members and management and the historical compensation of the officers and the performance of the Company, as well as RP Financial's studies of peer institutions. The Committee also prepares tally sheets summarizing compensation, awards and vesting over the past several years under the various plans and arrangements under which the officers receive compensation and benefits. In addition, the CEO and President provide the Committee with salary recommendations for each executive other than themselves. After reviewing the various materials and considering management's recommendations, the Committee discusses each executive individually and decides his or her base compensation for the upcoming year.

The bonus and incentive plans are heavily performance based, tied to the financial metrics described below, and remained a significant source of potential compensation in 2012. As a result, base salary determinations for 2012 were not directly related to statistical corporate performance. In addition, the Committee noted that stock-based awards were granted in 2011 and 2012 to a number of officers and key employees, including then serving executive officers.

Based upon those factors, the Committee determined that executive officers should receive increases in base salary for 2012, with amounts varying depending upon individual responsibilities and salary levels. The following table contains information showing the percentage increase in base salary that each of the named executive officers received in 2012.

<b>Name</b>	<b>2012 Base Salary (\$)</b>	<b>Increase in Base Salary Over 2011 (%)</b>
<b>Mr. Crowley Jr.</b>	696,000	0.0
<b>Mr. Baumgarten</b>	525,000	16.7
<b>Mr. Dosland</b>	212,000	7.1
<b>Mr. Anderegg</b>	212,000	2.4
<b>Mr. Larson</b>	215,000	7.5
<b>Mr. Mayne</b>	205,000	7.9

Mr. Crowley Jr., recognizing the additional duties being assumed by Mr. Baumgarten, declined to accept a salary increase for 2012 and waived all rights to any increase the Committee may have otherwise awarded. The higher percentage increase in base salary from 2011 to 2012 for Mr. Baumgarten when compared to other executive officers is because the Committee believed that it was appropriate to reward Mr. Baumgarten's continuing strong performance in his position and that the increased amount was commensurate with his expanding role with the Company going forward and was competitive with the market. The increases for Messrs. Dosland, Anderegg, Larson and Mayne reflected their continuing in their current positions, as well as a satisfactory review of personal performance.

The salary increases for the named executive officers in 2013 compared to 2012 were 0.0%, 14.3%, 3.8%, 3.8%, 3.7% and 5.9% for Messrs. Crowley Jr., Baumgarten, Dosland, Anderegg, Larson and Mayne, respectively. As in recent years, Mr. Crowley Jr. did not accept an increase, in spite of the Committee's satisfaction with his performance as a result of his recognition of the additional duties being assumed by Mr. Baumgarten. Mr. Baumgarten's increase for 2013 was at the high end of the range because of his continuing strong performance and his continued growing role with the Company. Subsequent to the Committee's compensation determinations for 2013, Mr. Crowley Jr. announced his intention to retire as Chief Executive Officer effective July 1, 2013. Following his retirement as CEO, Mr. Crowley Jr. will remain as non-executive Chairman of the Company and the Bank and will receive director fees on the same basis as other non-employee directors of the Company and the Bank; in addition, Mr. Baumgarten will become CEO at that time. The increases for Messrs. Dosland, Anderegg, Larson and Mayne for 2013 reflected their satisfactory personal performance and adjustments necessary to keep their base salaries competitive with other individuals performing similar functions within the geographic and industry market based on the Committee's informal review of available data.

*Cash Bonus/Incentives.* For fiscal 2012, annual cash bonus payments were determined under the Management Incentive Plan. Under the Management Incentive Plan, a portion of each participant's (other than the CEO's and the President's) incentive opportunities is based on corporate performance and a portion on individual performance. The Management Incentive Plan provides bonus payments depending whether the Company achieved various threshold, target or maximum levels of performance. The Committee used net income and diluted earnings per share as the performance metrics for 2012, and set the Company's net income target at \$5.2 million and the diluted earnings per share target at \$0.11. The targets represented the level of achievement for each metric as contained in the Company's budget for 2012. The Compensation Committee believed it was appropriate to set the target level at the budgeted number because the budget represented a satisfactory level of performance for the Company for the year and was a reasonable increase in performance over the prior year results. The Committee also believed that the budgeted numbers were appropriate because they balanced an increase in Company financial performance while still maintaining the Company's ongoing conservative operating principles and not encouraging unnecessary risks, and because it believes that the targets were reasonably achievable given maximum effort.

For 2012, if the targets were met, each of the named executive officers would receive target bonus payments (expressed as a percentage of base salary), which vary from 20% of salary for Messrs. Crowley Jr. and Baumgarten to 18% for other eligible named executive officers. Each eligible individual can earn up to double the target amount if performance reaches maximum levels. The actual amount of the bonus pool for all participants is determined based upon the Company's performance with respect to the financial criteria mentioned above; however, the actual bonus paid to each individual is determined only after also considering individual performance, as discussed below. For 2012, for each percentage point by which the Company missed its targets, the potential bonus pool would have been reduced by 1.5 percentage points. For each percentage point above target, the potential bonus pool would have been increased by 1 percentage point (in prior years, the potential bonus pool increased 2 percentage points for each percentage point above target). If Company performance reached at least 80% of the target amounts, participants would be eligible to receive threshold bonuses (which are equal to the target bonus amount minus the 1.5 times percentage point reduction discussed above -- i.e., 70% of target bonus payout). If the Company's performance was below 80% of the performance target, no bonuses would be paid. Net income and diluted earnings per share will be used as metrics for 2013.

The Management Incentive Plan also permits a portion of the bonus to be determined based on individual performance goals. Under the plan in 2012, 50% of the bonus for the eligible named executive officers (excluding Messrs. Crowley Jr. and Baumgarten) was connected to individual performance goals and the other 50% of bonuses was connected to corporate performance. This was a change from prior years (previously, the split had been 80% based on corporate performance and 20% based on individual performance) because the Committee wanted to impose more personal performance accountability on the plan participants. In practice, the Committee will determine the amount of the actual bonus pool based on the Company's performance under the chosen metrics and then will determine the actual bonus paid to each individual plan participant after evaluating and factoring in his or her individual performance. Under the plan in 2012, if the Company did not reach at least 80% of its targeted performance goals, no bonuses (neither corporate performance based nor personal performance based) would be paid; however, even in those cases, individuals may have been eligible to earn discretionary bonuses. In the case of Messrs. Crowley Jr. and Baumgarten, their bonuses are determined solely on corporate performance because, as the CEO and the President, respectively, each has responsibility for the Company and its operations as a whole and, as a result, each individual's personal performance can be measured by the Company's performance. Discretionary bonuses can be based on various factors, including for example, the successful completion of a specific project, achievement of meaningful business development or increased profitability, responding to adverse economic conditions, promotion to a new position or increased responsibilities and case-by-case increases driven by competitive pressures and market conditions.

With respect to fiscal 2012 corporate performance, the Company exceeded the targets set for each of the net income and the diluted earnings per share metrics. Near the end of 2012, the Committee evaluated the Company's financial performance for each of these metrics. Due to potential changes expected to be made to U.S. federal income tax laws related to the "fiscal cliff," the Committee decided that it was appropriate to accelerate into 2012 the payment of the bonuses under the Management Incentive Plan based on conservative estimates of the Company's financial results. The Committee determined that the Company's net income for 2012 for purposes of the Management Incentive Program was \$6.7 million or 128.8% of target, which would generate a payout of 128.8% of the target payout, and that the diluted earnings per share for purposes of the Management Incentive Program was

\$0.14 per share or 127.3% of target, which would generate a payout of 127.3% of the target payout. Together, under the formula, the corporate financial performance factors of the Management Incentive Plan generated a payout amount of approximately 128% of the target. Because the ultimate payout under the Management Incentive Plan is weighted to include both corporate financial performance (50%) and individual performance (50%) (except for Messrs. Crowley Jr. and Baumgarten, whose incentive opportunities under the plan are based 100% on corporate performance), the Committee, with significant input from Mr. Baumgarten, evaluated the individual performance of Management Incentive Plan participants to determine the ultimate payout to each participant. Based on those reviews, the Committee awarded incentive payments under the Management Incentive Plan to the named executive officers as follows: Mr. Crowley Jr. – \$180,960; Mr. Baumgarten – \$136,500; Mr. Dosland – \$48,760; Mr. Anderegg – \$48,760; Mr. Larson – \$49,450; and Mr. Mayne – \$47,150. In early 2013, it was determined that the definitive financial results for the plan metrics resulted in net income of \$6.8 million and diluted earnings per share of \$0.15, which in each case was slightly better than the amounts used in December to determine the payouts; however, the Committee did not adjust the payouts under the plan based on the higher results.

*Stock-Based Incentives.* The Committee believes that stock-based compensation can provide an important incentive to executive officers that aligns officers' interests with those of shareholders, since the value of the compensation will depend upon the performance of the stock price. However, in view of the significant awards made in 2001 and 2004 under the 2004 Stock Plan and its predecessor plan, the Committee did not grant any stock options, or award any restricted shares, to persons who were then serving as executive officers from 2005 through 2010, other than in connection with new hires. As mentioned above, in January 2011 and again in January 2012, the Committee made broadly-based equity awards to various persons, including certain executive officers. Similarly, in January 2013 the Committee granted options and restricted shares on a broad basis to various persons, including the executive officers.

*Other Benefits.* In 2012, Mr. Crowley Jr. received use of a business automobile, and Mr. Baumgarten received use of a gasoline credit card and monthly automobile allowance, which benefits were not on the same terms as other salaried employees. The value of these benefits totaled less than \$500 and \$5,000, respectively.

*Chief Executive Officer Compensation.* In addition to the factors discussed above, when determining the salary of the CEO, the Committee continued a transition, which began in 2002, to more incentive-based compensation because the Committee continues to believe that that type of compensation provides well-targeted incentives and encourages employees to strive to achieve corporate goals. Typically, in making its determinations, the Committee reviews the CEO's performance and goals during the prior year and also considers the substantial roles of the CEO in the Company and the Bank to determine an appropriate salary level for the CEO. However, prior to the Committee making its determination for 2012, Mr. Crowley Jr., recognizing the additional duties being assumed by Mr. Baumgarten, informed the Committee that he would decline to accept a salary increase and waived all rights to any increase the Committee may have otherwise awarded. Notwithstanding that he has declined salary increases from 2010 to 2013, the Committee believes that Mr. Crowley Jr.'s salary level compared to other executive officers is appropriate as it reflects his relative role in the organization. In addition, in 2012, the CEO received a bonus under the Management Incentive Plan equal to 128% of the target amount because the Company exceeded the financial targets set forth in the plan.

Because of the significant level of option and restricted stock awards in 2001 and 2004 under the 2004 Stock Plan and its predecessor, no awards were made to the CEO from 2005 through 2010. In 2011, 2012 and 2013, in connection with the equity awards discussed above, Mr. Crowley Jr. received options to purchase 15,000 shares in 2011, 20,000 option shares and 10,000 shares of restricted stock in 2012 and 12,000 option shares and 13,100 shares of restricted stock in 2013, respectively. The CEO also receives meeting fees for service on the Company's and the Bank's boards of directors. In accordance with long-standing company policy, in 2012, the CEO received \$8,000 in meeting fees related to service provided to the Company's board and \$16,800 in meeting fees related to service provided to the Bank's board. In his role as non-executive Chairman following his retirement as CEO, Mr. Crowley Jr. will receive director fees on the same basis as other non-employee directors.

*Restoration Plan and Supplemental Plan.* In setting compensation for 2012, the Committee considered the CEO's and the President's participation in the Company's Restoration Plan and their supplemental retirement benefits. Under the Restoration Plan (as well as a prior restoration plan relating to the ESOP), based on salary deferrals and Company contributions throughout his years of service to the Company, Mr. Crowley Jr. has

accumulated the right to receive payments totaling \$659,988, due to the limitation of benefits under qualified plans relating to the 401(k) Plan and the ESOP. Further, the increase in the actuarial present value of pension benefits under the Supplemental Plan during 2012 (which includes the affects of the discount rate used to calculate the present value) for Mr. Crowley Jr. and Mr. Baumgarten was \$1,285,419 and \$12,310, respectively. For more information about the change in the present value of pension benefits, see footnote 4 to the "Summary Compensation Table" and the "Pension Benefits" table below.

The Committee continued to believe it is fair and appropriate to maintain the Restoration Plan and the Supplemental Plan to fully recognize the CEO's and the President's compensation when determining benefits under other plans which generally are available to all full-time employees because it wants to remain competitive with industry peers and properly reward the CEO's and the President's efforts and because it has believed that it is not appropriate to provide the CEO and the President with a benefit that is proportionately less than other employees simply due to the Code's limits on covered salary and/or years of service which may be considered in a tax-qualified retirement plan. In essence, the Restoration Plan and Supplemental Plan only retain the same percentage level of benefit which would have applied but for the Code's limits.

***Employment Agreements/Change in Control Provisions.*** The Company maintains employment agreements, which include change in control provisions, with Messrs. Crowley Jr., Baumgarten, Dosland, Anderegg, Larson and Mayne. See "Executive Compensation—Employment Agreements and Potential Payments Upon Termination or Change in Control" below. The Company has entered into these employment agreements, and the Committee generally continues to renew them on an annual basis, because it believes that the agreements provide an appropriate degree of security for these officers which, in turn, enhances their continuing efforts to pursue Company goals, even in situations where they may not align with their personal interests. The employment agreements with Messrs. Crowley Jr. and Baumgarten are more extensive than those of other executives, in recognition of their more extensive responsibilities. The form of employment agreement is the same for Messrs. Dosland, Anderegg, Larson and Mayne. Mr. Crowley Jr.'s agreement has a rolling three-year period and Mr. Baumgarten's has a rolling two-year period; the agreements with the other executives have a one-year term. The employment agreements are renewed annually and may be extended. As of January 2013, Mr. Crowley Jr.'s agreement was renewed through the end of 2015 (although the agreement will terminate, other than for post-retirement obligations, upon Mr. Crowley's retirement later in 2013), Mr. Baumgarten's through the end of 2014 and the other executives through the end of 2013.

The employment agreements and the 2004 Stock Plan include provisions that provide additional protections to the employees in the event of a change in control of the Company. The Committee believes it is important to have these types of agreements with the executive officers in order to provide them with incentive to fully consider transactions that may be in the Company's best interest, but which may jeopardize the security of their individual positions. The Company has adopted particular change in control provisions in an attempt to balance the potential cost of these provisions to an acquirer, which the Committee believes to be quite modest, with a meaningful degree of security to the affected personnel. In particular, the change in control provisions in the Company's employment agreements have a "double trigger," which means that change in control benefits are payable to the executive only if the ownership or control of the Company changes and, after such change, the executive's compensation or duties are significantly reduced or altered. The Company utilizes the double trigger because it believes that, while it is appropriate to provide some protection to key personnel in the event of an acquisition, those protections should be limited to situations in which actions are taken that substantially affect their compensation or employment. However, under the 2004 Stock Plan, there is a single trigger so that unvested options and restricted shares automatically vest upon a change in control. The Committee also determined that it would be appropriate to cap the potential change in control payments to the amount for which the Company could achieve a tax deduction, in order to balance the interests of the Company and the individuals. The 2004 Stock Plan provides for automatic vesting upon a change in control because the Committee believes that the recipients of these awards should receive the intended benefits in the event that the Company's shareholders receive a commensurate benefit in a transaction.

**Tax Considerations.** Section 162(m) of the Code limits the deductibility of compensation in excess of \$1 million during a fiscal year to certain executive officers of publicly-held companies. Exceptions are made for, among other things, performance-based plans approved by shareholders. Stock options are considered performance-based compensation; however, restricted stock awards are not unless they are coupled with performance goals. The Committee is mindful of these limitations. Shareholder approval of the 2004 Stock Plan has been obtained, among other reasons, to qualify for an exception from current Section 162(m) for any stock options awarded under the plan. The board believed it was extremely unlikely that other awards that would not qualify for the Section 162(m) exclusion would be made at a level that would cause the Section 162(m) limit to be exceeded.

Other provisions of the Code can also affect the decisions the Company makes. Under Section 280G of the Code, a 20% excise tax is imposed upon executive officers who receive "excess" payments upon a change in control if the payments exceed an amount approximating three times their average annual compensation, determined by a five-year average. The excise tax applies to all payments over the executive's average annual compensation. Under Section 280G, the Company would not be able to deduct "excess" payments. To avoid application of Section 280G, the executives' change in control agreements provide that benefits payable pursuant to them are limited to 2.99 times the "average compensation" as determined under the Code.

Section 409A of the Code amended the tax rules to impose restrictions on funding, distributions and elections associated with nonqualified deferred compensation arrangements. Section 409A imposes substantial penalties and results in the loss of any tax deferral for nonqualified deferred compensation that does not meet its requirements. The Company has amended its compensation programs and plans, and employment agreements with executive officers, to comply with the distribution, timing and other requirements of Section 409A. These actions are intended to prevent certain elements of executive compensation to result in substantial tax liability for the named executive officers pursuant to Section 409A. These changes have not had a material tax or financial consequence on the Company.

#### **COMPENSATION COMMITTEE REPORT ON EXECUTIVE COMPENSATION**

As part of its duties, the Compensation Committee has reviewed and discussed with management the "Compensation Discussion and Analysis" contained above in this proxy statement. Based upon that review and those discussions, the Compensation Committee recommended to the board of directors that the Compensation Discussion and Analysis be incorporated by reference in the Company's annual report to shareholders on Form 10-K and be included in this proxy statement.

Members of the Compensation Committee:

William J. Mielke, Chairman  
David C. Boerke  
Thomas J. Lopina, Sr.  
Robert B. Olson

## EXECUTIVE COMPENSATION

The following table contains compensation information with respect to the Company's Chief Executive Officer, Chief Financial Officer and the four other most highly-compensated individuals who were serving as executive officers of the Company at the end of 2012 (collectively referred to occasionally in this section as the "named executive officers").

### Summary Compensation Table

Name and Principal Position	Year	Salary \$(1)	Bonus \$(2)	Stock Awards \$(3)	Option Awards \$(3)	Non-Equity Incentive Plan Compensation \$(2)	Change in Pension Value and Nonqualified Deferred Compensation Earnings \$(4)	All Other Compensation \$(5)	Total (\$)
<b>Michael T. Crowley, Jr.</b> <i>Chairman and Chief Executive Officer of the Company and the Bank (6)</i>	2012	720,800	0	33,900	17,200	180,960	1,077,425	7,932	2,038,217
	2011	717,400	125,280	0	17,400	0	1,739,700	7,440	2,607,220
	2010	721,400	0	0	0	0	826,944	21,123	1,569,467
<b>Michael W. Dosland</b> <i>Senior Vice President – Chief Financial Officer of the Company and the Bank</i>	2012	212,000	0	33,900	17,200	48,760	46,156	3,693	361,709
	2011	198,000	32,076	0	17,400	0	33,368	2,620	283,464
	2010	192,000	0	0	0	0	18,462	7,513	217,975
<b>David A. Baumgarten</b> <i>President of the Company and the Bank (6)</i>	2012	549,800	0	34,400	67,800	136,500	17,393	9,847	815,740
	2011	471,400	81,000	0	58,000	0	13,799	8,939	633,138
	2010	289,281	0	100,300	76,000	0	0	5,350	470,931
<b>P. Terry Anderegg</b> <i>Senior Vice President – Retail Banking of the Bank</i>	2012	212,000	0	33,900	17,200	48,760	183,448	3,493	498,801
	2011	207,000	33,534	0	17,400	0	178,893	2,070	438,897
	2010	202,300	0	0	0	0	91,453	9,831	303,584
<b>Gregory A. Larson</b> <i>Senior Vice President – Director of Commercial Banking of the Bank (7)</i>	2012	215,000	0	33,900	17,200	49,450	45,003	3,884	364,437
	2011	200,000	32,400	0	0	0	0	951	250,751
	2010	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
<b>Christopher L. Mayne</b> <i>Senior Vice President – Chief Credit Officer of the Bank (7)</i>	2012	205,000	0	33,900	17,200	47,150	15,733	1,846	320,829
	2011	182,700	45,780	50,500	58,000	0	0	600	337,580
	2010	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A

- (1) Includes amounts voluntarily deferred by the named persons under the Restoration Plan. The voluntarily deferred amounts are included in the "Executive Contributions in Last FY" column of the "Nonqualified Deferred Compensation" table below. Includes, for Messrs. Crowley Jr. and Baumgarten, amounts they received for meeting fees as a member of the boards of directors of the Bank and the Company. Mr.

Crowley Jr. received \$25,400, \$21,400 and \$24,800 for such service in 2010, 2011 and 2012, respectively. Mr. Baumgarten received \$13,800, \$21,400 and \$24,800 in 2010, 2011 and 2012, respectively.

- (2) No bonuses, either discretionary or based on the formulas under the Management Incentive Plan, were earned in fiscal 2010. In 2011, no bonuses were earned based on the formulas under the Management Incentive Plan; however, discretionary bonuses were awarded to participants under the Management Incentive Plan. For Mr. Larson, the 2011 bonus reflects a purely discretionary bonus outside of the Management Incentive Plan, as he was not a participant in the plan in 2011. For Mr. Mayne, the 2011 bonus amount also includes a \$15,000 signing bonus that he received when he started employment with the Company. In 2012, the Company exceeded the corporate performance targets set forth in the Management Incentive Plan; as a result, the named executive officers received a bonus in the amounts set forth under "Non-Equity Incentive Plan Compensation." See "Compensation Discussion and Analysis—2012 Annual Compensation Determinations—Cash Bonus/Incentives" for additional information regarding bonuses.
- (3) Other than a grant to Mr. Baumgarten in 2010, no options were granted, nor were shares of restricted stock awarded, to persons then serving as executive officers in 2010 (although Mr. Larson did receive an equity grant upon his joining the Company late in 2010). As discussed above, certain executive officers received option awards, and Mr. Mayne also received an award of restricted stock, in 2011, and certain executive officers, including the named executive officers, received option awards and restricted stock grants in 2012. The amounts shown reflect the grant date fair value computed in accordance with ASC 718 for grants and awards under the 2004 Stock Plan made in each year. ASC 718 requires the Company to recognize compensation expense for stock options and other stock-related awards granted to employees and directors based on the estimated fair value under ASC 718 of the equity instrument at the time of grant. The assumptions used to determine the valuation of the awards are discussed in Note 11 to the consolidated financial statements. See the "Outstanding Equity Awards at Fiscal Year-End" table below for information regarding all outstanding awards.

The ultimate value of the options will depend on the future market price of Company common stock, which the Company cannot forecast. The actual value, if any, that an optionee would realize upon exercise of an option depends on the market value of Company common stock as compared to the exercise price when the option is exercised.

- (4) Represents the increase in the actuarial present value of pension benefits, under both the tax-qualified Pension Plan and the related Supplemental Plan, between fiscal years. The present value of accumulated benefits at December 31, 2012, 2011 and 2010 was calculated based on discount rates of 3.70%, 4.21% and 5.32%, respectively, and using the RP 2000 mortality table for determining post-retirement mortality. Of the amounts listed under the column entitled "Change in Pension Value and Nonqualified Deferred Compensation Earnings" in the "Summary Compensation Table" above, the portion of the increase in the present value of pension benefits that is attributable to accumulated benefits and the portion of the increase that is attributable solely to the change in the discount rates used in the calculation of benefits is shown in the following table:

	Year	Change in Pension Value (\$)	Portion of Change in Present Value Attributable to Accumulated Benefit (\$)	Portion of Change in Present Value Solely Attributable to Change in Discount Rate Compared to the Prior Year (\$)
Mr. Crowley Jr.	2012	1,077,425	623,325	454,100
	2011	1,739,700	916,908	822,792
	2010	826,944	516,556	310,388
Mr. Dosland	2012	46,156	36,298	9,858
	2011	33,368	22,932	10,436
	2010	18,462	16,567	1,895
Mr. Baumgarten	2012	17,393	15,531	1,862
	2011	13,799	12,060	1,739
	2010	0	0	0
Mr. Anderegg	2012	183,448	130,038	53,410
	2011	178,893	89,297	89,596
	2010	91,453	58,477	32,976
Mr. Larson	2012	45,003	41,494	3,509
	2011	0	0	0
Mr. Mayne	2012	15,733	13,880	1,853
	2011	0	0	0

See the "Pension Benefits" and "Nonqualified Deferred Compensation" tables below for further discussion regarding pension and deferred compensation plans. See also Note 10 to the consolidated financial statements for additional information regarding the Company's employee benefit plans.

- (5) The amounts listed under the column entitled “All Other Compensation” in the “Summary Compensation Table” above include: Company contributions to the 401(k) Plan and the ESOP; contributions to the Restoration Plan; with respect to Messrs. Crowley and Baumgarten, an automobile allowance or expenses; and dividends paid on unvested restricted stock, which are listed in the table below:

	Year	Company Matching to 401(k) Plan (\$)	Company ESOP Allocation (\$)	Company Contribution to Benefits Restoration Plan		Automobile Allowance and Related Expenses (\$)	Dividends on Un-Vested Restricted Stock (\$)	Total (\$)
				401(k) (\$)	ESOP (\$)			
Mr. Crowley Jr.	2012	2,450	0	4,510	0	472	500	7,932
	2011	2,450	0	4,510	0	480	0	7,440
	2010	2,450	9,066	4,641	4,510	456	0	21,123
Mr. Dosland	2012	2,913	0	0	0	0	780	3,693
	2011	1,980	0	0	0	0	640	2,620
	2010	1,920	2,633	0	0	0	2,960	7,513
Mr. Baumgarten	2012	3,567	0	0	0	4,800	1,480	9,847
	2011	3,329	0	0	0	4,800	810	8,939
	2010	0	0	0	0	3,400	1,950	5,350
Mr. Anderegg	2012	2,943	0	0	0	0	500	3,493
	2011	2,070	0	0	0	0	0	2,070
	2010	2,023	7,808	0	0	0	0	9,831
Mr. Larson	2012	2,904	0	0	0	0	980	3,884
	2011	231	0	0	0	0	720	951
Mr. Mayne	2012	946	0	0	0	0	900	1,846
	2011	0	0	0	0	0	600	600

- (6) As previously announced, Mr. Crowley Jr. will retire as CEO of the Company and the Bank effective as of July 1, 2013, but will remain as non-executive Chairman of both. Mr. Baumgarten will become CEO of the Company and the Bank, effective upon Mr. Crowley Jr.’s retirement. Mr. Baumgarten became President of the Bank and the Company in 2010; the amounts related to him in the table reflect his compensation since his start date in April 2010.
- (7) Mr. Larson became Senior Vice President - Director of Commercial Banking of the Bank in December 2010 and Mr. Mayne became Senior Vice President - Chief Credit Officer of the Bank in January 2011, respectively. Each of their positions has been considered an executive officer position of the Company since February 2011. The amounts in the table reflect the compensation received in 2011 by Mr. Larson (entire year) and Mr. Mayne (beginning on his January 17, 2011 start date).

\* \* \*

As of December 31, 2012, the Company maintained employment agreements with each of Messrs. Crowley Jr., Dosland, Baumgarten, Anderegg, Larson and Mayne; those employment agreements cover, among other things, the compensation and benefits received by these persons and payments upon termination of employment. For more information regarding those agreements, see “Employment Agreements and Potential Payments upon Termination or Change in Control” below. In addition, equity-based awards are made under the 2004 Stock Plan, and annual cash incentive awards are made under the Management Incentive Plan, which is described under “Grants of Plan-Based Awards” below.

*401(k) Plan.* To provide an additional incentive for employees to save for their retirement, the Company maintains the Bank Mutual Corporation 401(k) Plan. The 401(k) Plan, a tax-qualified defined contribution plan, is

offered to substantially all Company employees. Under the 401(k) Plan, employees may voluntarily contribute additional funds to accounts for their benefit in the plan, and may designate within several specified choices how those funds will be invested. To provide additional incentives for these employees to contribute to their 401(k) accounts, the Company provides matching payments to contributions made by the participating employees. See "Compensation Discussion and Analysis – Elements of Compensation – Retirement and Post-Employment Compensation" above for more information about the Company matching payments under the 401(k) Plan.

*Restoration Plan.* The Company also maintains a Restoration Plan to compensate participants for benefits under the 401(k) Plan that they are unable to receive because of limitations under the Code on contributions and benefits under the plan (the Company also maintained a benefits restoration plan for the ESOP, although all of the shares available under the ESOP have been allocated and no unallocated shares remain). The Code restricts the amount of tax-qualified plan benefits that can be received by plan participants, and also limits salary deferrals that an employee may contribute to the 401(k) Plan.

The Restoration Plan related to the 401(k) Plan permits eligible participants to defer compensation that they are unable to contribute to the 401(k) Plan and receive Company allocations thereunder, in each case because of Code limits. Under the Code, in 2012, only the first \$250,000 of compensation is considered in determining benefits under tax-qualified plans.

The Restoration Plan related to the 401(k) Plan covers officers and key employees who are selected by the board. The annual allocations to employees under the Restoration Plan are not tax deductible by the employer or included in the taxable compensation of the employees receiving the allocations. When benefits are paid to the employees following the termination of employment, the payments, which will require board approval, will be deductible by the employer and included in the taxable compensation of the employees receiving those payments

*Employee Stock Ownership Plan.* The ESOP was a tax-qualified plan that covered substantially all salaried employees with at least one year of service and who had attained age 21. It became effective at the completion of the Company's 2000 restructuring. From 2001 to 2010, the ESOP allocated a certain number of shares released each year among the accounts of participants in accordance with a formula. After giving effect to 2010 service, all of the shares available under the ESOP had been allocated to participants' accounts and no unallocated shares remain.

**Grants of Plan-Based Awards  
2012**

Name	Award Type	Grant Date	Estimated Possible Payouts Under Non-Equity Incentive Plan Awards (1)			All Other Stock Awards: Number of Shares of Stock or Units (#) (2)	All Other Option Awards: Number of Securities Underlying Options (#) (2)	Exercise or Base Price of Option Awards (\$/sh) (2)	Closing Market Price on Grant Date (\$/sh) (2)	Grant Date Fair Value of Stock and Option Awards (\$) (3)
			Threshold (\$)	Target (\$)	Maximum (\$)					
Mr. Crowley Jr.	Management Incentive Plan	12/19/11	97,440	139,200	278,400	—	—	—	—	—
	Options	01/17/12	—	—	—	—	20,000	3.39	3.40	17,200
	Restricted Stock	01/17/12	—	—	—	10,000	—	—	—	34,000
Mr. Dosland	Management Incentive Plan	12/19/11	26,712	38,160	76,320	—	—	—	—	—
	Options	01/17/12	—	—	—	—	20,000	3.39	3.40	17,200
	Restricted Stock	01/17/12	—	—	—	10,000	—	—	—	34,000
Mr. Baumgarten	Management Incentive Plan	12/19/11	73,500	105,000	210,000	—	—	—	—	—
	Options	01/17/12	—	—	—	—	40,000	3.39	3.40	34,400
	Restricted Stock	01/17/12	—	—	—	20,000	—	—	—	68,000
Mr. Anderegg	Management Incentive Plan	12/19/11	26,712	38,160	76,320	—	—	—	—	—
	Options	01/17/12	—	—	—	—	20,000	3.39	3.40	17,200
	Restricted Stock	01/17/12	—	—	—	10,000	—	—	—	34,000
Mr. Larson	Management Incentive Plan	12/19/11	27,090	38,700	77,400	—	—	—	—	—
	Options	01/17/12	—	—	—	—	20,000	3.39	3.40	17,200
	Restricted Stock	01/17/12	—	—	—	10,000	—	—	—	34,000
Mr. Mayne	Management Incentive Plan	12/19/11	25,830	36,900	73,800	—	—	—	—	—
	Options	01/17/12	—	—	—	—	20,000	3.39	3.40	17,200
	Restricted Stock	01/17/12	—	—	—	10,000	—	—	—	34,000

(1) The amounts shown above represent amounts payable pursuant to the Management Incentive Plan. Of these amounts, 50% of the bonus was based on Company quantitative performance metrics (except for Messrs. Crowley Jr. and Baumgarten, whose bonuses are 100% based on those metrics); the named executive officers other than Messrs. Crowley Jr. and Baumgarten were able to earn up to 50% of their bonus based upon achievement of personal goals, but only if the Company's quantitative financial goals were met. In 2012, the Company exceeded the corporate performance targets set forth in the Management

Incentive Plan; as a result, the named executive officers received a bonus in the amounts set forth under the “Non-Equity Incentive Plan Compensation” column in the “Summary Compensation Table” above. See also “Compensation Discussion and Analysis–2012 Annual Compensation Determinations–Cash Bonus/Incentives” for additional information regarding bonuses.

- (2) On January 17, 2012, stock options and shares of restricted stock were awarded to various officers and key employees, including the named executive officers, under the 2004 Stock Plan. The stock options were granted at an exercise price of \$3.39 per share (average of the high and low trading prices on the date of grant). The options and restricted shares vest 20% per year in each of the five years after the January 2012 grant date, or earlier in the event of a change in control of the Company, death or disability.
- (3) For stock awards and options, this amount represents the grant date fair value calculated in accordance with ASC 718. The assumptions used to determine the valuation of the awards are discussed in Note 11 to the consolidated financial statements.

\* \* \*

The non-equity incentive awards in the above table were potential annual cash bonus amounts payable pursuant to the Company’s Management Incentive Plan. Under the Management Incentive Plan, the Compensation Committee sets targets near the beginning of the fiscal year for Company performance and cash bonus payments depend upon the degree to which the Company meets these targets. The actual amount of the bonus pool for all plan participants is determined based upon the Company’s performance as to those financial criteria; however, the actual bonus paid to each individual is determined only after also considering individual performance. In 2012, for each average percentage point by which the Company missed its targets, the potential bonus would have been reduced by 1.5 percentage points. No bonus is paid for performance more than 20% below targets. In 2012, for each average percentage point by which the Company exceeded its targets, the bonus would have been increased by 1 percentage point. No bonus is earned with respect to any criteria if Company performance is below threshold criteria, which is also set at the beginning of the year. In addition, the Management Incentive Plan permits a portion of the cash bonus to be determined based upon individual performance goals (except for Messrs. Crowley Jr. and Baumgarten, whose bonuses are based solely on corporate performance). In total, in 2012, Messrs. Crowley Jr. and Baumgarten were able to earn up to 14% at the threshold, 20% at the target, or 40% at maximum, of his base salary as bonus and Messrs. Dosland, Anderegg, Larson and Mayne up to 12.6%, 18% and 36%, respectively. For further information as to the computation of these awards for fiscal 2012, see “Compensation Discussion and Analysis–2012 Annual Compensation Determinations–Cash Bonus/Incentives” above.

In January 2012, stock options and shares of restricted stock were awarded to various officers and key employees, including certain executive officers, in the amounts shown in the table above, under the 2004 Stock Plan. Under the 2004 Stock Plan, the Compensation Committee may grant awards of stock options and/or restricted stock to officers, directors and other key employees of the Company and its subsidiaries. Options under the 2004 Stock Plan are priced at the average of the high and low trading prices on The Nasdaq Stock Market on the grant date. Grants thereunder vest upon service with the Company, with 20% of the options and/or shares awarded vesting on each of the first five anniversaries of the grant. The 2004 Stock Plan also includes provisions that provide for accelerated vesting in the event of a change in control of the Company, death or disability.

**Outstanding Equity Awards at Fiscal Year-End  
December 31, 2012**

Name	Option Awards (1)				Stock Awards (1)	
	Number of Securities Underlying Unexercised Options (#)		Option Exercise Price (\$)	Option Expiration Date	Number of Shares or Units of Stock That Have Not Vested (#)	Market Value of Shares or Units of Stock That Have Not Vested (\$)(9)
	Exercisable	Unexercisable				
<b>Mr. Crowley Jr.</b>	700,000	0	10.673	5/3/14 (2)		
	3,000	12,000	5.05	1/18/21 (3)		
	0	20,000	3.39	1/17/22 (4)		
					10,000 (4)	43,000
<b>Mr. Dosland</b>	40,000	10,000	12.025	8/18/18 (5)		
	3,000	12,000	5.05	1/18/21 (3)		
	0	20,000	3.39	1/17/22 (4)		
					4,000 (5)	17,200
				10,000 (4)	43,000	
<b>Mr. Baumgarten</b>	20,000	30,000	7.22	5/3/20 (6)		
	10,000	40,000	5.05	1/18/21 (3)		
	0	40,000	3.39	1/17/22 (4)		
					9,000 (6)	38,700
				20,000 (4)	86,000	
<b>Mr. Anderegg</b>	100,000	0	10.673	5/3/14 (2)		
	3,000	12,000	5.05	1/18/21 (3)		
	0	20,000	3.39	1/17/22 (4)		
					10,000 (4)	43,000
<b>Mr. Larson</b>	20,000	30,000	4.74	12/20/20 (7)		
	0	20,000	3.39	1/17/22 (4)		
					7,200 (7)	30,960
					10,000 (4)	43,000
<b>Mr. Mayne</b>	10,000	40,000	5.05	1/18/21 (3)		
	0	20,000	3.39	1/17/22 (4)		
					8,000 (8)	34,400
					10,000 (4)	43,000

- (1) All option awards were granted under the 2004 Stock Plan at an exercise price equal to the market value of Company common stock (using the average of the high and low trading prices) on the date of grant. All stock awards consist of restricted shares granted under the 2004 Stock Plan. All options and restricted shares vest in five annual increments of 20% each beginning on the first anniversary following the grant date.
- (2) Options granted on May 3, 2004. These options are fully vested.
- (3) Options granted on January 18, 2011, which vest in five annual increments of 20% each beginning on the first anniversary following the grant date. At December 31, 2012, 80% of these options remained unvested.

- (4) Options and restricted shares granted on January 17, 2012, which vest in five annual increments of 20% each beginning on the first anniversary following the grant date. At December 31, 2012, 100% of these options and restricted shares remained unvested.
- (5) Options and restricted shares granted on August 18, 2008, which vest in five annual increments of 20% each beginning on the first anniversary following the grant date. At December 31, 2012, 20% of these options and restricted shares remained unvested.
- (6) Options and restricted shares granted on May 3, 2010, which vest in five annual increments of 20% each beginning on the first anniversary following the grant date. At December 31, 2012, 60% of these options and restricted shares remained unvested.
- (7) Options and restricted shares granted on December 20, 2010, which vest in five annual increments of 20% each beginning on the first anniversary following the grant date. At December 31, 2012, 60% of these options and restricted shares remained unvested.
- (8) Restricted shares granted on January 18, 2011, which vest in five annual increments of 20% each beginning on the first anniversary following the award. At December 31, 2012, 80% of these restricted shares remained unvested.
- (9) Based on the \$4.30 per share closing price of a share of Company common stock on December 31, 2012, the last trading day of the year.

**Option Exercises and Stock Vested  
2012**

Name	Option Awards		Stock Awards	
	Number of Shares Acquired on Exercise (#)	Value Realized on Exercise (\$)(1)	Number of Shares Acquired on Vesting #(2)	Value Realized on Vesting (\$)(2)
Mr. Crowley Jr.	0	0	0	0
Mr. Dosland	0	0	4,000	17,520
Mr. Baumgarten	0	0	3,000	11,370
Mr. Anderegg	0	0	0	0
Mr. Larson	0	0	2,400	9,960
Mr. Mayne	0	0	2,000	7,180

- (1) Computed based on the difference between the market price of the underlying securities, computed as the average of the high and low price at exercise, and the option exercise price.
- (2) The number of shares acquired on vesting and the value realized on vesting relates to shares of restricted stock that were granted under the 2004 Stock Plan and that were subject to vesting at the rate of 20% per year in the five years after grant. The shares granted under the 2004 Stock Plan are valued at the average of the high and low trading prices on The Nasdaq Stock Market on the dates of vesting.

## Pension Benefits

The following table provides information on the benefits which are accrued under the Bank Mutual Corporation Pension Plan, the qualified defined benefit pension plan that covers substantially all of Company employees, and the Supplemental Plan, which applies to specified officers including Messrs. Crowley Jr. and Baumgarten.

Name	Plan Name	Number of Years Credited Service (#)	Present Value of Accumulated Benefit (\$)	Payments During Last Fiscal Year (\$)
Mr. Crowley Jr.	Pension Plan	45	2,540,136	0
Mr. Crowley Jr.	Supplemental Plan	45	9,066,722	0
Mr. Dosland	Pension Plan	3	98,256	0
Mr. Baumgarten	Pension Plan	2	7,245	0
Mr. Baumgarten	Supplemental Plan	2	23,947	0
Mr. Anderegg	Pension Plan	19	894,487	0
Mr. Larson	Pension Plan	1	45,003	0
Mr. Mayne	Pension Plan	1	15,733	0

### Pension Plan

The Pension Plan is a qualified defined benefit pension plan which, during 2012, covered all employees of the Company and its subsidiaries who are age 21 or over and who have completed at least one year of service with the Company. As discussed above, the Compensation Committee closed the Pension Plan to employees not eligible to participate as of January 1, 2013, as well as any employees hired after that date. In addition, effective for service performed after March 1, 2013, the Committee reduced certain future benefits formerly provided under the Pension Plan and the Supplemental Plan (discussed below), but did not reduce all future benefits. Pension benefits are based on the participant's average annual compensation (salary and bonus), including annual cash incentive compensation, and years of credited service to the Company and its subsidiaries. Participants vest in the Pension Plan five years after their hire date. However, years of credited service in the Pension Plan begin at the date of participation in the plan, which is one year after their hire date. Benefits are determined in the form of a 10-year certain and life annuity. In the table above, the present value of accumulated benefits under the Pension Plan was calculated assuming a retirement age of 65, or in Mr. Crowley's case, age 70, and a discount rate of 3.70% as of December 31, 2012 and using the RP 2000 mortality table for determining post-retirement mortality. See "Compensation Discussion and Analysis – Elements of Compensation – Retirement and Post-Employment Compensation" above for more information regarding recent changes to the Pension Plan.

### Supplemental Retirement Plan

Designated officers (currently only Messrs. Crowley Jr. and Baumgarten) also participate in the Supplemental Plan, which is a supplemental non-qualified defined benefit pension plan. The Supplemental Plan provides monthly supplemental benefits to participants that will be paid out of a "rabbi trust" established for the Supplemental Plan, or unsecured corporate assets. The amount of the Supplemental Plan benefit is determined as:

- An amount calculated under the Pension Plan without regard to the limitations imposed by the Code on benefit or compensation amounts and without regard to certain limitations on years of service, minus
- The pension benefit accrued under the Pension Plan.

In 2012, under Code limits, the maximum annual benefit payable through the Pension Plan was \$200,000 and the maximum annual compensation which could be taken into account to determine pension benefits was \$250,000. For 2013, those amounts are \$205,000 and \$255,000, respectively. The Code limits the number of years of service which may be taken into account to 40 years.

In the table above, the present value of accumulated benefits under the Supplemental Plan are calculated assuming a retirement age of 70 in the case of Mr. Crowley Jr. and a retirement age of 65 in the case of Mr. Baumgarten, and a discount rate of 3.70% as of December 31, 2012 and using the RP 2000 mortality table for determining post-retirement mortality. To support obligations payable under the Supplemental Plan, the Company maintains assets in a "rabbi trust," the amount of which is based on the actuarial value of future benefits; the Company expenses payments into the rabbi trust when they are made. These amounts will be paid from the Company's funds, including funds of the rabbi trust in the future; they will not be paid out of the assets in the Pension Plan.

### Nonqualified Deferred Compensation

The Company maintains the Restoration Plan which, in part, relates to Code limits on Company contributions made with respect to the 401(k) Plan. (The Company also maintained a restoration plan for the ESOP, although all of the shares available under the ESOP have been allocated and no unallocated shares remain.) The Code limits the salary deferral that an employee may contribute to the 401(k) Plan and also restricts the amount of tax-qualified plan benefits that can be received by plan participants. See the description included following the "Summary Compensation Table" above.

The following table includes information as to the additional contributions under the Restoration Plan related to the 401(k) Plan.

Name	Executive Contributions in Last FY (\$ (1))	Registrant Contributions in Last FY (\$ (2))	Aggregate Earnings in Last FY (\$)	Aggregate Withdrawals/Distributions (\$)	Aggregate Balance at Last FYE (\$ (3))
Mr. Crowley Jr.	22,560	4,510	71,110	0	293,976
Mr. Dosland	0	0	0	0	0
Mr. Baumgarten	0	0	0	0	0
Mr. Anderegg	0	0	3,932	0	23,321
Mr. Larson	0	0	0	0	0
Mr. Mayne	0	0	0	0	0

- (1) These amounts are also included under the "Salary" column of the "Summary Compensation Table" above.
- (2) These amounts are also included under the "All Other Compensation" column of the "Summary Compensation Table" above.
- (3) Of these balances, the following amounts were included in prior years' Summary Compensation Tables: Mr. Crowley Jr. - \$221,671 and Mr. Anderegg - \$7,822. The aggregate balance of the Restoration Plan related to the 401(k) Plan for each individual as of December 31, 2011 was as follows: Mr. Crowley Jr. - \$195,766 and Mr. Anderegg - \$19,389.

## **Employment Agreements and Potential Payments Upon Termination or Change in Control**

*Employment Agreements.* The Bank has employment agreements, which include change in control provisions, with Messrs. Crowley Jr., Dosland, Baumgarten, Anderegg, Larson and Mayne. The employment agreements with Messrs. Crowley Jr. and Baumgarten are more extensive than those of other executives, in recognition of their more extensive responsibilities. The form of employment agreement is the same for Messrs. Dosland, Anderegg, Larson and Mayne. After expiration of the initial terms of the agreements, they may be extended, upon agreement of the executive and by affirmative action of the Bank's board of directors, so that the agreement remains in effect for a one-, two- or three-year period, depending on the executive. Mr. Crowley Jr.'s agreement has a rolling three-year period and Mr. Baumgarten's has a rolling two-year period; the agreements with the other executives have a one-year term. The terms of the agreements for the executive officers were extended as of January 1, 2013 as follows: through December 31, 2015 for Mr. Crowley Jr. (although the agreement will terminate, other than for post-retirement obligations, upon Mr. Crowley's retirement later in 2013); through December 31, 2014 for Mr. Baumgarten; and through December 31, 2013 for the other executives.

Under the employment agreements, each executive is entitled to a base salary which is reviewed annually, but cannot be reduced, by the Bank's board, as well as benefits, perquisites, directors and officers insurance and indemnity, in accordance with the Bank's policies. Each executive is also entitled to incentive compensation based upon the Bank's incentive compensation plan as in effect from time to time and, occasionally, in the board's discretion.

The current 2013 annual base salary amounts for each of the named executive officers under the employment agreements are as follows: Mr. Crowley Jr. – \$696,000; Mr. Dosland – \$220,000; Mr. Baumgarten – \$600,000; Mr. Anderegg – \$220,000; Mr. Larson – \$223,000; and Mr. Mayne – \$217,000. These amounts may be changed in subsequent years, but may not be reduced.

The employment agreements can be terminated: at the election of the executive officer or the Bank at the expiration of the term; upon death, retirement or disability of the executive; at any time for cause (as defined in the agreements); or voluntarily without cause by the executive or the Bank. Each executive officer may also terminate his or her employment agreement under certain circumstances following a change in control. Upon any event of termination or a change in control, each executive will receive his or her earned but unpaid base salary and incentive compensation, as well as compensation for accrued but unused vacation time. In addition, depending on the manner of termination, each executive will receive additional benefits as discussed and quantified in the tables below.

If the Bank terminates Mr. Crowley Jr.'s agreement at the end of the term, he will receive a lump sum payment equal to 100% of his annual base salary at the time of termination. In addition, he will receive insurance benefits (life, medical, dental and optical) and required medical coverage at the Bank's expense for a period of up to 12 months in accordance with the Bank's policies and applicable law, and certain additional Medicare-related coverage. Messrs. Baumgarten, Dosland, Anderegg, Larson and Mayne do not receive any additional payments if terminated at the end of the current term of his agreement.

Upon each executive's death or retirement, the executive or executive's personal representative will receive his or her earned but unpaid base salary and incentive compensation, prorated to the end of the calendar month in which the termination occurred, and compensation for accrued but unused vacation time. The amounts owed in these circumstances will be a lump sum cash payment. Retirement age is set at 55 for Mr. Crowley Jr. and at 65 for the other executives. In Mr. Crowley Jr.'s case, the Bank will also pay for certain Medicare-related coverage. In addition, in the event of death of Mr. Crowley Jr., the Bank will provide certain medical coverage and benefits for his spouse.

Upon disability, each executive's unpaid base salary and incentive compensation will be prorated to the end of the calendar month in which the termination occurred. The executive will also receive an amount equal to 100% of his or her annual base salary at the time of termination, as well as insurance benefits (life, medical, dental and optical) at the Bank's expense for a period of up to 12 months in accordance with the Bank's policies and applicable law. Mr. Crowley Jr. is also entitled to receive further medical coverage required by COBRA at the Bank's expense for an additional 29 months and certain Medicare-related coverage. In addition, upon termination due to disability, Mr. Crowley Jr. will receive benefits comparable to the amount and duration that other executives would receive under the Bank's short- and long-term disability plans as if the maximum benefit limitation and eligibility periods did not apply.

If, during the term, the Bank terminates an executive without cause or the executive officer terminates his or her employment for cause (e.g., the Bank reduces the executive's base compensation or duties or breaches the employment agreement), the executive would be entitled to receive a lump sum payment equal to 100% of his or her base salary at the time of termination through the end of a one-year severance period. In Mr. Crowley Jr.'s case, he would receive such amount for an aggregate of 36 months. In addition, if the Bank terminates an executive officer without cause, the executive will receive insurance benefits (life, medical, dental and optical) at the Bank's expense through the end of the applicable severance period, in accordance with the Bank's policies and applicable law. In Mr. Crowley Jr.'s case, the benefits period is extended for a period of up to 36 months after the date of termination. Mr. Crowley Jr. also receives required medical coverage at the Bank's expense and certain Medicare-related coverage. If the Bank terminates the executive officer without cause, the Bank must also pay each executive officer a lump sum cash payment in an amount equal to the product of: (i) the Bank's annual aggregate contributions for the executive to all qualified retirement plans in the year preceding termination and (ii) the number of years in the applicable severance period (Mr. Crowley Jr. receives three times the Bank's annual aggregate contributions).

Each executive also has the right to terminate his or her employment following a change in control of the Bank if any of the following occur as a result of the change in control: the executive's compensation, benefits, responsibilities or duties are reduced; the executive is transferred more than 50 miles from his current principal office of employment; or the executive is required to travel as part of his or her duties more than in the past. Upon any termination resulting from a change in control, each executive has a right to receive severance payments and termination benefits as if a termination by the Bank without cause had occurred, except that in Mr. Baumgarten's case, the applicable severance period will be two years. In addition, Mr. Crowley Jr. will continue to receive certain benefits in the event of a change in control of the Bank.

Under each employment agreement, the aggregate amount of all severance payments and termination benefits payable to the executive officer, computed on a present value basis, may not exceed an amount which would cause the payments to be characterized as "parachute payments" within the meaning of Section 280G(b)(2) of the Code. That section generally defines parachute payments to include any severance payments and termination benefits which, on a present value basis, equal or exceed three times the person's average annual total compensation over a five-year period immediately preceding the change in control.

If an executive is terminated by the Bank for cause, the executive will receive his or her earned but unpaid base salary and incentive compensation, as well as compensation for accrued but unused vacation time; however, the executive will not be entitled to any compensation or employment benefits for any period after the date of such termination, or the continuation of any benefits, except as may be required by law. "Cause" is defined to include: the executive's personal dishonesty; incompetence; willful misconduct; breach of fiduciary duty involving personal profit; intentional failure to perform stated duties; willful violation of any law, rule or regulation (other than traffic violations or similar offenses) or final cease-and-desist order; or material breach of the employment agreement.

In addition, the employment agreements for the executives other than Mr. Crowley Jr. contain specific conditions under which the Bank's obligations to make payments or provide benefits would be suspended or terminated. If the executive is suspended or temporarily prohibited from participating in the Bank's affairs pursuant to the Federal Deposit Insurance Act ("FDIA"), the Bank's obligations will be suspended, and if the executive is removed or permanently prohibited from participating in the Bank's affairs pursuant to the FDIA, the Bank's obligations will terminate, except that the executive will still be entitled to vested rights. Each agreement may also be terminated by the Bank's regulator if it is determined that the Bank needs assistance or is in an unsafe or unsound condition.

The Bank has entered into a separate agreement with Mr. Crowley Jr., under which he agrees not to compete with the Bank following a termination of employment for a period equal to the greater of one year or the period for which he received post-employment compensation under the agreement, but not to exceed two years. In addition, the employment agreements for the other executive officers include provisions with respect to the use of confidential information and the non-solicitation of the Bank's customers and employees, in each case for a period of two years following termination of employment. If the executive breaches the non-compete, confidentiality and non-solicitation provisions, as applicable, the Bank is entitled to injunctive and equitable relief in addition to other remedies available at law.

*Termination and Change in Control Payments and Benefits.* The following tables set forth the estimated current value of benefits that could be paid to the named executive officers upon various events of termination or a change in control under the individual employment agreements with Messrs. Crowley Jr., Dosland, Baumgarten, Anderegg, Larson and Mayne and/or the terms of the Company's equity compensation plans. These amounts are estimates only and do not necessarily reflect the actual amounts that would be paid to the named executive officers; the actual amounts would be known only at the time that they become eligible for payment and would be payable only if a termination event or change in control were to occur. The tables reflect the amounts that could be payable under the various arrangements if a termination event or change in control had occurred at December 31, 2012. The tables do not include certain payments that are generally otherwise available on a non-discriminatory basis to all salaried employees in 2012 (such as accrued vacation time, if any; amounts, if any, payable pursuant to Company retirement plans; amounts, if any, payable related to third party insurance; and, in certain cases, amounts payable under certain benefits plans).

**Michael T. Crowley, Jr.**

<b>Event</b>	<b>Base Salary (\$ (1))</b>	<b>Incentive Compen- sation (\$ (2))</b>	<b>Early Vesting of Stock Options (\$ (3))</b>	<b>Early Vesting of Restricted Shares (\$ (4))</b>	<b>Other Benefits (\$ (5))</b>	<b>Total (\$)</b>
<b>Termination by Bank at End of Term</b>	696,000	180,960	N/A	N/A	236,105	1,113,065
<b>Retirement (6)</b>	N/A	180,960	N/A	N/A	239,392	420,352
<b>Death</b>	N/A	180,960	25,369	43,000	119,696	369,025
<b>Disability</b>	696,000	180,960	25,369	43,000	587,392 (7)	1,532,721
<b>Termination by Executive For Cause or by Bank Without Cause</b>	2,088,000	542,880	N/A	N/A	238,297	2,869,177
<b>Termination by Executive Due to Change in Control</b>	2,088,000	542,880	25,369	43,000	239,737	2,938,986

**Other Named Executive Officers**

<b>Event / Name of Executive Officer</b>	<b>Base Salary (\$ (1))</b>	<b>Incentive Compensation (\$ (2))</b>	<b>Early Vesting of Stock Options (\$ (3))</b>	<b>Early Vesting of Restricted Shares (\$ (4))</b>	<b>Other Benefits (\$ (5))</b>	<b>Total (\$)</b>
<b>Retirement (6)</b>						
Mr. Dosland	N/A	48,760	N/A	N/A	N/A	48,760
Mr. Baumgarten	N/A	136,500	N/A	N/A	N/A	136,500
Mr. Anderegg	N/A	48,760	N/A	N/A	N/A	48,760
Mr. Larson	N/A	49,450	N/A	N/A	N/A	49,450
Mr. Mayne	N/A	47,150	N/A	N/A	N/A	47,150
<b>Death</b>						
Mr. Dosland	N/A	48,760	25,369	60,200	N/A	134,329
Mr. Baumgarten	N/A	136,500	50,737	124,700	N/A	311,937
Mr. Anderegg	N/A	48,760	25,369	43,000	N/A	117,129
Mr. Larson	N/A	49,450	25,369	73,960	N/A	148,779
Mr. Mayne	N/A	47,150	25,369	77,400	N/A	149,919
<b>Disability</b>						
Mr. Dosland	212,000	48,760	25,369	60,200	N/A	346,329
Mr. Baumgarten	525,000	136,500	50,737	124,700	N/A	836,937
Mr. Anderegg	212,000	48,760	25,369	43,000	N/A	329,129
Mr. Larson	215,000	49,450	25,369	73,960	N/A	363,779
Mr. Mayne	205,000	47,150	25,369	77,400	N/A	354,919
<b>Termination by Executive For Cause or by Bank Without Cause</b>						
Mr. Dosland	212,000	48,760	N/A	N/A	38,665	299,425
Mr. Baumgarten	525,000	136,500	N/A	N/A	87,368	748,868
Mr. Anderegg	212,000	48,760	N/A	N/A	66,290	327,050
Mr. Larson	215,000	49,450	N/A	N/A	43,581	308,031
Mr. Mayne	205,000	47,150	N/A	N/A	17,013	269,163
<b>Termination by Executive Due to Change in Control</b>						
Mr. Dosland	212,000	48,760	25,369	60,200	38,665	384,994(8)
Mr. Baumgarten	1,050,000	273,000	50,737	124,700	87,368	1,585,805 (8)
Mr. Anderegg	212,000	48,760	25,369	43,000	66,290	395,419 (8)
Mr. Larson	215,000	49,450	25,369	73,960	43,581	407,360 (8)
Mr. Mayne	205,000	47,150	25,369	77,400	17,013	371,932 (8)

In the tables, "N/A" indicates that the type of payment specified is not applicable to the particular event.

- (1) For officers other than Messrs. Crowley Jr. and Baumgarten, this amount represents the executive's base salary in the year of the applicable termination event. In Mr. Crowley Jr.'s case, in the event of (i) termination by Mr. Crowley Jr. for cause, (ii) termination by the Bank without cause and (iii) termination by Mr. Crowley Jr. due to a change in control, this amount represents base salary for the remaining term of the agreement and up to one year post-term, with a 36-month maximum. In Mr. Baumgarten's case, in the event of termination by Mr. Baumgarten due to a change in control, this amount represents base salary for two years. Amounts payable to Messrs. Crowley Jr. and Baumgarten do not include compensation earned for service as a director of the Company or the Bank.
- (2) These amounts are based on the amount the executive actually received as a cash bonus under the formula set forth in the Management Incentive Plan for 2012. See "Compensation Discussion and Analysis—2012 Annual Compensation Determinations—Cash Bonus/Incentives" and the "Summary Compensation Table" above. Under the Management Incentive Plan, in the event of retirement, death or permanent disability during a plan year, incentive awards are paid at the end of the year on a pro-rata basis.
- (3) All outstanding unvested stock options would become vested (i) pursuant to each executive's employment agreement and the stock plans, upon a change in control and (ii) pursuant to the stock plans, upon death or disability of the executive. The amount shown represents the value of the options based on a closing stock price on December 31, 2012, the last trading day of the year, of \$4.30 per share. Unvested stock options held by executive officers as of December 31, 2012 with an exercise price greater than \$4.30 per share have no unrealized value at December 31, 2012 and, therefore, do not affect the values in the table.
- (4) All outstanding unvested shares of restricted stock would become vested, pursuant to the stock plans, upon a change in control or upon death or disability of the executive. This amount represents the value of the unvested restricted share awards held by the executive based on a closing stock price on December 31, 2012, the last trading day of the year, of \$4.30 per share.
- (5) These amounts include payments of premiums for employer-paid life insurance and employer-paid medical and dental benefits; however, they do not include payments, if any, to the extent that they are generally available on a non-discriminatory basis to all salaried employees. Further, in the case of termination of the executive by the Bank without cause or a change in control, these amounts also include the lump sum cash payment equal to the Bank's annual aggregate contributions for the executive to qualified benefit plans for the remaining employment term or severance period, as set forth in the executive's employment agreement. In the case of Mr. Crowley Jr., he is generally entitled to certain health and/or Medicare-related coverage. Further, in the event of a change in control, Mr. Crowley Jr.'s amounts also include certain additional benefits such as use of a company automobile and club membership dues. Certain of these benefits would not be payable if the executive accepts other employment.
- (6) In the event of retirement, except under the Management Incentive Plan, the executive officers other than Mr. Crowley Jr. do not receive any payments or benefits that are not otherwise generally available on a non-discriminatory basis to all salaried employees; provided however, that the executives would have been entitled to receive the bonuses earned in 2012 even if they had been terminated as of December 31, 2012. In the case of Messrs. Crowley Jr. and Baumgarten, each is entitled to receive retirement payments or benefits, which are not available to other employees, pursuant to the Supplemental Plan; however, Mr. Baumgarten was not vested in Supplemental Plan, therefore, the amounts for him do not include any such payments or benefits. The present value of accumulated benefits under the Supplemental Plan is \$9,066,722 and \$23,947 for Mr. Crowley Jr. and Mr. Baumgarten, respectively. See the "Pension Benefits" table above. He also is entitled to the payment of certain health insurance benefits, which are included in the table.
- (7) This amount includes a short-term disability payment to the executive for six months and assumes that, after that six-month period, the executive would elect to begin receiving retirement payments instead.
- (8) Per the employment agreements, the total amount payable is limited to 2.99 times the executive officer's Base Amount (defined as the average annual total compensation over a five-year period immediately preceding the change in beneficial ownership or control of the Bank) so as to prevent the payment from being classified as a parachute payment within the meaning of Section 280G(b)(2) of the Code. Therefore, the actual amounts payable to an executive might be less than the amount indicated in these tables.

In the event any of these persons otherwise voluntarily terminates or is terminated for cause, they would receive any accrued salary and vacation pay through the time of termination, on the same basis as is paid to other salaried employees.

## **RISK MANAGEMENT AND COMPENSATION**

In addition to relying on conservative operating principles generally, the Company designs and evaluates its compensation policies for executive officers and all other employees so as to not create incentives to take undue risks to the institution. In the case of executive officers and other senior personnel, historically most direct compensation has been in the form of salary and in equity awards which vest over a five-year time horizon. When establishing cash bonuses for executives, the Compensation Committee establishes incentives and goals that are consistent with corporate goals and that are reasonably achievable given maximum effort, but that do not encourage unnecessary risk taking; further, the cash bonuses that are determined over a relatively short-term performance horizon at target only represent up to 10%, 15% or 18% depending on position (20% in the case of the Chairman and CEO and the President) of annual salary, a relatively small portion of total compensation, or twice those amounts at the maximum achievement. Even for employees below these compensation levels, the Company's business underwriting standards and related policies, including management supervision and approval processes, minimize the risk that personnel who are compensated for making loans, managing investments or other more discrete functions are able to take excessive risks motivated by their compensation effect.

As a result and on this basis, the Company believes that the risks, if any, arising from its compensation policies and practices for its employees are not reasonably likely to have a material adverse effect on the Company.

## **ADVISORY VOTE ON EXECUTIVE COMPENSATION**

Under provisions adopted as part of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 and the provisions of the Section 14A of the Exchange Act adopted as a part thereof, publicly-traded companies such as the Company are required to hold an advisory vote of their shareholders at least once every three years to approve the compensation of named executive officers. The compensation is to be approved pursuant to the following resolution: "RESOLVED, that the compensation paid to the Company's named executive officers, as disclosed pursuant to Item 402 of Regulation S-K, including the Compensation Discussion and Analysis, compensation tables and narrative discussion, is hereby approved." The Company discloses that information under the headings "Compensation Discussion and Analysis" and "Executive Compensation" herein. The Company currently holds such votes annually. At last year's annual meeting, the Company's shareholders approved the compensation paid to the named executive officers.

As described in "Compensation Discussion and Analysis" above, the Company designs its executive compensation programs with an intent to use compensation to attract and retain talented and highly-experienced personnel and to provide incentives for that personnel to maximize corporate performance. The Compensation Committee particularly focuses on obtaining and retaining the services of highly-experienced personnel, especially those with a long-term commitment to the Company. A portion of the Company's executive officers' compensation is at risk, reflecting the Company's emphasis on pay that reflects performance and drives long-term shareholder value. While the Company recognizes equity ownership by executives and has made equity awards, it believes its awards have been relatively modest in amount. The Company believes its compensation program as a whole is well-suited to promote the Company's objectives in both the short-and long-term.

As an advisory vote, this proposal is not binding on the Company. However, the Compensation Committee, which is responsible for designing and administering the Company's executive compensation programs, values the opinions expressed by shareholders, and will consider the outcome of the vote when making future compensation decisions regarding the Company's executive compensation programs.

**The board unanimously recommends that shareholders vote FOR approval of the compensation of the Company's executive officers as described in this proxy statement.**

## CERTAIN TRANSACTIONS AND RELATIONSHIPS WITH THE COMPANY

### General Principles

Bank Mutual Corporation has a policy that transactions, if any, between the Company, on the one hand, and its executive officers or directors (or related party), on the other hand, must be on a basis that is fair and reasonable to the Company, and in accordance with Bank Mutual Corporation's code of ethics, banking laws and regulations and other policies. Lending transactions between the Bank and such a person that are on the same terms and conditions as applied to others must be approved in advance by the board of directors or the executive committee of the Bank and also must be brought to the attention of the Company's board of directors; depository transactions on the same terms and conditions as other customers do not need approval. Any other transactions with the Company's directors or executive officers, or their related parties, must be approved by either a disinterested majority of the Company's board of directors or by its Audit Committee.

### Banking Relationships

The Bank has had, and expects to continue to have, regular business dealings with its officers and directors, as well as their associates and the firms that they serve. The Company follows applicable banking laws and regulations with respect to those relationships. The Bank's historical policy has been that transactions, including loans, deposits and other securities, with its or the Company's directors and executive officers be on terms that are no more favorable to the director or executive officer than the Bank would provide to unaffiliated third parties; however, the Bank maintains certain limited preferential loan programs for the benefit of other Bank non-executive officers and employees. Directors and executive officers, and their associates, regularly deposit funds with the Bank; the deposits are made on the same terms and conditions which are offered to other depositors.

Certain directors and executive officers are, or in 2012 were, indebted to the Bank for loans made in the ordinary course of business. Those loans were made in the ordinary course of business and have been on substantially the same terms, including interest rates and collateral, as those then prevailing for comparable transactions with other persons. These loans do not involve more than the normal risk of collectability or present other unfavorable or preferential features. During 2012, Mr. Carter and a trust established for Mr. Buestrin's daughter each had an outstanding ordinary course, non-preferential residential mortgage loan from the Bank. During 2012, Mr. Lopina repaid in full an ordinary course, non-preferential commercial business loan from the Bank. In January 2012, Mr. Dosland repaid in full an ordinary course, non-preferential mortgage loan and an ordinary course, non-preferential home equity line of credit that he previously had from the Bank. In addition, all of the directors and executive officers had deposit accounts with the Bank; these accounts are on the same terms and conditions that are offered to the Bank's other customers. The board has considered these relationships when determining which directors are "independent" and has concluded that they do not affect independence.

### Family Relationships

Michael T. Crowley III, the adult son of Mr. Crowley Jr., is the Vice President-Bank Office Administration for the Southeast Region of the Bank. In 2012, his annual base salary was \$95,200, and he earned a bonus of \$17,136 and was granted options to purchase 7,500 shares; he was also granted options to purchase 5,000 shares in 2013. Mr. Crowley III participates in other Bank benefit plans on the same basis as other salaried employees of the Bank, and does not have an employment agreement with the Company or the Bank.

Michael T. Crowley Sr., the father of Mr. Crowley Jr., was a director of Bank Mutual Corporation until 2004. In addition, he was a director and executive officer of the Bank until his retirement in 2005. The Company makes various post-retirement payments to Mr. Crowley Sr. as described below.

*Deferred Compensation Agreement.* The Bank maintained a deferred compensation arrangement with Mr. Crowley Sr. for over 25 years under which it agreed to defer part of Mr. Crowley Sr.'s compensation in exchange for compensation payments at a later date. The precise provisions were modified from time to time, most recently in 1998. To fund this obligation, the Bank purchased a life insurance policy on Mr. Crowley Sr. The policy is fully paid, and the Bank believes the arrangement is fully funded.

Upon Mr. Crowley Sr.'s retirement in May 2005, he began to receive a monthly payment of \$10,607, to be received through May 2015. The monthly installments are equal to the amount that would be payable to the Bank under the life insurance policy if the Bank exercised a settlement option under the policy equal to a 10-year payment period. If Mr. Crowley Sr. dies before May 2015, the amounts otherwise payable to him will be paid to a beneficiary or beneficiaries named by him or to his estate. Under his employment agreement as in effect when he retired, Mr. Crowley Sr. also receives continuing medical insurance benefits in retirement, valued at \$7,679 in 2012.

*Defined Benefit Retirement Plans.* As a consequence of his retirement, Mr. Crowley Sr. participates in the Company's qualified defined benefit pension plan and the Supplemental Plan, both as described in "Executive Compensation" above. Under the qualified plan, Mr. Crowley Sr. had more than 70 years of service with the Bank prior to his retirement, and received \$105,963 in 2012, in accordance with the plan, reflecting Code limits. In addition, as a consequence of the legal limits described above, Mr. Crowley Sr. also received approximately \$297,288 in 2012, under the supplemental non-qualified plan; these amounts are paid out of a rabbi trust maintained by the Company.

## REPORT OF THE AUDIT COMMITTEE

The functions of the Audit Committee of the Bank Mutual Corporation board of directors include meeting with the Company's independent registered public accounting firm and making recommendations to the board regarding our independent registered public accounting firm; assessing the adequacy of internal controls over financial reporting, accounting methods and procedures; reviewing public disclosures required for compliance with securities laws; and considering and reviewing various other matters relating to the Company's financial accounting and reporting. No member of the Audit Committee is employed by or has any other material relationship with the Company. The members of the Audit Committee are "independent" as defined in Rule 5605(a)(2) of the The Nasdaq Marketplace Rules, applicable to companies listed on The Nasdaq Stock Market. The board of directors has adopted a written charter for the Audit Committee and reviews and reaffirms that charter annually. A copy of the charter is available on the Company's website.

In connection with its function to oversee and monitor the financial reporting process of the Company, the Audit Committee has done the following:

- reviewed and discussed the audited financial statements for the fiscal year ended December 31, 2012 with Bank Mutual Corporation management;
- discussed with Deloitte & Touche LLP, the Company's independent registered public accounting firm for 2012, those matters that are required to be discussed by the Statement of Auditing Standards No. 61, as amended (AICPA, Professional Standards, Vol. 1, AU section 380), and SEC Regulation S-X, Rule 2-07 "Communication with Audit Committees"; and
- received the written disclosures and the letter from Deloitte & Touche LLP required by applicable requirements of the Public Company Accounting Oversight Board regarding Deloitte & Touche LLP's communications with the audit committee concerning independence, and has discussed with Deloitte & Touche LLP its independence.

Based on the foregoing, the Audit Committee recommended to the board that those audited financial statements be included in the Company's annual report on Form 10-K for the year ended December 31, 2012.

In addition, the Audit Committee also considered the fees paid to Deloitte & Touche LLP for services provided by Deloitte & Touche LLP during 2012. See "Independent Registered Public Accounting Firm" below. The Committee believes that the provision of the non-audit services is compatible with maintaining Deloitte & Touche LLP's independence.

Members of the Audit Committee:

Richard A. Brown, Chairman  
Thomas H. Buestrin  
William J. Mielke  
Robert B. Olson

## INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The firm of Deloitte & Touche LLP audited the Company's financial statements for the years ended December 31, 2012 and 2011. The Audit Committee has decided, subject to shareholder ratification, to appoint Deloitte & Touche LLP, certified public accountants, as the independent registered public accounting firm to audit the Company's financial statements for the year ending December 31, 2013.

Although not required by law to submit the appointment to a vote by shareholders, the Audit Committee and the board believe it appropriate, as a matter of policy, to request that the shareholders ratify the appointment of Deloitte & Touche LLP as the independent registered public accounting firm for 2013. If the shareholders should not so ratify, the Audit Committee will reconsider the appointment.

Representatives of Deloitte & Touche LLP are expected to be present at the 2013 annual meeting to respond to appropriate questions and to make a statement if they so desire.

### **Fees Paid to Independent Registered Public Accounting Firm**

Fees (including reimbursements for out-of-pocket expenses) paid to Deloitte & Touche LLP for services relating to 2012 and 2011 were as follows:

	<b>2012</b>	<b>2011</b>
Audit fees:	\$509,500	\$540,614
Audit-related fees:	0	0
Tax fees:	54,900	57,200
All other fees:	0	0

Tax services consisted of tax compliance and advice, including tax return assistance and consulting services related to tax accounting method changes. The Audit Committee considered the compatibility of non-audit services by Deloitte & Touche LLP with the maintenance of that firm's independence.

### **Audit Committee Pre-Approval Policy**

The Audit Committee generally approves all engagements of the independent registered public accounting firm in advance, including approval of the related fees. The Audit Committee approves individual projects and the approved levels of fees for each. Management must have such projects approved by the Audit Committee. Projects of the types approved in general by the Audit Committee for which fees total less than \$10,000 in each case may be approved by management with the concurrence of the chairman of the Audit Committee, subject to review and approval by the Audit Committee at its next meeting. There were no services or fees in 2012 or 2011 that were not approved in advance by the Audit Committee or its chairman under this policy.

## SHAREHOLDER PROPOSALS AND NOTICES

Shareholder proposals must be received by the corporate secretary of Bank Mutual Corporation no later than November 11, 2013 in order to be considered for inclusion in next year's annual meeting proxy materials pursuant to the SEC's Rule 14a-8 under the Securities Exchange Act.

Under SEC rules relating to the discretionary voting of proxies at shareholder meetings, if a proponent of a matter for shareholder consideration (other than a shareholder proposal under Rule 14a-8 described above) fails to appropriately notify Bank Mutual Corporation of the matter at least 45 days prior to the month and day of mailing the prior year's proxy statement, then management proxies are allowed to use their discretionary voting authority with respect to such a matter if it is raised at the annual meeting, without any discussion of the matter in the proxy statement. Therefore, for inclusion, any such matters must be received by the Company by no later than January 25, 2014 in the case of the 2014 annual meeting of shareholders. If such a notice is not received, the persons voting the proxies may use their discretion on any such matter. The Company is not aware of any such proposals for the 2013 annual meeting.

In addition, as a separate requirement, the Company's bylaws also require that any nomination of a director or submission of a matter for consideration of the meeting must be presented, with specified accompanying information, to Bank Mutual Corporation's corporate secretary at least 70, but not more than 100, days before the scheduled date for the next annual meeting of shareholders. No such submissions under the bylaws have been received by the Company for the 2013 annual meeting. Assuming that the 2014 annual meeting is held as scheduled on May 5, 2014, the period in which materials must be received is between January 25, 2014 and February 24, 2014 for the 2014 annual meeting in order to be considered.

By Order of the Board of Directors

James P. Carter  
Vice President and Secretary

Milwaukee, Wisconsin  
March 8, 2013

A copy, without exhibits, of Bank Mutual Corporation's Annual Report on Form 10-K filed with the SEC for the year ended December 31, 2012 is attached to this proxy statement. The Company will provide an additional copy of the 10-K, without exhibits, without charge to any record or beneficial owner of Company common stock upon the written request of that person directed to: James P. Carter, Vice President and Secretary, Bank Mutual Corporation, 4949 West Brown Deer Road, Milwaukee, Wisconsin 53223. The 10-K provides a list of exhibits, which will be provided for a reasonable fee to reflect duplication and mailing costs; exhibits are also available through the SEC's website at [www.sec.gov](http://www.sec.gov).

**Multiple Shareholders Sharing the Same Address.** In some cases, there are multiple shareholders of record at a single address. The Company is sending a single annual report and proxy statement to that address unless the Company received instructions to the contrary. Each shareholder of record, however, will continue to receive a separate proxy card. This practice, known as "householding," is designed to reduce printing and postage costs. If you wish to receive separate copies of the annual report and proxy statement now or in the future, or to discontinue householding entirely, you may call the Company's transfer agent, Registrar and Transfer Company, at (800) 368-5948, contact it by e-mail at [info@rtco.com](mailto:info@rtco.com), or provide written instructions to Registrar and Transfer Company, 10 Commerce Drive, Cranford, New Jersey 07016-3572.

If you receive multiple copies of the annual report and proxy statement, you also may contact the transfer agent at the telephone number or address above to request householding. If your shares are held in street name through a bank, broker or other holder of record, you may request householding by contacting that bank, broker or other holder of record.

SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
FORM 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
For the fiscal year ended December 31, 2012

Commission file number: 000-31207

**BANK MUTUAL CORPORATION**  
(Exact name of registrant as specified in its charter)

Wisconsin  
(State or other jurisdiction of incorporation or organization)

39-2004336  
(I.R.S. Employer Identification No.)

4949 West Brown Deer Road, Milwaukee, Wisconsin  
(Address of principal executive offices)

53223  
(Zip Code)

Registrant's telephone number, including area code: (414) 354-1500

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

Common Stock, \$0.01 Par Value  
(Title of each class)

The NASDAQ Stock Market LLC  
(Name of each exchange on which registered)

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

NONE

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

Yes \_\_\_\_\_ No X

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the 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 has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files.)

Yes X No \_\_\_\_\_

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

Large accelerated filer \_\_\_\_\_ Accelerated filer X Non-accelerated filer \_\_\_\_\_ Smaller reporting company \_\_\_\_\_

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

Yes \_\_\_\_\_ No X

As of February 28, 2013, 46,420,084 shares of Common Stock were validly issued and outstanding. The aggregate market value of the Common Stock (based upon the \$4.41 last sale price on The NASDAQ Global Select Market on June 29, 2012, the last trading date of the Company's second fiscal quarter) held by non-affiliates (excluding outstanding shares reported as beneficially owned by directors and executive officers; does not constitute an admission as to affiliate status) was approximately \$189.9 million.

Documents Incorporated by Reference

Part of Form 10-K Into Which  
Portions of Document are Incorporated

Proxy Statement for Annual Meeting of Shareholders on May 6, 2013

Part III

**BANK MUTUAL CORPORATION**  
**FORM 10-K ANNUAL REPORT TO**  
**THE SECURITIES AND EXCHANGE COMMISSION**  
**FOR THE YEAR ENDED DECEMBER 31, 2012**

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## Part I

### Cautionary Statement

This report contains or incorporates by reference various forward-looking statements concerning the Company's prospects that are based on the current expectations and beliefs of management. Forward-looking statements may contain, and are intended to be identified by, words such as "anticipate," "believe," "estimate," "expect," "objective," "projection," "intend," and similar expressions; the use of verbs in the future tense and discussions of periods after the date on which this report is issued are also forward-looking statements. The statements contained herein and such future statements involve or may involve certain assumptions, risks, and uncertainties, many of which are beyond the Company's control, that could cause the Company's actual results and performance to differ materially from what is stated or expected. In addition to the assumptions and other factors referenced specifically in connection with such statements, the following factors could impact the business and financial prospects of the Company: general economic conditions, including volatility in credit, lending, and financial markets; declines in the real estate market, which could further affect both collateral values and loan activity; continuing relatively high unemployment and other factors which could affect borrowers' ability to repay their loans; negative developments affecting particular borrowers, which could further adversely impact loan repayments and collection; legislative and regulatory initiatives and changes, including action taken, or that may be taken, in response to difficulties in financial markets and/or which could negatively affect the right of creditors; monetary and fiscal policies of the federal government; the effects of further regulation and consolidation within the financial services industry, including substantial changes under the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"); regulators' increasing expectations for financial institutions' capital levels and restrictions imposed on institutions, as to payments of dividends or otherwise, to maintain or achieve those levels, including the possible effects of potential new regulatory capital requirements under Basel III; pending and/or potential rulemaking or other actions by the Consumer Financial Protection Bureau ("CFPB"); potential regulatory or other actions affecting the Company or the Bank; potential changes in the Federal National Mortgage Association ("Fannie Mae") and the Federal Home Loan Mortgage Corporation ("Freddie Mac"), which could impact the home mortgage market; increased competition and/or disintermediation within the financial services industry; changes in tax rates, deductions and/or policies; potential further changes in Federal Deposit Insurance Corporation ("FDIC") premiums and other governmental assessments; changes in deposit flows; changes in the cost of funds; fluctuations in general market rates of interest and/or yields or rates on competing loans, investments, and sources of funds; demand for loan or deposit products; illiquidity of financial markets and other negative developments affecting particular investment and mortgage-related securities, which could adversely impact the fair value of and/or cash flows from such securities; changes in customers' demand for other financial services; the Company's potential inability to carry out business plans or strategies; changes in accounting policies or guidelines; natural disasters, acts of terrorism, or developments in the war on terrorism; the risk of failures in computer or other technology systems or data maintenance, or breaches of security relating to such systems; and the factors discussed in "Item 1A. Risk Factors," as well as Part II, "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations."

### Item 1. Business

The discussion in this section should be read in conjunction with "Item 1A. Risk Factors," "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations," "Item 7A. Quantitative and Qualitative Disclosures about Market Risk," and "Item 8. Financial Statements and Supplementary Data."

#### General

Bank Mutual Corporation (the "Company") is a Wisconsin corporation headquartered in Milwaukee, Wisconsin. The Company owns 100% of the common stock of Bank Mutual (the "Bank") and currently engages in no substantial activities other than its ownership of such stock. Consequently, the Company's net income and cash flows are derived primarily from the Bank's operations and capital distributions. The Company is regulated as a savings and loan holding company by the Board of Governors of the Federal Reserve ("FRB"). The Company's common stock trades on The NASDAQ Global Select Market under the symbol BKMU.

The Bank was founded in 1892 and is a federally-chartered savings bank headquartered in Milwaukee, Wisconsin. It is regulated by the Office of the Comptroller of the Currency ("OCC") and its deposits are insured within limits established by the FDIC. The Bank's primary business is community banking, which includes attracting deposits from and making loans to the general public and private businesses, as well as governmental and non-profit entities. In addition to

deposits, the Bank obtains funds through borrowings from the Federal Home Loan Bank (“FHLB”) of Chicago. These funding sources are principally used to originate loans, including one- to four-family residential loans, multi-family residential loans, commercial real estate loans, commercial business loans and lines of credit, and consumer loans and lines of credit. From time-to-time the Bank also purchases and/or participates in loans from third-party financial institutions and is an active seller of residential loans in the secondary market. It also invests in mortgage-related and other investment securities.

The Company’s principal executive office is located at 4949 Brown Deer Road, Milwaukee, Wisconsin, 53223, and its telephone number at that location is (414) 354-1500. The Company’s website is [www.bankmutualcorp.com](http://www.bankmutualcorp.com). The Company will make available through that website, free of charge, its Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, and amendments to those reports, as soon as reasonably practical after the Company files those reports with, or furnishes them to, the Securities and Exchange Commission (“SEC”). Also available on the Company’s website are various documents relating to the corporate governance of the Company, including its Code of Ethics and its Code of Conduct.

### **Market Area**

At December 31, 2012, the Company had 75 banking offices in Wisconsin and one in Minnesota. At June 30, 2012, the Company had a 1.50% market share of all deposits held by FDIC-insured institutions in Wisconsin. The Company is the fourth largest financial institution headquartered in Wisconsin, based on deposit market share.

The largest concentration of the Company’s offices is in southeastern Wisconsin, consisting of the Milwaukee Metropolitan Statistical Area (“MSA”), the Racine MSA, and the Kenosha, Wisconsin, and Lake County, Illinois MSA. The Company has 26 offices in these MSAs. The Company has also five offices in south central Wisconsin, consisting of the Madison MSA and the Janesville/Beloit MSA, as well as six other offices in communities in east central Wisconsin.

The Company also operates 20 banking offices in northeastern Wisconsin, including the Green Bay MSA. A few of the offices in this region are located near the Michigan border. Therefore, the Company also draws customers from the upper peninsula of Michigan. Finally, the Company has 18 offices in northwestern Wisconsin, including the Eau Claire MSA, and one office in Woodbury, Minnesota, which is located near the Wisconsin state border on the eastern edge of the Minneapolis-St. Paul MSA.

The services provided through the Company's banking offices are supplemented by services offered through a customer service call center, 24-hour phone banking, internet banking services, and ATMs located in the Company’s market areas.

### **Competition**

The Company faces significant competition in attracting deposits, making loans, and selling other financial products and services. Wisconsin has many banks, savings banks, savings and loan associations, and tax-exempt credit unions, which offer the same types of banking products and services as the Company. The Company also faces competition from other types of financial service companies, such as mortgage brokerage firms, finance companies, insurance companies, investment brokerage firms, and mutual funds. As a result of electronic commerce, the Company also competes with financial service providers outside of Wisconsin.

Many of the Company’s competitors have greater resources and/or offer services that the Company currently does not provide. For example, the Company does not offer trust services. However, the Company does offer mutual fund investments, tax-deferred annuities, credit life and disability insurance, property and casualty insurance, and brokerage services through a subsidiary, BancMutual Financial & Insurance Services, Inc.

### **Lending Activities**

**General** At December 31, 2012, the Company’s total loans receivable was \$1.4 billion or 58.0% of total assets. The Company’s loan portfolio consists primarily of mortgage loans, which includes loans secured by one- to four-family residences, multi-family properties, and commercial real estate properties, as well as construction and development loans secured by the same types of properties and land. To a lesser degree, the loan portfolio includes consumer loans consisting principally of home equity lines of credit, fixed and adjustable-rate home equity loans, student loans, and automobile loans. Finally, the Company’s loan portfolio also contains commercial business loans, to which it has

given increased emphasis in recent years. The nature, type, and terms of loans originated or purchased by the Company are subject to federal and state laws and regulations. The Company has no significant concentrations of loans to particular borrowers or to borrowers engaged in similar activities. In addition, the Company limits its lending activities primarily to borrowers and related loan collateral located in its market areas, which consist of Wisconsin and contiguous regions of Illinois, Minnesota, and northern Michigan, as previously described. For specific information related to the Company's loans receivable for the periods covered by this report, refer to "Financial Condition—Loans Receivable" in "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations."

**Residential Mortgage Lending** The Company originates and purchases first mortgage loans secured by one- to four-family properties. At December 31, 2012, the Company's portfolio of these types of loans was \$465.2 million or 31.0% of its gross loans receivable. Most of these loans are owner-occupied; however, the Company also originates first mortgage loans secured by second homes, seasonal homes, and investment properties.

The Company originates primarily conventional fixed-rate residential mortgage loans and adjustable-rate residential mortgage ("ARM") loans with maturity dates up to 30 years. Such loans generally are underwritten to Fannie Mae standards. In general, ARM loans are retained by the Company in its loan portfolio. Conventional fixed-rate residential mortgage loans are generally sold in the secondary market without recourse, although the Company typically retains the servicing rights to such loans. From time-to-time, the Company may elect to retain in its loan portfolio conventional fixed-rate loans with maturities of up to 15 years. The Company also originates "jumbo" single family mortgage loans in excess of the Fannie Mae maximum loan amount, which was \$417,000 for single family homes in its primary market areas in 2012. Fannie Mae has higher limits for two-, three- and four-family homes. The Company generally retains fixed-rate jumbo single family mortgage loans in its portfolio.

From time-to-time the Company also originates fixed-rate and ARM loans under special programs for low- to moderate-income households and first-time home buyers. These programs are offered to help meet the credit needs of the communities the Company serves and are retained by the Company in its loan portfolio. Among the features of these programs are lower down payments, no mortgage insurance, and generally less restrictive requirements for qualification compared to the Company's conventional one- to four-family mortgage loans. These loans generally have maturities up to 30 years.

From time-to-time the Company also originates loans under programs administered by various federal and state government agencies such as the State Veteran's Administration ("State VA"), the Wisconsin Housing and Economic Development Authority ("WHEDA"), the U.S. Department of Agriculture ("USDA") Guaranteed Rural Housing Program, and the Federal Housing Administration ("FHA"). Loans originated under these programs may or may not be held by the Company in its loan portfolio and the Company may or may not retain the servicing rights for such loans.

ARM loans pose credit risks different from the risks inherent in fixed-rate loans, primarily because as interest rates rise, the underlying payments from the borrowers increase, which increases the potential for payment default. At the same time, the marketability and/or value of the underlying property may be adversely affected by higher interest rates. ARM loans generally have an initial fixed-rate term of one to seven years. Thereafter, they are adjusted on an annual basis up to a maximum of 200 basis points per year. The Company originates ARM loans with lifetime caps set at 6% above the origination rate. Monthly payments of principal and interest are adjusted when the interest rate adjusts. The Company does not offer ARM loans with negative amortization or with interest-only payment features. The Company currently utilizes the monthly average yield on United States treasury securities, adjusted to a constant maturity of one year ("constant maturity treasury index") as the base index to determine the interest rate payable upon the adjustment date of ARM loans. Some of the ARM loans are granted with conversion options that provide for terms of up to seven years in which the borrower may convert the ARM loan to a fixed-rate mortgage loan. The terms at which the ARM loan may be converted to a fixed-rate loan are established at the date of loan origination and are set to allow the Company to sell the loan into the secondary market upon conversion. The volume and types of ARM loans the Company originates have been affected by the level of market interest rates, competition, consumer preferences, and the availability of funds. ARM loans are susceptible to early prepayment during periods of lower interest rates as borrowers refinance into fixed-rate loans.

The Company requires an appraisal of the real estate that secures a residential mortgage loan, which must be performed by an independent certified appraiser approved by the board of directors. A title insurance policy is required for all real estate first mortgage loans. Evidence of adequate hazard insurance and flood insurance, if applicable, is required prior to closing. Borrowers are required to make monthly payments to fund principal and

interest as well as private mortgage insurance and flood insurance, if applicable. With some exceptions for lower loan-to-value ratio loans, borrowers are also generally required to escrow in advance for real estate taxes. Generally, no interest is paid on these escrow deposits. If borrowers with loans having a lower loan-to-value ratio want to handle their own taxes and insurance, an escrow waiver fee is charged. With respect to escrowed real estate taxes, the Company generally makes this disbursement directly to the borrower as obligations become due.

The Company's staff underwriters review all pertinent information prior to making a credit decision on an application. All recommendations to deny are reviewed by a designated senior officer of the Company, in addition to staff underwriters, prior to the final disposition of the application. The Company's lending policies generally limit the maximum loan-to-value ratio on single family mortgage loans secured by owner-occupied properties to 95% of the lesser of the appraised value or purchase price of the property. This limit is lower for loans secured by two-, three-, and four-family homes. Loans above 80% loan-to-value ratios are subject to private mortgage insurance to reduce the Company's exposure to less than 80% of value, except for certain low to moderate income loan program loans.

In addition to servicing the loans in its own portfolio, the Company continues to service most of the loans that it sells to Fannie Mae and other third-party investors ("loans serviced for others"). Servicing mortgage loans, whether for its own portfolio or for others, includes such functions as collecting monthly principal and interest payments from borrowers, maintaining escrow accounts for real estate taxes and insurance, and making certain payments on behalf of borrowers. When necessary, servicing of mortgage loans also includes functions related to the collection of delinquent principal and interest payments, loan foreclosure proceedings, and disposition of foreclosed real estate. As of December 31, 2012, loans serviced for others amounted to \$1.1 billion. These loans are not reflected in the Company's Consolidated Statements of Financial Condition.

When the Company services loans for others, it is compensated through the retention of a servicing fee from borrowers' monthly payments. The Company pays the third-party investors an agreed-upon yield on the loans, which is generally less than the interest agreed to be paid by the borrowers. The difference, typically 25 basis points or more, is retained by the Company and recognized as servicing fee income over the lives of the loans, net of amortization of capitalized mortgage servicing rights ("MSRs"). The Company also receives fees and interest income from ancillary sources such as delinquency charges and float on escrow and other funds.

Management believes that servicing mortgage loans for third parties provides a natural hedge against other risks inherent in the Company's mortgage banking operations. For example, fluctuations in volumes of mortgage loan originations and resulting gains on sales of such loans caused by changes in market interest rates will generally be offset by opposite changes in the amortization of the MSRs. These fluctuations are usually the result of actual loan prepayment activity and/or changes in management expectations for future prepayment activity, which impacts the amount of MSRs amortized in a given period. However, fluctuations in the recorded value of MSRs may also be caused by valuation adjustments required to be recognized under generally accepted accounting principles ("GAAP"). That is, the value of servicing rights may fluctuate because of changes in the future prepayment assumptions or discount rates used to periodically value the MSRs. Although most of the Company's serviced loans that prepay are replaced by new serviced loans (thus preserving the future servicing cash flow), GAAP requires impairment losses resulting from a change in future prepayment assumptions to be recorded when the change occurs. MSRs are particularly susceptible to impairment losses during periods of declining interest rates during which prepayment activity typically accelerates to levels above that which had been anticipated when the servicing rights were originally recorded. Alternatively, in periods of increasing interest rates, during which prepayment activity typically declines, the Company could potentially recapture through earnings all or a portion of a previously established valuation allowance for impairment.

***Multi-family and Commercial Real Estate Loans*** At December 31, 2012, the Company's aggregate portfolio of multi-family and commercial real estate loans was \$527.8 million or 35.2% of its gross loans receivable. The Company's multi-family and commercial real estate loan portfolios consist of fixed-rate and adjustable-rate loans originated at prevailing market rates usually tied to various market indices. This portfolio generally consists of loans secured by apartment buildings, office buildings, retail centers, warehouses, and industrial buildings. Loans in this portfolio may be secured by either owner or non-owner occupied properties. Loans in this portfolio typically do not exceed 80% of the lesser of the purchase price or an independent appraisal by an appraiser designated by us. Loans originated with balloon maturities are generally amortized on a 25 to 30 year basis with a typical balloon term of 3 to 5 years.

Loans secured by multi-family and commercial real estate are granted based on the income producing potential of the property, the financial strength and/or income producing potential of the borrower, and the appraised value of the property. In most cases, the Company also obtains personal guarantees from the principals involved. The Company's approval process includes a review of the other debt obligations and overall sources of cash flow available to the borrower and guarantors. The property's net operating income must be sufficient to cover the payments relating to the outstanding debt. The Company generally requires an assignment of rents or leases to be assured that the cash flow from the property will be used to repay the debt. Appraisals on properties securing multi-family and larger commercial real estate loans are performed by independent state certified or licensed fee appraisers approved by the board of directors. Title and hazard insurance are required as well as flood insurance, if applicable. Environmental assessments are performed on certain multi-family and commercial real estate loans in excess of \$1.0 million, as well as all loans secured by certain properties that the Company considers to be "environmentally sensitive." In addition, the Company performs an annual credit review of its multi-family and commercial real estate loans over \$1.0 million.

Loans secured by multi-family and commercial real estate properties are generally larger and involve a greater degree of credit risk than one- to four-family residential mortgage loans. Such loans typically involve large balances to single borrowers or groups of related borrowers. The Bank has internal lending limits to single borrowers or a group of related borrowers that are adjusted from time-to-time, but are generally well below the Bank's legal lending limit of approximately \$40.0 million as of December 31, 2012. Because payments on loans secured by multi-family and commercial real estate properties are often dependent on the successful operation or management of the properties, repayment of such loans may be subject to adverse conditions in the real estate market or the economy. Furthermore, borrowers' problems in areas unrelated to the properties that secure the Company's loans may have an adverse impact on such borrowers' ability to comply with the terms of the Company's loans.

**Construction and Development Loans** At December 31, 2012, the Company's portfolio of construction and development loans was \$129.3 million or 8.6% of its gross loans receivable. These loans typically have terms of 18 to 24 months, are interest-only, and carry variable interest rates tied to the prime rate. Disbursements on these loans are based on draw requests supported by appropriate lien waivers. As a general matter, construction loans convert to permanent loans and remain in the Company's loan portfolio upon the completion of the project. Development loans are typically repaid as the underlying lots or housing units are sold. Construction and development loans are generally considered to involve a higher degree of risk than mortgage loans on completed properties. The Company's risk of loss on a construction and development loan is dependent largely upon the accuracy of the initial estimate of the property's value at completion of construction, the estimated cost of construction, the appropriate application of loan proceeds to the work performed, and the borrower's ability to advance additional construction funds if necessary. In addition, in the event a borrower defaults on the loan during its construction phase, the construction project often needs to be completed before the full value of the collateral can be realized by the Company. The Company performs an annual credit review of its construction and development loans over \$1.0 million.

**Commercial Business Loans** At December 31, 2012, the Company's portfolio of commercial business loans was \$132.4 million or 8.9% of its gross loans receivable. This portfolio consists of loans to businesses for equipment purchases, working capital, debt refinancing or restructuring, business acquisition or expansion, Small Business Administration ("SBA") loans, and domestic standby letters of credit. Typically, these loans are secured by general business security agreements and personal guarantees. The Company offers variable, adjustable, and fixed-rate commercial business loans. The Company also has commercial business loans that have an initial period where interest rates are fixed, generally one to five years, and thereafter are adjustable based on various market indices. Fixed-rate loans are priced at either a margin over various market indices with maturities that correspond to the maturities of the notes or to match competitive conditions and yield requirements. Term loans are generally amortized over a three to seven year period. Commercial lines of credit generally have a term of one year and are subject to annual renewal thereafter. The Company performs an annual credit review of all commercial business borrowers having an exposure to the Company of \$500,000 or more.

**Consumer Loans** At December 31, 2012, the Company's portfolio of consumer loans was \$246.9 million or 16.5% of its gross loans receivable. Consumer loans include fixed term home equity loans, home equity lines of credit, home improvement loans, automobile loans, recreational vehicle loans, boat loans, deposit account loans, overdraft protection lines of credit, unsecured consumer loans, and to a lesser extent, unsecured consumer loans through credit card programs that are administered by third parties. The Company no longer originates student loans through programs guaranteed by the federal government. Student loans that continue to be held by the Company are administered by a third party.

The Company's primary focus in consumer lending has been the origination of loans secured by real estate, which includes home equity loans, home improvement loans, and home equity lines of credit. These loans are typically secured by junior liens on owner-occupied one- to four-family residences, but in many instances are secured by first liens on such properties. Underwriting procedures for the home equity and home equity lines of credit loans include a comprehensive review of the loan application, an acceptable credit score, verification of the value of the equity in the home, and verification of the borrower's income. Home equity and home improvement loan originations are developed through cross-sales to existing customers, advertisements in local media, the Bank's website, and from time-to-time, direct mail.

The Company originates fixed-rate home equity and home improvement term loans with loan-to-value ratios of up to 89.99% (when combined with any other mortgage on the property). Pricing on fixed-rate home equity and home improvement term loans is periodically reviewed by management. Generally, loan terms are in the three to fifteen year range in order to minimize interest rate risk.

The Company also originates home equity lines of credit. Home equity lines of credit are variable-rate loans secured by first liens or junior liens on owner-occupied one- to four-family residences. Current interest rates on home equity lines of credit are tied to an index rate, adjust monthly after an initial interest rate lock period, and generally have floors that vary depending on the loan-to-value ratio. Home equity line of credit loans are made for terms up to 10 years and require minimum monthly payments.

Consumer loans generally have shorter terms and higher rates of interest than conventional mortgage loans, but typically involve more credit risk because of the nature of the collateral and, in some instances, the absence of collateral. In general, consumer loans are more dependent upon the borrower's continuing financial stability, more likely to be affected by adverse personal circumstances, and often secured by rapidly depreciating personal property such as automobiles. In addition, various laws, including bankruptcy and insolvency laws, may limit the amount that may be recovered from a borrower. However, such risks are mitigated to some extent in the case of home equity loans and lines of credit. These types of loans are secured by a first or second mortgage on the borrower's residence for which the total principal balances outstanding (including the first mortgage) does not generally exceed 89.99% of the property's value at the time of the loan.

The Company believes that the higher yields earned on consumer loans compensate for the increased risk associated with such loans and that consumer loans are important to the Company's efforts to increase the interest rate sensitivity and shorten the average maturity of its loan portfolio.

In conjunction with its consumer lending activities, the Company offers customers credit life and disability insurance products underwritten and administered by an independent insurance provider. The Company receives commission revenue related to the sales of these products, although such amounts are not a material source of revenue for the Company.

### **Asset Quality**

**General** The Company has policies and procedures in place to manage its exposure to credit risk related to its lending operations. As a matter of policy, the Company limits its lending to geographic areas in which it has substantial familiarity and/or a physical presence. Currently, this is limited to certain specific market areas in Wisconsin and contiguous states. In addition, from time-to-time the Company will prohibit or restrict lending in situations in which the underlying business operations and/or collateral exceed management's tolerance for risk. The Company obtains appraisals of value prior to the origination of mortgage loans or other secured loans. It also manages its exposure to risk by regularly monitoring loan payment status, conducting periodic site visits and inspections, obtaining regular financial updates from large borrowers and/or guarantors, corresponding regularly with large borrowers and/or guarantors, and/or updating appraisals as appropriate, among other things. These procedures are emphasized when a borrower has failed to make scheduled loan payments, has otherwise defaulted on the terms of the loan agreement, or when management has become aware of a significant adverse change in the financial condition of the borrower, guarantor, or underlying collateral. For specific information relating to the Company's asset quality for the periods covered by this report, refer to "Financial Condition—Asset Quality" in "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations."

**Internal Risk Ratings and Classified Assets** OCC regulations require thrift institutions to review and, if necessary, classify their assets on a regular basis. Accordingly, the Company has internal policies and procedures in place to internally evaluate risk ratings on all of its loans and certain other assets. In general, these internal risk ratings

correspond with regulatory requirements to adversely classify problem loans and certain other assets as “substandard,” “doubtful,” or “loss.” A loan or other asset is adversely classified as substandard if it is determined to involve a distinct possibility that the Company could sustain some loss if deficiencies associated with the loan are not corrected. A loan or other asset is adversely classified as doubtful if full collection is highly questionable or improbable. A loan or other asset is adversely classified as loss if it is considered uncollectible, even if a partial recovery could be expected in the future. The regulations also provide for a “special mention” designation, described as loans or assets which do not currently expose the Company to a sufficient degree of risk to warrant adverse classification, but which demonstrate clear trends in credit deficiencies or potential weaknesses deserving management’s close attention (refer to the following paragraph for additional discussion). As of December 31, 2012, \$37.7 million or 2.7% the Company’s loans were classified as special mention and \$57.6 million or 4.1% were classified as substandard. The latter includes all loans placed on non-accrual in accordance with the Company’s policies, as described below. In addition, as of December 31, 2012, \$35.9 million of the Company’s mortgage-related securities, consisting of private-label collateralized mortgage obligations (“CMOs”) rated less than investment grade, were classified as substandard in accordance with regulatory guidelines. The Company had no loans or other assets classified as doubtful or loss at December 31, 2012.

Loans that are not classified as special mention or adversely classified as substandard, doubtful, or loss are classified as “pass” or “watch” in accordance with the Company’s internal risk rating policy. Pass loans are generally current on contractual loan and principal payments, comply with other contractual loan terms, and have no noticeable credit deficiencies or potential weaknesses. Watch loans are also generally current on payments and in compliance with loan terms, but a particular borrower’s financial or operating conditions may exhibit early signs of credit deficiencies or potential weaknesses that deserve management’s close attention. Such deficiencies and/or weaknesses typically include, but are not limited to, the borrower’s financial or operating condition, deterioration in liquidity, increased financial leverage, declines in the condition or value of related collateral, recent changes in management or business strategy, or recent developments in the economic, competitive, or market environment of the borrower. If adverse observations noted in these areas are not corrected, further downgrade of the loan may be warranted.

***Delinquent Loans*** When a borrower fails to make required payments on a loan, the Company takes a number of steps to induce the borrower to cure the delinquency and restore the loan to a current status. In the case of one- to four-family mortgage loans, the Company’s loan servicing department is responsible for collection procedures from the 15th day of delinquency through the completion of foreclosure. Specific procedures include late charge notices, telephone contacts, and letters. If these efforts are unsuccessful, foreclosure notices will eventually be sent. The Company may also send either a qualified third party inspector or a loan officer to the property in an effort to contact the borrower. When contact is made with the borrower, the Company attempts to obtain full payment or work out a repayment schedule to avoid foreclosure of the collateral. Many borrowers pay before the agreed upon payment deadline and it is not necessary to start a foreclosure action. The Company follows collection procedures and guidelines outlined by Fannie Mae, Freddie Mac, State VA, WHEDA, and the Guaranteed Rural Housing Program.

The collection procedures for consumer loans, excluding student loans and credit card loans, include sending periodic late notices to a borrower and attempts to make direct contact with a borrower once a loan becomes 30 days past due. If collection activity is unsuccessful, the Company may pursue legal remedies itself, refer the matter to legal counsel for further collection effort, seek foreclosure or repossession of the collateral (if any), and/or charge-off the loan. All student loans are serviced by a third party, which guarantees that its servicing complies with all U.S. Department of Education guidelines. The Company’s student loan portfolio is guaranteed under programs sponsored by the U.S. government. Credit card loans are serviced by a third party administrator.

The collection procedures for multi-family, commercial real estate, and commercial business loans include sending periodic late notices to a borrower once a loan is past due. The Company attempts to make direct contact with a borrower once a loan becomes 15 days past due. The Company’s managers of the multi-family and commercial real estate loan areas review loans 10 days or more delinquent on a regular basis. If collection activity is unsuccessful, the Company may refer the matter to legal counsel for further collection effort. After 90 days, loans that are delinquent are typically proposed for repossession or foreclosure.

In working with delinquent borrowers, if the Company cannot develop a repayment plan that substantially complies with the original terms of the loan agreement, the Company’s practice has been to pursue foreclosure or repossession of the underlying collateral. As a matter of practice, the Company has not restructured or modified troubled loans in a manner that has resulted in a loss under accounting rules. However, the Company’s policies do not preclude such practice and the Company may elect in the future to restructure certain troubled loans in a manner that could result in losses under accounting rules. In most cases the Company continues to report restructured or modified troubled

loans as non-performing loans unless the borrower has clearly demonstrated the ability to service the loan in accordance with the new terms.

The Company's policies require that management continuously monitor the status of the loan portfolio and report to the board of directors on a monthly basis. These reports include information on classified loans, delinquent loans, restructured or modified loans, allowance for loan losses, and foreclosed real estate.

**Non-Accrual Policy** With the exception of student loans that are guaranteed by the U.S. government, the Company generally stops accruing interest income on loans when interest or principal payments are 90 days or more in arrears or earlier when the future collectability of such interest or principal payments may no longer be certain. In such cases, borrowers have often been able to maintain a current payment status, but are experiencing financial difficulties and/or the properties that secure the loans are experiencing increased vacancies, declining lease rates, and/or delays in unit sales. In such instances, the Company generally stops accruing interest income on the loans even though the borrowers are current with respect to all contractual payments. Although the Company generally no longer accrues interest on these loans, the Company may continue to record periodic interest payments received on such loans as interest income provided the borrowers remain current on the loans and provided, in the judgment of management, the Company's net recorded investment in the loans are deemed to be collectible. The Company designates loans on which it stops accruing interest income as non-accrual loans and establishes a reserve for outstanding interest that was previously credited to income. All loans on non-accrual are considered to be impaired. The Company returns a non-accrual loan to accrual status when factors indicating doubtful or uncertain collection no longer exist. In general, non-accrual loans are also classified as substandard, doubtful, or loss in accordance with the Company's internal risk rating policy. As of December 31, 2012, \$25.8 million or 1.84% of the Company's loans were considered to be non-performing in accordance with the Company's policies.

**Foreclosed Properties and Repossessed Assets** As of December 31, 2012, \$14.0 million or 0.6% of the Company's total assets consisted of foreclosed properties and repossessed assets. In the case of loans secured by real estate, foreclosure action generally starts when the loan is between the 90th and 120th day of delinquency following review by a senior officer and the executive loan committee of the board of directors. If, based on this review, the Company determines that repayment of a loan is solely dependent on the liquidation of the collateral, the Company will typically seek the shortest redemption period possible, thus waiving its right to collect any deficiency from the borrower. Depending on whether the Company has waived this right and a variety of other factors outside the Company's control (including the legal actions of borrowers to protect their interests), an extended period of time could transpire between the commencement of a foreclosure action by the Company and its ultimate receipt of title to the property.

When the Company ultimately obtains title to the property through foreclosure or deed in lieu of foreclosure, it transfers the property to "foreclosed properties and repossessed assets" on the Company's Consolidated Statements of Financial Condition. In cases in which a borrower has surrendered control of the property to the Company or has otherwise abandoned the property, the Company may transfer the property to foreclosed properties as an "in substance foreclosure" prior to actual receipt of title. Foreclosed properties and repossessed assets are adversely classified in accordance with the Company's internal risk rating policy.

Foreclosed real estate properties are initially recorded at the lower of the recorded investment in the loan or fair value. Thereafter, the Company carries foreclosed real estate at fair value less estimated selling costs (typically 5% to 10%). Foreclosed real estate is inspected periodically to evaluate its condition. Additional outside appraisals are obtained as deemed necessary or appropriate. Additional write-downs may occur if the property value deteriorates further after it is acquired. These additional write-downs are charged to the Company's results of operations as they occur.

In the case of loans secured by assets other than real estate, action to repossess the underlying collateral generally starts when the loan is between the 90th and 120th day of delinquency following review by management. The accounting for repossessed assets is similar to that described for real estate, above.

**Loan Charge-Offs** The Company typically records loan charge-offs when foreclosure or repossession becomes likely or legal proceedings related to such have commenced, the secondary source of repayment (consisting of a guarantor or operating entity) files for bankruptcy, or the loan is otherwise deemed uncollectible. The amount of the charge-off will depend on the fair market value of the underlying collateral, if any, and may be zero if the fair market value exceeds the loan amount. All charge-offs are recorded as a reduction to allowance for loan losses. All charge-off activity is reviewed by the board of directors.

**Allowance for Loan Losses** As of December 31, 2012, the Company's allowance for loan losses was \$21.6 million or 1.54% of loans receivable and 83.6% of non-performing loans. The allowance for loan losses is maintained at a level believed adequate by management to absorb probable losses inherent in the loan portfolio and is based on factors such as the size and current risk characteristics of the portfolio, an assessment of individual problem loans and pools of homogenous loans within the portfolio, and actual loss, delinquency, and/or risk rating experience within the portfolio. The Company also considers current economic conditions and/or events in specific industries and geographical areas, including unemployment levels, trends in real estate values, peer comparisons, and other pertinent factors, including regulatory guidance. Finally, as appropriate, the Company also considers individual borrower circumstances and the condition and fair value of the loan collateral, if any. For additional information relating to the Company's allowance for loan losses for the periods covered by this report, refer to "Results of Operations—Provision for Loan Losses" and "Financial Condition—Asset Quality" in "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations."

Determination of the allowance is inherently subjective as it requires significant management judgment and estimates, including the amounts and timing of expected future cash flows on loans, the fair value of underlying collateral (if any), estimated losses on pools of homogeneous loans based on historical loss experience, changes in risk characteristics of the loan portfolio, and consideration of current economic trends, all of which may be susceptible to significant change. Higher rates of loan defaults than anticipated would likely result in a need to increase provisions in future years. Also, increases in the Company's multi-family, commercial real estate, construction and development, and commercial business loan portfolios could result in a higher allowance for loan losses as these loans typically carry a higher risk of loss. Finally, various regulatory agencies, as an integral part of their examination processes, periodically review the Company's loan and foreclosed real estate portfolios and the related allowance for loan losses and valuation allowance for foreclosed real estate. One or more of these agencies, particularly the OCC, may require the Company to increase the allowance for loan losses or the valuation allowance for foreclosed real estate based on their judgments of information available to them at the time of their examination, thereby adversely affecting the Company's results of operations. As a result of applying management judgment, it is possible that there may be periods when the amount of the allowance and/or its percentage to total loans or non-performing loans may decrease even though non-performing loans may increase.

Periodic adjustments to the allowance for loan loss are recorded through provision for loan losses in the Company's Consolidated Statements of Income. Actual losses on loans are charged off against the allowance for loan losses. In the case of loans secured by real estate, charge-off typically occurs when foreclosure or repossession is likely or legal proceedings related to such have commenced, when the secondary source of repayment (consisting of a guarantor or operating entity) files for bankruptcy, or when the loan is otherwise deemed uncollectible in the judgment of management. Loans not secured by real estate, as well as unsecured loans, are charged off when the loan is determined to be uncollectible in the judgment of management. Recoveries of loan amounts previously charged off are credited to the allowance as received. Management reviews the adequacy of the allowance for loan losses on a monthly basis. The board of directors reviews management's judgments related to the allowance for loan loss on at least a quarterly basis.

The Company maintains general allowances for loan loss against certain homogenous pools of loans. These pools generally consist of smaller one- to four-family, multi-family, commercial real estate, consumer, and commercial business loans that do not warrant individual review due to their size. In addition, pools may also consist of larger multi-family, commercial real estate, and commercial business loans that have not been individually identified as impaired by management. Certain of these pools, such as the one- to four-family and consumer loan pools, are further segmented according to the nature of the collateral that secures the loans. For example, the consumer loan pool is segmented by collateral type, such as loans secured by real estate, loans secured by automobiles, and loans secured by other collateral. The various loan pools are further segmented by management's internal risk rating of the loans. Management has developed factors for each pool or segment based on the historical loss experience of each pool or segment, recent delinquency performance, internal risk ratings, and consideration of current economic trends, in order to determine what it believes is an appropriate level for the general allowance. Given the significant amount of management judgment involved in this process there could be significant variation in the Company's allowance for loan losses and provision for loan losses from period to period.

The Company maintains specific allowances for loan loss against individual loans that have been identified by management as impaired. These loans are generally larger loans, but management may also establish specific allowances against smaller loans from time-to-time. The allowance for loan loss established against these loans is based on one of two methods: (1) the present value of the future cash flows expected to be received from the

borrower, discounted at the loan's effective interest rate, or (2) the fair value of the loan collateral, if the loan is considered to be collateral dependent. In the Company's experience, loss allowances using the first method have been rare. In working with problem borrowers, if the Company cannot develop a repayment plan that substantially complies with the original terms of the loan agreement, the Company's practice has been to pursue foreclosure or repossession of the underlying collateral. As a matter of practice, the Company does not restructure troubled loans in a manner that results in a loss under the first method. As a result, most loss allowances are established using the second method because the related loans have been deemed collateral dependent by management.

Management considers loans to be collateral dependent when, in its judgment, there is no source of repayment for the loan other than the ultimate sale or disposition of the underlying collateral and foreclosure is probable. Factors management considers in making this determination typically include, but are not limited to, the length of time a borrower has been delinquent with respect to loan payments, the nature and extent of the financial or operating difficulties experienced by the borrower, the performance of the underlying collateral, the availability of other sources of cash flow or net worth of the borrower and/or guarantor, and the borrower's immediate prospects to return the loan to performing status. In some instances, because of the facts and circumstances surrounding a particular loan relationship, there could be an extended period of time between management's identification of a problem loan and a determination that it is probable that such loan is or will become collateral dependent. Based on recent experience, however, management has noted the length of time has shortened between when a loan is classified as non-performing and when it is considered to be collateral dependent. Management believes this is a trend that will continue as long as economic conditions and/or commercial real estate values remain depressed.

Management generally measures impairment of impaired loans whether or not foreclosure is probable based on the estimated fair value of the underlying collateral. Such estimates are based on management's judgment or, when considered appropriate, on an updated appraisal or similar evaluation. Updated appraisals are also typically obtained on or about the time of foreclosure or repossession of the underlying collateral. Prior to receipt of the updated appraisal, management has typically relied on the original appraisal and knowledge of the condition of the collateral, as well as the current market for the collateral, to estimate the Company's exposure to loss on impaired loans. In the judgment of management, this practice was acceptable in periods of relative stability in real estate markets. However, as a result of deterioration in commercial real estate markets since 2008, as well as the Company's recent experience, management believes that as long as economic conditions and/or real estate markets remain depressed updated appraisals will continue to be obtained on impaired loans earlier in the evaluation process than may have been typical during periods of more stable real estate markets.

### **Investment Activities**

At December 31, 2012, the Company's portfolio of mortgage-related securities available-for-sale was \$550.2 million or 22.8% of its total assets. As of the same date its portfolio of mortgage-related securities held-to-maturity was \$157.6 million or 6.5% of total assets. Mortgage-related securities consist principally of mortgage-backed securities ("MBSs"), real estate mortgage investment conduits ("REMICs"), and CMOs. Most of the Company's mortgage-related securities are directly or indirectly insured or guaranteed by Freddie Mac, Fannie Mae, or the Government National Mortgage Association ("Ginnie Mae"). The remaining securities are private-label CMOs. Private-label CMOs generally carry higher credit risks and higher yields than mortgage-related securities insured or guaranteed by the aforementioned agencies of the U.S. Government. Although the latter securities have less exposure to credit risk, like private-label CMOs they remain exposed to fluctuating interest rates and instability in real estate markets, which may alter the prepayment rate of underlying mortgage loans and thereby affect the fair value of the securities. For additional information related to the Company's mortgage-related securities, refer to "Financial Condition—Mortgage-Related Securities Available-for-Sale" and "Financial Condition—Mortgage-Related Securities Held-to-Maturity" in "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations."

In addition to the mortgage-related securities previously described, the Company's investment policy authorizes investment in various other types of securities, including U.S. Treasury obligations, federal agency obligations, state and municipal obligations, certain certificates of deposit of insured banks and savings institutions, certain bankers' acceptances, repurchase agreements, federal funds, commercial paper, mutual funds, and, subject to certain limits, corporate debt and equity securities.

The objectives of the Company's investment policy are to meet the liquidity requirements of the Company and to generate a favorable return on investments without compromising objectives related to overall exposure to risk, including interest rate risk, credit risk, and investment portfolio concentrations. In addition, the Company pledges

eligible securities as collateral for certain deposit liabilities, FHLB of Chicago advances, and other purposes permitted or required by law.

The Company's investment policy requires that securities be classified as trading, available-for-sale, or held-to-maturity at the date of purchase. The Company's available-for-sale securities are carried at fair value with the change in fair value recorded as a component of shareholders' equity rather than affecting the statement of operations. The Company's held-to-maturity securities are carried at amortized cost. The Company has not engaged in trading activities.

The Company's investment policy allows the use of hedging instruments such as financial futures, options, forward commitments, and interest rate swaps, but only with prior approval of the board of directors. Other than forward commitments related to its sale of residential loans in the secondary market, the Company did not have any investment hedging transactions in place at December 31, 2012. The Company's investment policy prohibits the purchase of non-investment grade securities, although the Company may continue to hold investments that are reduced to less than investment grade after their purchase. Securities rated less than investment grade are adversely classified as substandard in accordance with federal guidelines (refer to Asset Quality—Internal Ratings and Classified Assets," above).

### **Deposit Liabilities**

At December 31, 2012, the Company's deposit liabilities were \$1.9 billion or 77.2% of its total liabilities and equity. The Company offers a variety of deposit accounts having a range of interest rates and terms for both retail and business customers. The Company currently offers regular savings accounts (consisting of passbook and statement savings accounts), interest-bearing demand accounts, non-interest-bearing demand accounts, money market accounts, and certificates of deposit. The Company also offers IRA time deposit accounts and health savings accounts. When the Company determines its deposit rates, it considers rates offered by local competitors, benchmark rates on U.S. Treasury securities, and rates on other sources of funds such as FHLB of Chicago advances. For additional information, refer to "Financial Condition—Deposit Liabilities" in "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations."

Deposit flows are significantly influenced by general and local economic conditions, changes in prevailing interest rates, pricing of deposits, and competition. The Company's deposits are primarily obtained from the market areas surrounding its bank offices. The Company relies primarily on competitive rates, quality service, and long-standing relationships with customers to attract and retain these deposits. The Company does not rely on a particular customer or related group of individuals, organizations, or institutions for its deposit funding. From time to time the Company has used third-party brokers and a nationally-recognized reciprocal deposit gathering network to obtain wholesale deposits. As of December 31, 2012, the Company did not have any brokered deposits outstanding and had less than \$500,000 in reciprocal deposits outstanding.

### **Borrowings**

At December 31, 2012, the Company's borrowed funds were \$210.8 million or 8.7% of its total liabilities and equity. The Company borrows funds to finance its lending, investing, operating, and, when active, stock repurchase activities. Substantially all of its borrowings take the form of advances from the FHLB of Chicago and are on terms and conditions generally available to member institutions. The Company's FHLB of Chicago borrowings typically carry fixed rates of interest, have stated maturities, and are generally subject to significant prepayment penalties if repaid prior to their stated maturity. The Company has pledged one- to four-family mortgage loans and certain multi-family mortgage loans and available-for-sale securities as blanket collateral for current and future advances. For additional information regarding the Company's outstanding advances from the FHLB of Chicago as of December 31, 2012, refer to "Financial Condition—Borrowings" in "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations."

### **Shareholders' Equity**

At December 31, 2012, the Company's shareholders' equity was \$271.9 million or 11.24% of its total liabilities and equity. The Company is not currently required to maintain minimum regulatory capital at the holding company level. However, refer to "Regulation and Supervision—Regulation of the Company," below, for additional information related to regulatory capital requirements for the Company.

Although the Company is not currently required to maintain minimum regulatory capital, the Bank is required to maintain specified amounts of regulatory capital pursuant to regulations promulgated by the OCC and the FDIC. The Bank's objective is to maintain its regulatory capital in an amount sufficient to be classified in the highest regulatory category (i.e., as a "well capitalized" institution). At December 31, 2012, the Bank exceeded all regulatory minimum requirements, as well as the amount required to be classified as a "well capitalized" institution. For additional discussion relating to regulatory capital standards refer to "Regulation and Supervision of the Bank—Regulatory Capital Requirements" and "—Prompt Corrective Action," below. For additional information related to the Company's equity and the Bank's regulatory capital for the periods covered by this report, refer to "Financial Condition—Shareholders' Equity" in "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations," as well as "Note 8. Shareholders' Equity" in "Item 8. Financial Statements and Supplementary Data."

The Company has paid quarterly cash dividends since its initial stock offering in 2000. The payment of dividends is discretionary with the Company's board of directors and depends on the Company's operating results, financial condition, compliance with regulatory capital requirements, and other considerations. In addition, the Company's ability to pay dividends is highly dependent on the Bank's ability to pay dividends to the Company. As such, there can be no assurance that the Company will be able to continue the payment of dividends or that the level of dividends will not be reduced in the future. For additional information, refer to "Regulation and Supervision of the Bank—Dividend and Other Capital Distribution Limitations," below.

From time to time, the Company has repurchased shares of its common stock, and such repurchases have had the effect of reducing the Company's capital. However, as with the payment of dividends above, the repurchase of common stock is discretionary with the Company's board of directors and depends on a variety of factors, including market conditions for the Company's stock, the financial condition of the Company and the Bank, compliance with regulatory capital requirements, and other considerations. The Company does not have a current stock repurchase program. As a result of these considerations, there can be no assurances as to if or when the Company will be able to resume repurchases of its common stock.

### **Subsidiaries**

BancMutual Financial & Insurance Services, Inc. ("BMFIS"), a wholly-owned subsidiary of the Bank, provides investment, brokerage, and insurance services to the Bank's customers and the general public. Investment services include tax-deferred and tax-free investments, mutual funds, and government securities. Personal insurance, business insurance, life and disability insurance, mortgage protection products, and investment advisory services are also offered by BMFIS. Certain of BMFIS's brokerage services are provided through an operating agreement with a third-party, registered broker-dealer.

Mutual Investment Corporation ("MIC"), a wholly-owned subsidiary of the Bank, owns and manages investment and mortgage-related securities. First Northern Investment Inc. ("FNII"), a wholly-owned subsidiary of the Bank, also owns and manages investment and mortgage-related securities, as well a small number of one- to four-family mortgage loans.

MC Development LTD ("MC Development"), a wholly-owned subsidiary of the Bank, is involved in land development and sales. It owns five parcels of developed land totaling 15 acres in Brown Deer, Wisconsin. In addition, in 2004, MC Development established Arrowood Development LLC with an independent third party to develop approximately 300 acres for residential purposes in Oconomowoc, Wisconsin. In the initial transaction, the third party purchased approximately one-half interest in that land, all of which previously had been owned by MC Development.

In addition, the Bank has four wholly-owned subsidiaries that are inactive, but are reserved for possible future use in related or other areas.

### **Employees**

At December 31, 2012, the Company employed 639 full time and 81 part time associates. Management considers its relations with its associates to be good.

## **Regulation and Supervision**

### ***General***

The Company is a Wisconsin corporation and a registered savings and loan holding company under federal law. The Company files reports with and is subject to regulation and examination by the FRB. As a Wisconsin corporation, the Company is subject to the provisions of the Wisconsin Business Corporation Law, and as a public company, it is subject to regulation by the SEC. The Bank is a federally-chartered savings bank and is subject to OCC requirements as well as those of the FDIC. Any change in these laws and regulations, whether by the FRB, the OCC, the FDIC, or through legislation, could have a material adverse impact on the Company, the Bank, and the Company's shareholders.

Certain current laws and regulations applicable to the Company and the Bank, and other material consequences of recent legislation, are summarized below. These summaries do not purport to be complete and are qualified in their entirety by reference to such laws, regulations, or administrative considerations.

### ***Termination of Memoranda of Understanding***

In May 2011 the Company and the Bank agreed to address certain items identified by the Office of Thrift Supervision ("OTS"), their former regulator, during a regular examination by each entering into a separate Memorandum of Understanding ("MOU") with the OTS. An MOU is an agreement between the regulator and a financial institution which requires the institution to exercise reasonable good faith efforts to comply with the requirements of the MOU. In addition to other requirements, under their respective MOUs the Company and the Bank were required to obtain the prior written non-objection or approval of federal regulators prior to declaring or paying cash dividends and, in the case of the Company, prior to repurchasing common shares, or incurring, issuing, increasing, modifying or redeeming any debt or lines of credit. However, as a result of the Company's and Bank's compliance with the requirements of the MOUs, as well as their improved financial condition and operating results, the FRB and OCC recently terminated the MOUs with the Company and Bank, respectively.

### ***Financial Services Industry Legislation and Related Actions***

In response to instability in the U.S. financial system, lawmakers and federal banking agencies have taken various actions intended to stabilize the financial system and housing markets, and to strengthen U.S. financial institutions.

***Dodd-Frank Act*** In 2010 Congress enacted the Dodd-Frank Act, which significantly changed the U.S. financial institution regulatory structure, as well as the lending, investment, trading, and operating activities of financial institutions and their holding companies. In 2011 the Dodd-Frank Act eliminated the OTS and transferred all of its functions and authority relating to federal thrifts, such as the Bank, to the OCC. In addition, the FRB acquired supervisory and rule-making authority over all savings and loan holding companies, such as the Company. The Dodd-Frank Act also requires the FRB to apply to savings and loan holding companies the current consolidated leverage and risk-based capital standards that insured depository institutions must follow, which will include capital requirements for the Company effective in July 2015 (refer to "Regulation and Supervision—Regulation of the Company," below, for additional information related to regulatory capital requirements for the Company). Further, the Dodd-Frank Act has imposed new disclosure and governance requirements on publicly-held companies, such as the Company.

The Dodd-Frank Act also created the Consumer Financial Protection Bureau ("CFPB") with broad powers to supervise and enforce consumer protection laws. The CFPB has broad rule-making authority for a wide range of consumer protection laws that apply to all banks and savings institutions, such as the Bank. However, institutions with \$10 billion or less in assets, such as the Bank, will be examined for CFPB compliance by their applicable bank regulators, rather than the CFPB itself.

The Dodd-Frank Act broadened the base for FDIC insurance assessments, which beginning in April 2011 was based on the average consolidated total assets less tangible equity capital of a financial institution. Prior to that time insurance assessments had been based on an insured institution's domestic deposits. The Dodd-Frank Act also permanently increases the maximum amount of deposit insurance for insured institutions to \$250,000 per depositor.

Many of the provisions of the Dodd-Frank Act are subject to future rule-making procedures and studies, and the full effects of the Dodd-Frank Act on the Company and/or the Bank cannot yet be determined. The OCC is continuing a

complete review of former OTS regulations that it now administers, with a goal of achieving consistency with the OCC's regulations for national banks and has already updated certain regulations and pronouncements. These provisions and reviews, or any other regulatory or legislative changes to laws applicable to the financial industry, if enacted or adopted, may impact the profitability of the Company's or the Bank's business activities or change certain of their business practices, including the Bank's ability to offer new products, obtain financing, attract deposits, make loans, and achieve satisfactory interest spreads, and could expose the Company to additional costs, including increased compliance costs. These changes also may require the Company to invest significant management attention and resources to make any necessary changes to operations in order to comply and could therefore also materially affect the Company's and the Bank's business, financial condition, and results of operations.

### ***Regulation and Supervision of the Bank***

**General** As a federally-chartered, FDIC-insured savings bank, the Bank is subject to extensive regulation by the OCC, as well as the regulations of the FDIC. Lending activities and other investments must comply with federal statutory and regulatory requirements. This federal regulation and supervision establishes a comprehensive framework of activities in which a federal savings bank may engage and is intended primarily for the protection of the FDIC and depositors rather than the shareholders of the Company. This regulatory structure gives authorities extensive discretion in connection with their supervisory and enforcement activities and examination policies, including policies regarding the classification of assets and the establishment of adequate loan loss reserves.

The OCC regularly examines the Bank and issues a report on its examination findings to the Bank's board of directors. The Bank's relationships with its depositors and borrowers are also regulated by federal law, especially in such matters as the ownership of savings accounts and the form and content of the Bank's loan documents.

The Bank must file reports with the OCC and the FDIC concerning its activities and financial condition, and must obtain regulatory approvals prior to entering into transactions such as mergers or acquisitions.

**Regulatory Capital Requirements** OCC regulations require savings associations such as the Bank to meet three capital standards. The minimum standards are tangible capital equal to at least 1.5% of adjusted total assets, Tier 1 ("core") capital equal to at least 4% of adjusted total assets (also known as the "leverage ratio"), and total risk-based capital equal to at least 8% of total risk-weighted assets. If a savings association is rated in the OCC's highest supervisory category, the minimum leverage ratio is reduced to 3%. These capital standards are in addition to the capital standards promulgated by the OCC under its prompt corrective action regulations and standards required by the FDIC, which in some cases are more stringent than the above standards.

In the Bank's case, core capital is equal to tangible capital. Core capital generally consists of common shareholders' equity, noncumulative perpetual preferred stock and related surplus, and minority interests in the equity accounts of consolidated subsidiaries, less goodwill, other intangible assets, and certain deferred tax assets. Supplemental bank capital generally consists of core capital plus the allowance for loan and lease losses (up to a maximum of 1.25% of risk-weighted assets), cumulative perpetual preferred stock, long-term preferred stock and any related surplus, certain hybrid capital investments, term subordinated debt instruments and related surplus, and up to 45% of the pretax net unrealized holding gains on various instruments and other assets. Supplemental capital may not represent more than 50% of the total capital for the risk-based capital standard.

A savings association calculates its risk-weighted assets by multiplying each asset and off-balance sheet item by various risk factors as determined by the OCC, which range from 0% for cash to 100% for delinquent loans, property acquired through foreclosure, commercial loans, and other assets. In addition, certain available-for-sale securities rated less than investment grade are assigned a risk factor of 200%.

The Bank's objective is to maintain its regulatory capital in an amount sufficient to be classified in the highest regulatory category (i.e., as a "well capitalized" institution). At December 31, 2012, the Bank exceeded all regulatory minimum requirements, as well as those required to be classified as a "well capitalized" institution. For additional information related to the Bank's regulatory capital for the periods covered by this report, refer to "Note 8. Shareholders' Equity" in "Item 8. Financial Statements and Supplementary Data."

**Prompt Corrective Action** The FDIC has established a system of prompt corrective action to resolve the problems of undercapitalized insured institutions and has a broad range of grounds under which it may appoint a receiver or conservator for an insured depository institution, particularly when an institution fails to meet adequate capitalization requirements. The OCC has adopted the FDIC's regulations governing the supervisory actions that may be taken

against undercapitalized institutions, the severity of which increases as a bank's capital decreases with the three undercapitalized categories defined in the regulations. These regulations establish and define five capital categories, in the absence of a specific capital directive, as follows:

<u>Category:</u>	<u>Total Risk-Based Capital to Risk Weighted Assets</u>	<u>Tier 1 Capital to Risk Weighted Assets</u>	<u>Tier 1 Capital to Total Assets</u>
Well capitalized	≥ 10%	≥ 6%	≥ 5%
Adequately capitalized	≥ 8%	≥ 4%	≥ 4% (1)
Under capitalized	< 8%	< 4%	< 4% (2)
Significantly undercapitalized	< 6%	< 3%	< 3%
Critically undercapitalized (3)			

(1) ≥ 3% if the bank receives the highest rating under the uniform system.

(2) < 3% if the bank receives the highest rating under the uniform system.

(3) Tangible assets to capital of equal to or less than 2%.

**Proposed Regulatory Capital Requirements** In 2012 the federal banking agencies issued proposed rules that would implement certain revisions to regulatory capital requirements as specified by the Basel Committee of Banking Supervision (known as Basel III). The proposed rules, if adopted, are expected to have a significant impact on the minimum regulatory requirements of regulated financial institutions such as the Bank. However, management believes the regulatory capital of the Bank will exceed the minimum requirements established in the proposed rules and that the implementation or timing of the rules will not have a significant adverse impact on the financial condition, liquidity, or operations of the Bank. It is not known at this time when the proposed rules will become effective or whether the proposed rules will be substantially modified prior to their becoming effective.

**Dividend and Other Capital Distribution Limitations** OCC regulations generally govern capital distributions by savings associations such as the Bank, which include cash dividends and stock repurchases. A savings association must file an application with the OCC for approval of a capital distribution if, among other things, the total amount of capital distributions for the applicable calendar year exceeds the sum of the savings association's net income for that year to date plus the savings association's retained net income for the preceding two years.

In addition, even if an application is not required, a savings association must give the OCC notice at least 30 days before the board of directors declares a dividend or approves a capital distribution if the savings association is a subsidiary of a savings and loan holding company (as is the Bank) or the proposed distribution would negatively affect the adequacy of capital. In the case of a subsidiary, there is an exception; if the subsidiary is filing a notice for a cash dividend and neither an application (discussed above) or a notice (discussed in this paragraph) with the OCC is otherwise required, then the subsidiary need only file an informational copy of such notice with the OCC, in which case the subsidiary dividend to the holding company is also subject to the approval or non-objection of the FRB.

The OCC may disapprove a notice or application if (i) the savings association would be undercapitalized, significantly undercapitalized or critically undercapitalized following the distribution; (ii) the proposed capital distribution raises safety and soundness concerns; or (iii) the capital distribution would violate any applicable statute, regulation, agreement or OCC-imposed condition. The OCC has substantial discretion in making these decisions. The FRB may disapprove a dividend for similar reasons.

For additional discussion related to the Bank and Company's dividends and the Company's share repurchases refer to "Financial Condition—Shareholders' Equity" in "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operation."

**Qualified Thrift Lender Test** Federal savings associations must meet a qualified thrift lender ("QTL") test or they become subject to operating restrictions. The Bank met the QTL test as of December 31, 2012, and anticipates that it will maintain an appropriate level of mortgage-related investments (which must be at least 65% of portfolio assets) and will otherwise continue to meet the QTL test requirements. Portfolio assets are all assets minus goodwill and other intangible assets, property used by the institution in conducting its business, and liquid assets not exceeding 20% of total assets. Compliance with the QTL test is determined on a monthly basis in nine out of every twelve months.

**Liquidity Standards** Each federal savings association must maintain sufficient liquidity to ensure its safe and sound operations. Management of the Bank believes it has established policies, procedures, and practices to maintain sufficient liquidity to meet the Bank's obligations and otherwise ensure its safe and sound operation.

**Federal Home Loan Bank System** The Bank is a member of the FHLB of Chicago, one of twelve regional Federal Home Loan Banks. Each Federal Home Loan Bank serves as a reserve or central bank for its members within its region. It is funded primarily from funds deposited by member financial institutions and proceeds from the sale of consolidated obligations of the Federal Home Loan Bank System. The FHLB of Chicago makes loans ("advances") to members pursuant to policies and procedures established by its board of directors. The FHLB of Chicago imposes limits on advances made to member banks, including limitations relating to the amount and type of collateral and the amount of advances.

As a member of the FHLB of Chicago, the Bank must meet certain eligibility requirements and must purchase and maintain common stock in the FHLB of Chicago in an amount equal to the greater of (i) 1% of its mortgage-related assets at the most recent calendar year end, (ii) 5% of its outstanding advances from the FHLB of Chicago, or (iii) \$10,000. At December 31, 2012, the Bank owned \$15.8 million in FHLB of Chicago common stock, which was approximately \$5.3 million more than the Bank would otherwise be required to own under minimum guidelines established by the FHLB of Chicago. Management believes the FHLB of Chicago will repurchase this excess common stock in 2013, although there can be no assurances. During 2012, the FHLB of Chicago repurchased \$30.3 million of excess common stock that had been owned by the Bank. For additional discussion related to the Bank's investment in the common stock of the FHLB of Chicago, refer to "Item 1A. Risk Factors" and "Financial Condition—Other Assets" in "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations."

**Deposit Insurance** The deposit accounts held by customers of the Bank are insured by the FDIC up to maximum limits, as provided by law. Insurance on deposits may be terminated by the FDIC if it finds that the Bank has engaged in unsafe or unsound practices, is in an unsafe or unsound condition to continue operations or has violated any applicable law, regulation, rule, order or condition imposed by the FDIC or the OCC. The management of the Bank does not know of any practice, condition, or violation that might lead to termination of the Bank's deposit insurance.

The FDIC sets deposit insurance premiums based upon the risks a particular bank or savings association poses to its deposit insurance funds. Under the risk-based assessment system, the FDIC assigns an institution to one of three capital categorizations based on the institution's financial information. With respect to these three categorizations, institutions are classified as well capitalized, adequately capitalized or undercapitalized using ratios that are substantially similar to the prompt corrective action capital ratios discussed above. The FDIC also assigns an institution to one of three supervisory sub-categorizations within each capital group. This assignment is based on a supervisory evaluation provided by the institution's primary federal regulator and information that the FDIC determines to be relevant to the institution's financial condition and the risk posed to the deposit insurance fund.

An institution's assessment rate depends on the capital categorizations and supervisory sub-categorizations to which it is assigned. Under the risk-based assessment system, there are then four assessment risk categories to which different assessment rates are applied (refer to the next paragraph for a description of these assessment rates). Any increase in insurance assessments could have an adverse effect on the earnings of insured institutions, including the Bank.

Effective in April 2011 the FDIC changed the definition of a financial institution's deposit insurance assessment base and revised the deposit insurance risk-based assessment rate schedule, among other things. Under the revised rule the assessment base changed from an insured institution's domestic deposits (minus certain allowable exclusions) to an insured institution's average consolidated total assets minus average tangible equity and certain other adjustments. In addition, the assessment rates were established in a range of 2.5 to 45 basis points, depending on the institution's capital category and supervisor sub-category, as previously described. For additional discussion, refer to "Results of Operations—Non-Interest Expense" in "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations."

In 2008 the FDIC created the Transaction Account Guarantee Program ("TAGP"), which provided participating banks with full deposit insurance coverage for non-interest-bearing transaction deposit accounts, regardless of dollar amount through December 31, 2012 (as subsequently extended). As of January 1, 2013, however, FDIC-insured financial

institutions' non-interest-bearing transaction deposit accounts are no longer fully-insured under this program. This development is not expected to have a material impact on the Bank or the deposit insurance premiums paid by the Bank.

**Transactions With Affiliates** Sections 23A and 23B of the Federal Reserve Act and FRB Regulation W govern transactions between an insured federal savings association, such as the Bank, and any of its affiliates, such as the Company. An affiliate is any company or entity that controls, is controlled by or is under common control with it. Sections 23A and 23B limit the extent to which an institution or a subsidiary may engage in "covered transactions" with any one affiliate to an amount equal to 10% of such savings association's capital stock and surplus, and limit all such transactions with all affiliates to 20% of such stock and surplus. The term "covered transaction" includes the making of loans, purchase of assets, issuance of guarantees, derivatives transactions, securities borrowing, and lending transactions to the extent that they result in credit exposure to an affiliate. Further, most loans by a savings association to any of its affiliates must be secured by specified collateral amounts. All such transactions must be on terms that are consistent with safe and sound banking practices and must be on terms that are at least as favorable to the savings association as those that would be provided to a non-affiliate. At December 31, 2012, the Company and Bank did not have any covered transactions.

**Acquisitions and Mergers** Under the federal Bank Merger Act, any merger of the Bank with or into another institution would require the approval of the OCC, or the primary federal regulator of the resulting entity if it is not an OCC-regulated institution. Refer also to "Regulation and Supervision of the Company—Acquisition of Bank Mutual Corporation," below.

**Prohibitions Against Tying Arrangements** Savings associations are subject to the prohibitions of 12 U.S.C. Section 1972 on certain tying arrangements. A savings association is prohibited, subject to exceptions, from extending credit to or offering any other service, or fixing or varying the consideration for such credit or service, on the condition that the customer obtain some additional service from the institution or its affiliates or not obtain services of a competitor.

**Uniform Real Estate Lending Standards** The federal banking agencies adopted uniform regulations prescribing standards for extensions of credit that are secured by liens on interests in real estate or are made to finance the construction of a building or other improvements to real estate. All insured depository institutions must adopt and maintain written policies that establish appropriate limits and standards for such extensions of credit. These policies must establish loan portfolio diversification standards, prudent underwriting standards that are clear and measurable, loan administration procedures, and documentation, approval and reporting requirements.

These lending policies must reflect consideration of the Interagency Guidelines for Real Estate Lending Policies that have been adopted by the federal bank regulators. These guidelines, among other things, require a depository institution to establish internal loan-to-value limits for real estate loans that are not in excess of specified supervisory limits, which generally vary and provide for lower loan-to-value limits for types of collateral that are perceived as having more risk, are subject to fluctuations in valuation, or are difficult to dispose. Although there is no supervisory loan-to-value limit for owner-occupied one- to four-family and home equity loans, the guidelines provide that an institution should require credit enhancement in the form of mortgage insurance or readily marketable collateral for any such loan with a loan-to-value ratio that equals or exceeds 90% at origination. The guidelines also clarify expectations for prudent appraisal and evaluation policies, procedures, and practices, and make other changes, in light of the Dodd-Frank Act and other recent federal statutory changes affecting appraisals.

**Community Reinvestment Act** Under the Community Reinvestment Act ("CRA"), any insured depository institution, including the Bank, must, consistent with its safe and sound operation, help meet the credit needs of its entire community, including low and moderate income neighborhoods. The CRA does not establish specific lending requirements or programs nor does it limit an institution's discretion to develop the types of products and services that it believes are best suited to its particular community. The CRA requires the OCC to assess the institution's record of meeting the credit needs of its community and to take such record into account in its evaluation of certain applications by such institution, including applications for additional branches and acquisitions.

Among other things, the CRA regulations contain an evaluation system that rates an institution based on its actual performance in meeting community needs. In particular, the evaluation system focuses on three tests: (i) a lending test, to evaluate the institution's record of making loans in its service areas, (ii) an investment test, to evaluate the institution's record of making community development investments, and (iii) a service test, to evaluate the institution's delivery of services through its branches, ATMs and other offices. The CRA requires the OCC to provide a written evaluation of the Bank's CRA performance utilizing a four-tiered descriptive rating system and

requires public disclosure of the CRA rating. The Bank received a “satisfactory” overall rating in its most recent CRA examination.

***Safety and Soundness Standards*** Each federal banking agency, including the OCC, has guidelines establishing general standards relating to internal controls, information and internal audit systems, loan documentation, credit underwriting, interest rate exposure, asset growth, asset quality, customer privacy, liquidity, earnings, and compensation and benefits. The guidelines require, among other things, appropriate systems and practices to identify and manage the risks and exposures specified in the guidelines. The guidelines also prohibit excessive compensation as an unsafe and unsound practice.

***Loans to Insiders*** A savings association’s loans to its executive officers, directors, any owner of more than 10% of its stock (each, “an insider”) and certain entities affiliated with any such person (an insider’s “related interest”) are subject to the conditions and limitations imposed by Section 22(h) of the Federal Reserve Act and the FRB’s Regulation O thereunder. Under these restrictions, the aggregate amount of the loans to any insider and related interests may not exceed the loans-to-one-borrower limit applicable to national banks. All loans by a savings association to all insiders and related interests in the aggregate may not exceed the savings association’s unimpaired capital and surplus. With certain exceptions, the Bank’s loans to an executive officer (other than certain education loans and residential mortgage loans) may not exceed \$100,000. Regulation O also requires that any proposed loan to an insider or a related interest be approved in advance by a majority of the Bank’s board of directors, without the vote of any interested director, if such loan, when aggregated with any existing loans to that insider and related interests, would exceed \$500,000. Generally, such loans must be made on substantially the same terms as, and follow credit underwriting procedures that are no less stringent than, those for comparable transactions with other persons and must not present more than a normal risk of collectability. There is an exception for extensions of credit pursuant to a benefit or compensation plan of a savings association that is widely available to employees that does not give preference to officers, directors, and other insiders. As of December 31, 2012, total loans to insiders were \$411,000 (including \$138,000 which relates to residential mortgages that have been sold in the secondary market).

### ***Regulation and Supervision of the Company***

***General*** The Company is a registered savings and loan holding company under federal law and is subject to regulation, supervision, and enforcement actions by the FRB. Among other things, this authority permits the FRB to restrict or prohibit activities that are determined to be a risk to the Bank and to monitor and regulate the Company’s capital and activities such as dividends and share repurchases that can affect capital. Under long-standing FRB policy, holding companies are expected to serve as a source of strength for their depository subsidiaries, and may be called upon to commit financial resources and support to those subsidiaries. The requirement that the Company act as a source of strength for the Bank, and the future capital requirements at the Company level (refer to “Regulatory Capital Requirements,” below), may affect the Company’s ability to pay dividends or make other distributions.

The Company may engage in activities permissible for a savings and loan holding company, a bank holding company, or a financial holding company, which generally encompass a wider range of activities that are financial in nature. The Company may not engage in any activities beyond that scope without the approval of the FRB.

Federal law prohibits a savings and loan holding company from acquiring control of another savings institution or holding company without prior written regulatory approval. With some exceptions, it also prohibits the acquisition or retention of more than 5% of the equity securities of a company engaged in activities that are not closely related to banking or financial in nature or acquiring an institution that is not federally-insured. In evaluating applications to acquire savings institutions, the regulator must consider the financial and managerial resources, future prospects of the institution involved, the effect of the acquisition on the risk to the insurance fund, the convenience and needs of the community and competitive factors.

***Regulatory Capital Requirements*** The Company is not currently required by the FRB to maintain minimum regulatory capital at the consolidated level. However, under the Dodd-Frank Act, the FRB is required to impose capital requirements on savings and loan holding companies effective in 2015. Management believes these capital requirements will be substantially the same as those currently required for bank holding companies. Management also believes the Company would have exceeded all regulatory minimum capital requirements as of December 31, 2012, had it been subject to bank holding company capital requirements as of that date.

***Proposed Regulatory Capital Requirements*** In 2012 the federal banking agencies issued proposed regulatory capital rules under Basel III, as previously described. The proposed rules, if adopted, are expected to have a significant

impact on the minimum regulatory requirements of regulated financial institutions such as the Company, to include accelerating the timing of the regulatory capital requirements for the Company at the consolidated level, as discussed in the previous paragraph. However, management believes the regulatory capital of the Company will exceed the minimum requirements established in the proposed rules and that the implementation or timing of the rules will not have a significant adverse impact on the financial condition, liquidity, or operations of the Company. It is not known at this time when the proposed rules will become effective or whether the proposed rules will be substantially modified prior to their becoming effective.

**Federal Securities Laws** The Company's common stock is registered with the SEC under the Securities Exchange Act of 1934. The Company is therefore subject to the information, proxy solicitation, insider trading restrictions and other requirements under the Securities Exchange Act. As a publicly-traded company, the Company is also subject to legislation intended to strengthen the securities markets and public confidence in them. Because some FRB accounting and governance regulations also refer to the SEC's regulations, the SEC rules may also affect the Bank.

**Acquisition of Bank Mutual Corporation** No person may acquire control of the Company without first obtaining the approval of such acquisition by the appropriate federal regulator. Currently, under the federal Change in Bank Control Act and the Savings and Loan Holding Company Act, any person, including a company, or group acting in concert, seeking to acquire 10% or more of the outstanding shares of the Company must, depending on the circumstances, obtain the approval of, and/or file a notice with the FRB. Also, any person or group acting in concert seeking to acquire more than 25% of the Company's common stock must obtain the prior approval of the FRB.

#### **Federal and State Taxation**

**Federal Taxation** The Company and its subsidiaries file a calendar year consolidated federal income tax return, reporting income and expenses using the accrual method of accounting. The federal income tax returns for the Company's subsidiaries have been examined and audited or closed without audit by the Internal Revenue Service for tax years prior to 2007.

**State Taxation** The Company and its subsidiaries are subject to combined reporting in the state of Wisconsin, which includes the Bank's out-of-state investment subsidiaries since 2009. For additional discussion regarding the impact of this change, refer to "Results of Operations—Income Tax Expense (Benefit)" in "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations." Also, refer to "Item 1A. Risk Factors," for additional discussion.

## **Item 1A. Risk Factors**

In addition to the discussion and analysis set forth in “Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations,” and the cautionary statements set forth in “Item 1. Business,” the following risk factors should be considered when evaluating the Company’s results of operations, financial condition, and outlook. These risk factors should also be considered when evaluating any investment decision with respect to the Company’s common stock.

### **The Global Credit Market Volatility and Weak Economic Conditions May Significantly Affect the Company’s Liquidity, Financial Condition, and Results of Operations**

Global financial markets continue to be unstable and unpredictable, and economic conditions have been relatively weak. Developments relating to the federal budget, federal borrowing authority, or other political issues could also negatively impact these markets, as could global developments such as the European sovereign debt crisis. Continued, and potentially increased, volatility, instability and weakness could affect the Company’s ability to sell investment securities and other financial assets, which in turn could adversely affect the Company’s liquidity and financial position. These factors could also affect the prices at which the Company could make any such sales, which could adversely affect its results of operations and financial condition. Conditions could also negatively affect the Company’s ability to secure funds or raise capital for acquisitions and other projects, which in turn, could cause the Company to use deposits or other funding sources for such projects.

In addition, the volatility of the markets and weakness of the economy could affect the strength of the Company’s customers or counterparties, their willingness to do business with, and/or their ability or willingness to fulfill their obligations to the Company, which could further affect the Company’s results of operations. Current conditions, including relatively high unemployment, weak corporate performance, and soft real estate markets, could negatively affect the volume of loan originations and prepayments, the value of the real estate securing the Company’s mortgage loans, and borrowers’ ability or willingness to repay loan obligations, all of which could adversely impact the Company’s results of operations and financial condition.

### **The Company’s Actual Loan Losses May Exceed its Allowance for Loan Losses, Which Could Have a Material Adverse Affect on the Company’s Results of Operations**

The Company has policies and procedures in place to manage its exposure to risk related to its lending operations. However, despite these practices, the Company’s loan customers may not repay their loans according to the terms of the loans and the collateral securing the payment of these loans may be insufficient to pay any remaining loan balance. Economic weakness, including high unemployment rates and lower values for the collateral underlying loans, may affect borrowers’ ability or willingness to repay their loan obligations that could lead to increased loan losses or provisions. As a result, the Company may experience significant loan losses, including losses that may exceed the amounts established in the allowance for loan losses, which could have a material adverse effect on its operating results and capital.

### **Further Declines in Real Estate Values May Continue to Adversely Affect Collateral Values and the Company’s Results of Operations**

The Company’s market areas have generally experienced lower real estate values, higher levels of residential and non-residential tenant vacancies, and weakness in the market for sale of new or existing properties, for both commercial and residential real estate. These developments could continue to negatively affect the value of the collateral securing the Company’s mortgage and related loans. That decrease in value could in turn lead to increased losses on loans in the event of foreclosures. Increased losses would affect the Company’s loan loss allowance and may cause it to increase its provision for loan losses resulting in a charge to earnings and capital.

### **Some of the Company’s Lending Activities Are Riskier than One- to Four-Family Real Estate Loans**

The Company has identified commercial real estate, commercial business, construction, and consumer loans as areas for lending emphasis and has augmented its personnel in recent periods to increase its penetration in the commercial lending market. While the Company is pursuing this lending diversification for the purpose of increasing net interest income, these types of loans historically have carried greater risk of payment default than residential real estate loans. As the volume of these types of loans increases, credit risk increases. In the event of continued substantial borrower

defaults and/or increased defaults resulting from these diverse types of lending, the Company's provision for loan losses would further increase and loans may be written off, and therefore, earnings would be reduced.

Further, as the portion of the Company's loans secured by the assets of commercial enterprises increases, the Company becomes increasingly exposed to environmental liabilities and compliance burdens. Even though the Company is subject to environmental requirements in connection with residential real estate lending, the possibility of liability increases in connection with commercial lending, particularly in industries that use hazardous materials and/or generate waste or pollution or that own property that was the subject of prior contamination. If the Company does not adequately assess potential environment risks, the value of the collateral it holds may be less than it expects, and it may be exposed to liability for remediation or other environmental compliance.

### **Regulators Are Becoming Increasingly Stringent, which may Affect the Company's Business and Results of Operations**

In addition to new laws and increasing amounts of regulation, the regulatory climate in the U.S., particularly for financial institutions, has become increasingly strict and stringent. As a consequence, regulatory activity affecting specific institutions has also increased in recent periods. Further, because the responsibility for regulating savings associations and their holding companies has transitioned to different regulatory agencies, the FRB and the OCC, these agencies may approach that regulation in different or stricter ways than the predecessor agency, which also could affect the Company's and the Bank's costs of compliance and results of operations.

### **The Bank's Ability to Pay Dividends to the Company Is Subject to Current and Potential Future Limitations That May Affect the Company's Ability to Pay Dividends to Its Shareholders and Repurchase Its Stock**

The Company is a separate legal entity from the Bank and engages in no substantial activities other than its ownership of the common stock of the Bank. Consequently, the Company's net income and cash flows are derived primarily from the Bank's operations and capital distributions. The availability of dividends from the Bank to the Company is limited by various statutes and regulations, including those of the OCC and FRB; as a result, it is possible, depending on the results of operations and the financial condition of the Bank and other factors, that the OCC and/or the FRB could restrict the payment by the Bank of dividends or other capital distributions or take other actions which could negatively affect the Bank's results and dividend capacity. The federal regulators have become increasingly stringent in their interpretation, application and enforcement of banks' capital requirements, which could affect the regulators' willingness to allow Bank dividends to the Company. If the Bank is required to reduce its dividends to the Company, or is unable to pay dividends at all, or the FRB separately does not allow the Company to pay dividends, the Company may not be able to pay dividends to its shareholders at existing levels or at all and/or may not be able to repurchase its common stock.

### **Future Events May Result in a Valuation Allowance Against the Company's Deferred Tax Asset Which May have a Significant Effect On the Company's Results of Operations and Financial Condition**

As of December 31, 2012, the Company's net deferred tax asset was \$34.2 million. Management evaluates this asset on an on-going basis to determine if a valuation allowance is required. Management determined that no valuation allowance was required to be recorded against the Company's net deferred tax asset as of December 31, 2012. This determination required significant management judgment based on positive and negative considerations. Such considerations included the Company's cumulative three-year net loss, the nature of the components of such cumulative loss, recent trends in earnings excluding one-time charges (such as the FHLB prepayment penalty in 2010 and the goodwill impairment in 2011), expectations for the Company's future earnings, the duration of federal and state net operating loss carryforward periods, and other factors. Future events or circumstances could result in conditions that differ significantly from management's current assessment of these positive and negative considerations, particularly as such relate to the Company's future earnings. Changes in these considerations could result in a significant valuation allowance being recorded against the Company's net deferred tax asset, which could have a significant effect on the Company's future results of operations and financial condition.

### **Recent and Future Legislation and Rulemaking in Response to Market and Economic Conditions May Significantly Affect the Company's Results of Operations and Financial Condition**

Instability, volatility, and failures in the credit and financial institutions markets in recent years have led regulators and legislators to consider and/or adopt proposals that will significantly affect financial institutions and their holding companies, including the Company. Legislation such as the Emergency Economic Stabilization Act of 2008, the

American Recovery and Reinvestment Act of 2009, and the Dodd-Frank Act of 2010, as well as programs such as the Troubled Assets Relief Program, were adopted. In addition, in 2012 the federal banking agencies issued proposed rules to implement certain revisions to regulatory capital requirements as specified by Basel III. Although designed to address capital and liquidity issues in the banking system, there can be no assurance as to the ultimate impact of these actions on financial markets, which could have a material, adverse effect on the Company's business, financial condition, results of operations, access to credit or the value of the Company's securities. Further legislative and regulatory proposals to reform the U.S. financial system would also affect the Company and the Bank.

The Dodd-Frank Act created the CFPB, which has broad rulemaking and enforcement authority with respect to entities, including financial institutions, that offer to consumers covered financial products and services. The CFPB is required to adopt rules identifying practices or acts that are unfair, deceptive or abusive relating to any customer transaction for a consumer financial product or service, or the offering of a consumer financial product or service. The full scope of the impact of this authority has not yet been determined as related rules have not all yet been adopted. The Company cannot yet determine the costs and limitations related to these additional regulatory requirements; however, the costs of compliance and the effect on its business may have a material adverse effect on the Company's operations and results.

Recently enacted laws, proposed acts, taxes and fees, or any other legislation or regulations ultimately enacted, could materially affect the Company, the Bank and their operations and profitability by imposing additional regulatory burdens and costs, imposing limits on fees and other sources of income, and otherwise more generally affecting the conduct of their business.

#### **The Interest Rate Environment May Have an Adverse Impact on the Company's Net Interest Income**

Volatile interest rate environments make it difficult for the Company to coordinate the timing and amount of changes in the rates of interest it pays on deposits and borrowings with the rates of interest it earns on loans and securities. In addition, volatile interest rate environments cause corresponding volatility in the demand by individuals and businesses for the loan and deposit products offered by the Company. These factors have a direct impact on the Company's net interest income, and consequently, its net income. Future interest rates could continue to be volatile and management is unable to predict the impact such volatility would have on the net interest income and profits of the Company.

#### **Changes in Market Interest Rates or Other Conditions May Have an Adverse Impact on the Fair Value of the Company's Available-for-Sale Securities, Shareholders' Equity, and Profits**

GAAP requires the Company to carry its available-for-sale securities at fair value on its balance sheet. Unrealized gains or losses on these securities, reflecting the difference between the fair market value and the amortized cost, net of its tax effect, are included as a component of shareholders' equity. When market rates of interest increase, the fair value of the Company's securities available-for-sale generally decreases and equity correspondingly decreases. When rates decrease, fair value generally increases and shareholders' equity correspondingly increases. However, due to significant disruptions in global financial markets, such as those which occurred in 2008, this usual relationship can be disrupted. Despite a generally declining interest rate environment since that time, certain of the Company's available-for-sale securities (specifically, its private-label CMOs) from time-to-time have experienced fair values substantially less than amortized cost. Management expects continued volatility in the fair value of its private-label CMOs and is not able to predict when or if the fair value of such securities will fully recover.

#### **Wisconsin Tax Developments Could Reduce the Company's Net Income**

Like many Wisconsin financial institutions, the Company has established non-Wisconsin subsidiaries that hold and manage investment assets and loans, the income from which had not previously been subject to Wisconsin tax prior to 2009. Under a Wisconsin Department of Revenue (the "Department") audit program specifically aimed at financial institutions' out-of-state investment subsidiaries, the Department has asserted the position that some or all of the income of the out-of-state subsidiaries in years prior to 2009 was taxable in Wisconsin. In 2010 the Department's auditor issued a Notice of Proposed Audit Report to the Bank which proposes to tax all of the income of the Bank's out-of-state investment subsidiaries for all periods that are still open under the statute of limitations, which includes tax years back to 1997. This is a preliminary determination made by the auditor and does not represent a formal assessment. The Bank's outside legal counsel has met with representatives of the Department to discuss, and object to, the auditor's proposed adjustments. The Department has requested further information to support the Company's position, which the Company has provided. The Company is awaiting a further response from the Department.

Management continues to believe that the Bank has reported income and paid Wisconsin taxes in prior periods in accordance with applicable legal requirements and the Department's long-standing interpretations of them and that the Bank's position will prevail in discussions with the Department, court proceedings, or other actions that may occur. Ultimately, however, an adverse resolution of these matters could result in additional Wisconsin tax obligations for prior periods, which could have a substantial negative impact on the Bank's earnings in the period such resolution is reached. The Bank may also incur further costs in the future to address and defend these issues.

### **Strong Competition Within the Company's Market Area May Affect Net Income**

The Company encounters strong competition both in attracting deposits and originating real estate and other loans. The Company competes with commercial banks, savings institutions, mortgage banking firms, credit unions, finance companies, mutual funds, insurance companies, and brokerage and investment banking firms. The Company's market area includes branches of several commercial banks that are substantially larger than the Company in terms of deposits and loans. In addition, tax-exempt credit unions operate in most of the Company's market area and aggressively price their products and services to a large part of the population. If competitors succeed in attracting business from the Company's customers, its deposits and loans could be reduced, which would likely affect earnings.

### **Developments in the Marketplace, Such as Alternatives to Traditional Financial Institutions, or Adverse Publicity Could Affect the Company's Ongoing Business**

Changes in the marketplace are allowing consumers to use alternative means to complete financial transactions that previously had been conducted through banks. For example, consumers can increasingly maintain funds in accounts other than bank deposits or through on-line alternatives, or complete payment transactions without the assistance of banks. Continuation or acceleration of these trends, including newly developing means of communications and technology, could cause consumers to utilize fewer of the Company's services, which could have a material adverse effect on its results.

Financial institutions such as the Company are increasingly under governmental, media and other scrutiny as to the conduct of their businesses, and potential issues and adverse developments (real and perceived) are receiving widespread media attention. If there were to be significant adverse publicity about the Company, that publicity could affect its reputation in the marketplace. If the Company's reputation is diminished, it could affect its business and results of operations as well as the price of the Company's common stock.

### **The Company Is Subject to Security Risks and Failures and Operational Risks Relating to the Use of Technology that Could Damage Its Reputation and Business**

Security breaches in the Company's internet, telephonic, or other electronic banking activities could expose it to possible liability and damage its reputation. Any compromise of the Company's security also could deter customers from using its internet banking services that involve the transmission of confidential information. The Company relies on standard internet and other security systems to provide the security and authentication necessary to effect secure transmission of data. These precautions may not protect the Company's systems from compromises or breaches of its security measures, which could result in damage to the Company's reputation and business and affect its results of operations.

Additionally, as a financial institution, the Company's business is data intensive. Beyond the inherent nature of a financial institution that requires it to process and track extremely large numbers of financial transactions and accounts, the Company is required to collect and maintain significant data about its customers. These operations require the Company to obtain and maintain technology and security-related systems that are mission critical to its business. The Company's failure to do so could significantly affect its ability to conduct business and its customers' confidence in it. Further, the Company outsources a large portion of its data processing to third parties. If these third party providers encounter technological or other difficulties or if they have difficulty in communicating with the Company, it will significantly affect the Company's ability to adequately process and account for customer transactions, which would significantly affect business operations.

Further, the technology affecting the financial institutions industry and consumer financial transactions is rapidly changing, with the frequent introduction of new products, services, and alternatives. The future success of the Company requires that it continue to adapt to these changes in technology to address its customers' needs. Many of the Company's competitors have greater technological resources to invest in these improvements. These changes could be costly to the

Company and if the Company does not continue to offer the services and technology demanded by the marketplace, this failure to keep pace with change could materially affect its business, financial condition, and results of operation.

#### **Future FDIC Increases in Deposit Insurance Premiums Could Increase the Company's Expenses**

In 2009 the FDIC significantly increased the initial base assessment rates paid by financial institutions for deposit insurance and imposed a special assessment. These measures were partly in response to the high level of bank failures which has caused an increase in FDIC resolution costs and a reduction in the deposit insurance fund. Effective in April 2011 the FDIC issued a new rule that changed the assessment base and risk-based assessment rates of all insured financial institutions. Although this latest development benefited the Company by lowering the total dollar amount of its FDIC deposit insurance premiums, future changes in the assessment base and/or rates, if any, may have an adverse affect on the earnings of the Company.

#### **The Company's Ability to Grow May Be Limited if It Cannot Make Acquisitions**

The Company will continue to seek to expand its banking franchise by growing internally, acquiring other financial institutions or branches, acquiring other financial services providers, and opening new offices. The Company's ability to grow through selective acquisitions of other financial institutions or branches will depend on successfully identifying, acquiring, and integrating those institution or branches. The Company has not made any acquisitions in recent years, as management has not identified acquisitions for which it was able to reach an agreement on terms management believed were appropriate and/or that met its acquisition criteria. The Company cannot provide any assurance that it will be able to generate internal growth, identify attractive acquisition candidates, make acquisitions on favorable terms, or successfully integrate any acquired institutions or branches.

#### **The Company Depends on Certain Key Personnel and the Company's Business Could Be Harmed by the Loss of Their Services or the Inability to Attract Other Qualified Personnel**

The Company's success depends in large part on the continued service and availability of its management team, and on its ability to attract, retain and motivate qualified personnel. The management team has been augmented to attempt to increase the Company's penetration into the commercial lending market. The Company may need to attract further talent in the future. The competition for these individuals can be significant, and the loss of key personnel could harm the Company's business. The Company cannot provide assurances that it will be able to retain existing key personnel or attract additional qualified personnel.

#### **If the Company is Unable to Maintain Effective Internal Control Over Its Financial Reporting, Investors Could Lose Confidence in the Reliability of Its Financial Statements, Which Could Result in a Reduction in the Value of Its Common Stock**

Under the Sarbanes-Oxley Act, public companies must include a report of management regarding companies' control over financial reporting in their annual reports and that report must contain an assessment by management of the effectiveness of the companies' internal control over financial reporting. In addition, the independent registered public accounting firm that audits a company's financial statements must attest to and report on the effectiveness of the company's internal control over financial reporting.

If the Company is unable to maintain the required effective internal control over financial reporting, including in connection with regulatory changes and/or changes in accounting rules and standards that apply to it, this could lead to a failure to meet its reporting obligations to the SEC. Such a failure in turn could result in an adverse reaction to the Company in the marketplace or a decline in value of the Company's common stock, due to a loss of confidence in the reliability of the Company's financial statements.

#### **The Cost to Provide Employee Healthcare Insurance and/or Benefits Could Increase in the Future**

The Affordable Care Act (the "ACA"), which was adopted in 2010 and is being phased in over several years, significantly affects the provision of both health care services and benefits in the United States. It is possible that ACA the will negatively affect the Company's cost of providing health insurance and/or benefits, and may also impact various other aspects of the Company's business. While the ACA did not have a material impact on the Company in 2012, 2011 or 2010, the Company is continuing to assess the possible future impact of the ACA on its health care benefit costs.

### **Item 1B. Unresolved Staff Comments**

None.

### **Item 2. Properties**

The Company and its subsidiaries conduct their business through an executive office and 76 banking offices, which had an aggregate net book value of \$48.1 million as of December 31, 2012, excluding furniture, fixtures, and equipment. As of December 31, 2012, the Company owned the building and land for 69 of its property locations and leased the space for eight.

The Company also owns 15 acres of developed land in a suburb of Milwaukee, Wisconsin, through its MC Development subsidiary, as well as approximately 300 acres of undeveloped land in another community located near Milwaukee through MC Development's 50% ownership in Arrowood Development LLC. The net book value of these parcels of land was \$5.4 million at December 31, 2012.

### **Item 3. Legal Proceedings**

The Company is not involved in any pending legal proceedings other than routine legal proceedings occurring in the ordinary course of business. Management believes that these routine legal proceedings, in the aggregate, are immaterial to the Company's financial condition, results of operations, and cash flows. Refer also to "Item 1A. Risk Factors—Wisconsin Tax Developments Could Reduce the Company's Net Income" regarding certain Wisconsin income tax developments.

### **Item 4. Mine Safety Disclosures**

Not applicable.

## Part II

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

The common stock of the Company is traded on The NASDAQ Global Select Market under the symbol BKMU.

As of February 28, 2013, there were 46,420,084 shares of common stock outstanding and approximately 8,800 shareholders of record.

The Company paid a total cash dividend of \$0.05 per share in 2012. A cash dividend of \$0.02 per share was paid on March 1, 2013, to shareholders of record on February 15, 2013. For additional discussion relating to the Company's dividends, refer to "Financial Condition—Shareholders' Equity" in "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations." The payment of dividends in the future is discretionary with the Company's board of directors and will depend on the Company's operating results, financial condition, and other considerations. Interest on deposits will be paid prior to payment of dividends on the Company's common stock. Refer also to "Item 1. Business—Regulation and Supervision" for information relating to regulatory limitations on the Company's payment of dividends to shareholders, as well as the payment of dividends by the Bank to the Company, which in turn could affect the payment of dividends by the Company.

The high and low trading prices of the Company's common stock from January 1, 2011, through December 31, 2012, by quarter, and the dividends paid in each quarter, were as follows:

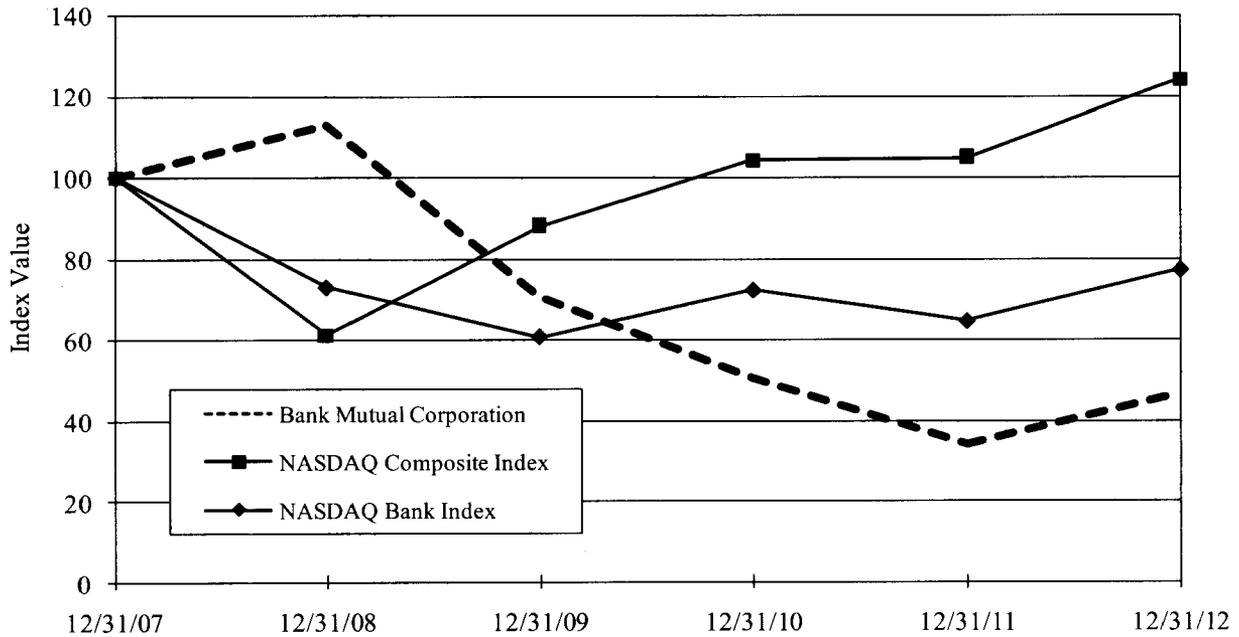
	2012 Stock Prices		2011 Stock Prices		Cash Dividends Paid	
	High	Low	High	Low	2012	2011
1 <sup>st</sup> Quarter	\$4.45	\$3.15	\$5.08	\$3.81	\$0.01	\$0.03
2 <sup>nd</sup> Quarter	4.41	3.43	4.28	3.54	0.01	0.01
3 <sup>rd</sup> Quarter	4.69	3.95	3.91	2.57	0.01	0.01
4 <sup>th</sup> Quarter	4.64	4.03	3.68	2.43	0.02	0.01
				Total	<u>\$0.05</u>	<u>\$0.06</u>

From January 1, 2013, to February 28, 2013, the trading price of the Company's common stock ranged between \$4.43 to \$5.88 per share, and closed this period at \$5.72 per share.

The Company did not repurchase any of its common stock during 2012 and the Company's board of directors has not authorized a new stock repurchase program. For additional discussion relating to the Company's repurchase of its common stock, refer to "Item 1. Business—Shareholders' Equity" and "Item 1. Business—Regulation and Supervision."

Set forth below is a line graph comparing the cumulative total shareholder return on Company common stock, based on the market price of the common stock and assuming reinvestment of cash dividends, with the cumulative total return of companies on the NASDAQ Stock Market U.S. Index ("NASDAQ Composite Index") and the NASDAQ Stock Market Bank Index. The graph assumes that \$100 was invested on December 31, 2007, in Company common stock and each of those indices.

Total Return Performance



Index	Period Ending					
	12/31/07	12/31/08	12/31/09	12/31/10	12/31/11	12/31/12
Bank Mutual Corporation	100.00	112.94	70.63	50.37	34.04	46.61
NASDAQ Composite Index	100.00	61.17	87.93	104.13	104.69	123.85
NASDAQ Bank Index	100.00	72.91	60.66	72.13	64.51	77.18

## Item 6. Selected Financial Data

The following table provides selected financial data for the Company for its past five fiscal years. The data is derived from the Company's audited financial statements, although the table itself is not audited. The following data should be read together with the Company's consolidated financial statements and related notes and "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations."

	At December 31				
	2012	2011	2010	2009	2008
Selected financial condition data:	(Dollars in thousands, except number of shares and per share amounts)				
Total assets	\$2,418,264	\$2,498,484	\$2,591,818	\$3,512,064	\$3,489,689
Loans receivable, net	1,402,246	1,319,636	1,323,569	1,506,056	1,829,053
Loans held-for-sale	10,739	19,192	37,819	13,534	19,030
Investment securities available-for-sale	—	—	228,023	614,104	419,138
Mortgage-related securities available-for-sale	550,185	781,770	435,234	866,848	850,867
Mortgage-related securities held-to-maturity	157,558	—	—	—	—
Foreclosed properties and repossessed assets	13,961	24,724	19,293	17,689	4,768
Goodwill	—	—	52,570	52,570	52,570
Mortgage servicing rights, net	6,821	7,401	7,769	6,899	3,703
Deposit liabilities	1,867,899	2,021,663	2,078,310	2,137,508	2,128,277
Borrowings	210,786	153,091	149,934	906,979	907,971
Shareholders' equity	271,853	265,771	312,953	402,477	399,611
Tangible shareholders' equity (1)	271,853	265,771	260,383	349,907	347,041
Number of shares outstanding, net of treasury stock	46,326,484	46,228,984	45,769,443	46,165,635	47,686,759
Book value per share	\$5.87	\$5.75	\$6.84	\$8.72	\$8.38
Tangible shareholders' equity per share (1)	\$5.87	\$5.75	\$5.69	\$7.58	\$7.28
	For the Year Ended December 31				
	2012	2011	2010	2009	2008
Selected operating data:	(Dollars in thousands, except per share amounts)				
Total interest income	\$83,022	\$89,345	\$112,569	\$151,814	\$177,556
Total interest expense	21,641	26,756	66,276	83,784	104,191
Net interest income	61,381	62,589	46,293	68,030	73,365
Provision for loan losses	4,545	6,710	49,619	12,413	1,447
Total non-interest income	29,259	23,158	40,603	31,681	17,881
Total non-interest expense (2)	76,057	124,900	159,825	68,155	63,550
Income (loss) before income taxes	10,038	(45,863)	(122,548)	19,143	26,250
Income tax expense (benefit)	3,336	1,752	(49,909)	5,418	9,094
Net income (loss) before non-controlling interest	6,702	(47,615)	(72,639)	13,725	17,155
Net loss (income) attributable to non-controlling interest	52	50	(1)	—	1
Net income (loss)	\$6,754	\$(47,565)	\$(72,640)	\$13,725	\$17,156
Earnings (loss) per share-basic	\$0.15	\$(1.03)	\$(1.59)	\$0.29	\$0.36
Earnings (loss) per share-diluted	\$0.15	\$(1.03)	\$(1.59)	\$0.29	\$0.35
Cash dividends paid per share	\$0.05	\$0.06	\$0.20	\$0.34	\$0.36

(1) This is a non-GAAP measure. Tangible shareholders' equity is total shareholders' equity minus goodwill.

(2) Total non-interest expense in 2011 includes a goodwill impairment of \$52.6 million and in 2010 includes \$89.3 million in loss on early repayment of FHLB borrowings.

	At or For the Year Ended December 31				
	2012	2011	2010	2009	2008
Selected financial ratios:					
Net interest margin (3)	2.67%	2.76%	1.47%	2.09%	2.21%
Net interest rate spread	2.57	2.64	1.26	1.82	1.85
Return on average assets	0.27	(1.87)	(2.12)	0.39	0.48
Return on average shareholders' equity	2.50	(16.37)	(18.47)	3.40	4.15
Efficiency ratio (4)	84.04	85.07	99.36	73.32	68.77
Non-interest expense as a percent of adjusted average assets (5)					
Shareholders' equity to total assets	3.03	2.84	2.06	1.95	1.80
Tangible shareholders' equity to adjusted total assets (6)	11.24	10.64	12.07	11.39	11.45
Selected asset quality ratios:					
Non-performing loans to loans receivable, net	1.84%	5.69%	9.29%	2.83%	1.81%
Non-performing assets to total assets	1.64	4.00	5.49	1.72	1.08
Allowance for loan losses to non-performing loans	83.64	37.17	39.03	39.99	36.89
Allowance for loan losses to total loans receivable, net	1.54	2.12	3.63	1.13	0.67
Charge-offs to average loans	0.78	1.96	1.26	0.45	0.05

(3) Net interest margin is calculated by dividing net interest income by average earnings assets.

(4) Efficiency ratio is calculated by dividing non-interest expense (excluding goodwill impairment and loss on early repayment of FHLB borrowings) by the sum of net interest income and non-interest income (excluding gains and losses on investments).

(5) The ratio in 2011 excludes the impact of the goodwill impairment and in 2010 excludes the impact of the prepayment penalty on the early repayment of FHLB borrowings.

(6) This is a non-GAAP measure. The ratio is calculated by dividing total shareholders' equity less intangible assets (net of deferred taxes) divided by total assets less intangible assets (net). Intangible assets consist of goodwill and other intangible assets. Deferred taxes have been established only on other intangible assets and are immaterial in amount.

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

The discussion and analysis in this section should be read in conjunction with “Item 8. Financial Statements and Supplementary Data,” and “Item 7A. Quantitative and Qualitative Disclosures about Market Risk,” as well as “Item 1. Business” and “Item 1A. Risk Factors.”

### **Results of Operations**

**Overview** The Company’s net income (loss) for the years ended December 31, 2012, 2011, and 2010, was \$6.8 million, \$(47.6) million, and \$(72.6) million, respectively. Diluted earnings (loss) per share during these periods were \$0.15, \$(1.03), and \$(1.59), respectively.

The Company’s net income in 2012 was impacted by the following favorable developments compared to 2011:

- a one-time \$52.6 million loss in 2011 on the impairment of goodwill;
- a \$7.2 million or 121% increase in gain on loan sales activities; and
- a \$2.2 million or 32.3% decrease in provision for loan losses.

These favorable developments were partially offset by the following unfavorable developments in 2012 compared to 2011:

- a \$3.5 million or 8.9% increase in compensation-related costs;
- a \$1.5 million unfavorable change in net loan-related fees and servicing revenue;
- a \$1.2 million or 1.9% decrease in net interest income; and
- a \$1.6 million or 90.4% increase in income tax expense.

The Company’s net loss in 2011 was impacted by the following unfavorable developments compared to 2010:

- a one-time \$52.6 million loss in 2011 on the impairment of goodwill;
- a \$14.9 million or 93.0% decrease in gain on investments;
- a \$2.8 million or 7.9% increase in compensation-related expenses;
- a \$2.6 million or 30.4% decrease in gain on loan sales activities; and
- a \$51.7 million change in income taxes from a benefit of \$49.9 million in 2010 to an expense of \$1.8 million in 2011.

These unfavorable developments were partially offset by the following favorable developments in 2011 compared to 2010:

- a one-time \$89.3 million loss in 2010 on early repayment of FHLB borrowings;
- a \$42.9 million or 86.5% decrease in provision for loan losses;
- a \$16.3 million or 35.2% increase in net interest income; and
- a \$1.2 million or 14.6% decrease in net losses and expenses on foreclosed real estate.

The following paragraphs discuss these developments in greater detail, as well as other changes in the components of net income (loss) during the years ended December 31, 2012, 2011, and 2010.

**Net Interest Income** Net interest income declined by \$1.2 million or 1.9% during the year ended December 31, 2012, compared to 2011. This decline was primarily attributable to a decrease in the Company’s net interest margin, which

was 2.67% in 2012 compared to 2.76% in 2011. This decline was primarily the result of a lower interest rate environment in 2012, which reduced the return on the Company's earning assets more than the cost of its funding sources. Contributing to the reduction in the cost of the Company's funding sources in 2012 was its repayment of \$100.0 million in high-cost borrowings from the FHLB of Chicago that matured during the period.

The impact of a lower net interest margin in 2012 was partially offset by the favorable impact of higher average earning assets during the year. In 2012 the Company purchased \$158.9 million in held-to-maturity securities that were funded by term borrowings from the FHLB of Chicago (for additional discussion refer to "Financial Condition—Mortgage-Related Securities Held-to-Maturity"). In addition, during 2012 average total loans increased by \$21.9 million or 1.6% compared to 2011.

Net interest income increased by \$16.3 million or 35.2% during the year ended December 31, 2011, compared to 2010. This increase was primarily attributable to an improvement in the Company's net interest margin, which increased to 2.76% in 2011 from 1.47% in 2010. This improvement was primarily the result of the Company's early repayment of \$756.0 million in high-cost borrowings from the FHLB of Chicago in December 2010, as described below. The repayment resulted in a significant decline in the average cost of interest-bearing liabilities in 2011 compared to 2010. Also contributing to the improvement in the Company's net interest margin in 2011 was a decline in its average cost of deposits. The Company's average cost of deposits declined by 40 basis points in 2011 compared to 2010. Also contributing to the improvement in the net interest margin in 2011 was a 38 basis point improvement in the yield on interest-earning assets compared to the previous year. This improvement was caused by a favorable change in the mix of earning assets from lower-yielding assets, such as overnight investments and short-term securities, to higher-yielding assets, such as loans receivable. Partially offsetting the favorable impact of this improved asset mix was a decrease in the average yield on loans receivable and available-for-sale securities in 2011 compared to 2010. These decreases were caused by a declining interest rate environment that resulted in lower yields on these assets in 2011. In addition, the Company sold a substantial number of higher-yielding securities in 2010 at gains, as noted below, which reduced the overall yield on its securities portfolio in 2011 compared to 2010.

In December 2010 the Company repaid \$756.0 million in fixed-rate borrowings from the FHLB of Chicago prior to the stated maturities of the borrowings. As a result of this prepayment, the Company recognized a one-time charge of \$89.3 million in 2010. At the time, the borrowings had an average remaining maturity of six years and a weighted-average interest cost of 4.17%. The Company considered it prudent to repay these borrowings prior to their stated maturities due to the lack of acceptable investment or lending alternatives that could provide sufficient yield to justify the high cost of the borrowings.

The following table presents certain details regarding the Company's average balance sheet and net interest income for the periods indicated. The tables present the average yield on interest-earning assets and the average cost of interest-bearing liabilities. The yields and costs are derived by dividing income or expense by the average balance of interest-earning assets or interest-bearing liabilities, respectively, for the periods shown. The average balances are derived from daily balances over the periods indicated. Interest income includes fees, which are considered adjustments to yields. Net interest spread is the difference between the yield on interest-earning assets and the rate paid on interest-bearing liabilities. Net interest margin is derived by dividing net interest income by average interest-earning assets. No tax equivalent adjustments were made since the Company does not have any tax exempt investments.

	Year Ended December 31								
	2012			2011			2010		
	Average Balance	Interest Earned/ Paid	Avg. Yield/ Cost	Average Balance	Interest Earned/ Paid	Avg. Yield/ Cost	Average Balance	Interest Earned/ Paid	Avg. Yield/ Cost
(Dollars in thousands)									
Assets:									
Interest-earning assets:									
Loans receivable, net (1)	\$1,389,313	\$65,478	4.71%	\$1,367,450	\$69,936	5.11%	\$1,478,433	\$79,266	5.36%
Mortgage-related securities	792,989	17,309	2.18	656,343	16,374	2.49	589,070	17,445	2.96
Investment securities (2)	25,443	73	0.29	156,793	2,877	1.83	840,424	15,428	1.84
Interest-earning deposits	91,801	162	0.18	84,505	158	0.19	250,909	430	0.17
Total interest-earning assets	2,299,546	83,022	3.61	2,265,091	89,345	3.94	3,158,836	112,569	3.56
Non-interest-earning assets	210,599			278,872			266,270		
Total average assets	<u>\$2,510,145</u>			<u>\$2,543,963</u>			<u>\$3,425,106</u>		
Liabilities and equity:									
Interest-bearing liabilities:									
Savings deposits	\$217,255	63	0.03	\$212,644	78	0.04	\$208,544	104	0.05
Money market accounts	434,549	716	0.16	405,033	1,696	0.42	347,906	2,075	0.60
Interest-bearing demand accounts	219,038	51	0.02	199,909	85	0.04	200,292	107	0.05
Certificates of deposit	954,047	13,825	1.45	1,069,708	17,709	1.66	1,234,411	26,320	2.13
Total deposit liabilities	1,824,889	14,655	0.80	1,887,294	19,568	1.04	1,991,153	28,606	1.44
Advance payment by borrowers for taxes and insurance	21,141	2	0.01	19,551	5	0.03	19,606	6	0.03
Borrowings	227,573	6,984	3.07	156,521	7,183	4.59	871,212	37,664	4.32
Total interest-bearing liabilities	2,073,603	21,641	1.04	2,063,366	26,756	1.30	2,881,971	66,276	2.30
Non-interest-bearing liabilities:									
Non-interest-bearing deposits	130,734			110,784			96,370		
Other non-interest-bearing liabilities	35,208			79,314			53,506		
Total non-interest-bearing liabilities	165,942			190,098			149,876		
Total liabilities	2,239,545			2,253,464			3,031,847		
Total equity	270,600			290,499			393,259		
Total average liabilities and equity	<u>\$2,510,145</u>			<u>\$2,543,963</u>			<u>\$3,425,106</u>		
Net interest income and net interest rate spread		\$61,381	2.57%		\$62,589	2.64%		\$46,293	1.26%
Net interest margin			2.67%			2.76%			1.47%
Average interest-earning assets to interest-bearing liabilities			1.11x			1.10x			1.10x

- (1) For the purposes of these computations, non-accruing loans and loans held-for-sale are included in the average loans outstanding.
- (2) FHLB of Chicago stock is included in investment securities.

The following tables present the extent to which changes in interest rates and changes in the volume of interest-earning assets and interest-bearing liabilities have affected the Company's interest income and interest expense during the periods indicated. Information is provided in each category with respect to the change attributable to change in volume (change in volume multiplied by prior rate), the change attributable to change in rate (change in rate multiplied by prior volume), and the net change. The change attributable to the combined impact of volume and rate has been allocated proportionately to the change due to volume and the change due to rate.

	Year Ended December 31, 2012, Compared to Year Ended December 31, 2011		
	Increase (Decrease)		
	Volume	Rate	Net
Interest-earning assets:		(Dollars in thousands)	
Loans receivable	\$1,084	\$(5,542)	\$(4,458)
Mortgage-related securities	3,129	(2,194)	935
Investment securities	(1,395)	(1,409)	(2,804)
Interest-earning deposits	13	(9)	4
Total interest-earning assets	2,831	(9,154)	(6,323)
Interest-bearing liabilities:			
Savings deposits	6	(21)	(15)
Money market deposits	116	(1,096)	(980)
Interest-bearing demand deposits	7	(41)	(34)
Certificates of deposit	(1,808)	(2,076)	(3,884)
Advance payment by borrowers for taxes and insurance	—	(3)	(3)
Borrowings	2,637	(2,836)	(199)
Total interest-bearing liabilities	958	(6,073)	(5,115)
Net change in net interest income	\$1,873	\$(3,081)	\$(1,208)

	Year Ended December 31, 2011, Compared to Year Ended December 31, 2010		
	Increase (Decrease)		
	Volume	Rate	Net
Interest-earning assets:		(Dollars in thousands)	
Loans receivable	\$(5,740)	\$(3,590)	\$(9,330)
Mortgage-related securities	1,882	(2,953)	(1,071)
Investment securities	(12,511)	(40)	(12,551)
Interest-earning deposits	(311)	39	(272)
Total interest-earning assets	(16,680)	(6,544)	(23,224)
Interest-bearing liabilities:			
Savings deposits	(5)	(21)	(26)
Money market deposits	307	(686)	(379)
Interest-bearing demand deposits	—	(22)	(22)
Certificates of deposit	(3,216)	(5,395)	(8,611)
Advance payment by borrowers for taxes and insurance	—	(1)	(1)
Borrowings	(32,668)	2,187	(30,481)
Total interest-bearing liabilities	(35,582)	(3,938)	(39,520)
Net change in net interest income	\$18,902	\$(2,606)	\$16,296

**Provision for Loan Losses** The Company's provision for loan losses was \$4.5 million, \$6.7 million, and \$49.6 million during the years ended December 31, 2012, 2011, and 2010, respectively. In 2012 the Company recorded loss provisions of \$6.3 million against a number of multi-family, commercial real estate, and business loan relationships, as well as residential and consumer loans. The losses on these loans were based on updated independent appraisals and/or internal management evaluations of the collateral that secures the loan, as well as management's knowledge of current market conditions. This development was partially offset by \$1.8 million in loss recaptures related to certain non-performing loans that paid off during the period and to recoveries related to previously charged-off loans.

In 2011 the Company recorded \$11.8 million in loss provisions against a number of larger multi-family, commercial real estate, and business loan relationships, as well as certain smaller residential and consumer loans. The losses on these loans were based on updated independent appraisals and/or internal management evaluations of the collateral that secures the loan, as well as management's knowledge of current market conditions. In addition, during 2011

the Company recorded approximately \$2.4 million in additional loss provisions that reflected management's general concerns at the time related to continued economic weakness, elevated levels of unemployment, depressed real estate values, and the internal downgrades of certain loans. These developments were partially offset by \$7.5 million in loss recaptures on loans that were paid-off during the period, were upgraded to performing status, or improved in performance and/or prospects.

In 2010 the Company noted increased vacancy rates, declining rents, and/or delays in unit sales for many of the properties that secure Company's loans. In many instances, management's observations included loans that borrowers and/or loan guarantors had managed to keep current despite underlying difficulties with the collateral properties. In view of those developments and their expected continuation, as well as an increasingly strict regulatory environment, management concluded in 2010 that the probability of a number of its loans being collateral dependent had increased, which resulted in a significant increase in provision for loan losses. In 2010 the Company recorded \$31.0 million in loss provisions against 34 larger loan relationships aggregating \$91.6 million. These loans were secured by commercial real estate, multi-family real estate, undeveloped land, and, in the case of a few commercial business loans, certain other non-real estate assets. During 2010 the Company also recorded \$10.0 million in loss provisions on a large number of smaller commercial real estate, multi-family real estate, and commercial business loan relationships, as well as \$1.3 million in loss provisions on one- to four-family loans and consumer loans. In general, these losses were based on updated independent appraisals that were received during 2010, but in some cases were based on management judgment. Finally, during 2010 the Company recorded \$7.3 million in additional loss provisions that reflected management's general concerns at the time related to declines in commercial real estate values, weak economic conditions, and high levels of unemployment.

The Company's provision for loan losses was substantially lower in 2012 and 2011 than it was in 2010. This trend is directionally consistent with declines in the Company's non-performing loans and classified loans, as described in "Financial Condition—Asset Quality," below, and is consistent with general trends in the banking industry. It should be noted, however, that the Company's loan portfolio continues to be impacted by slow economic growth, persistent unemployment, and low real estate values. These conditions are particularly challenging for borrowers whose loans are secured by commercial real estate, multi-family real estate, and land. As such, there can be no assurances that non-performing loans and/or classified loans will continue to trend lower in future periods or that the Company's provision for loan losses will not vary considerably in future periods. Refer to "Item 1. Business—Asset Quality," above, for additional discussion related to the Company's policies and procedures related to its provision for loan losses, allowance for loan losses, and asset quality.

**Non-Interest Income** Total non-interest income for the years ended December 31, 2012, 2011, and 2010, was \$29.3 million, \$23.2 million, and \$40.6 million, respectively. The following paragraphs discuss the principal components of non-interest income and primary reasons for their changes from 2011 to 2012, as well as 2010 to 2011.

Service charges on deposits were \$6.9 million, \$6.4 million, and \$6.1 million in 2012, 2011, and 2010, respectively. Management attributes the improvements in 2012 and 2011 to an increase in the Company's average checking accounts, which increased by \$39.1 million or 11.8% in 2012 compared to 2011 and \$14.0 million or 4.7% in 2011 compared to 2010. In addition, enhancements in recent periods to the Company's commercial deposit products and services generated increased fee revenue in these years, particularly related to treasury management services.

Brokerage and insurance commissions were \$3.0 million, \$2.8 million, and \$3.1 million for the years ended December 31, 2012, 2011, and 2010, respectively. This revenue item consists of commissions earned on sales of tax-deferred annuities, mutual funds, and certain other securities, as well as personal and business insurance products. Commission revenue in 2012 benefited from a lower interest rate environment that encouraged customers to purchase tax-deferred annuities due to higher returns compared to deposit-related products. Commission revenue in 2010 benefited from favorable trends in equity markets in the first half of that year, which resulted in increased revenue from sales of mutual funds and other equity investments relative to 2012 and 2011.

Net loan-related fees and servicing revenue was a loss of \$1.9 million and \$402,000 in 2012 and 2011, respectively, and income of \$103,000 in 2010. The following table presents the primary components of net loan-related fees and servicing revenue for the periods indicated:

	Year Ended December 31		
	2012	2011	2010
	(Dollars in thousands)		
Gross servicing fees	\$2,826	\$2,718	\$2,584
MSR amortization	(3,904)	(2,747)	(3,277)
MSR valuation (loss) recovery	(1,528)	(862)	281
Loan servicing revenue, net	(2,606)	(891)	(412)
Other loan fee income	695	489	515
Loan-related fees and servicing revenue, net	\$(1,911)	\$(402)	\$103

Gross servicing fees increased in 2012 and 2011 due to an increase in the amount of loans the Company services for third-party investors. During 2012, 2011, and 2010, the Company serviced an average of \$1.13 billion, \$1.09 billion, and \$1.03 billion, respectively, in loans for third-party investors. Loans serviced for third-party investors have increased the past two years due to increased sales of loans by the Company in the secondary market, as described below. The Company typically retains the servicing on these loans. Related amortization of MSR's was higher in the 2012 and 2010 periods due to generally lower market interest rates for one- to four-family mortgage loans in those periods, which resulted in increased loan prepayments and faster amortization of the MSR's in such years.

Loan-related fees and servicing revenue is also impacted by changes in the valuation allowance that is established against MSR's. The change in this allowance is recorded as a recovery or charge, as the case may be, in the period in which the change occurs. In 2012 the valuation allowance increased by \$1.5 million due principally to a decline in market interest rates, which resulted in increased loan prepayment expectations. The valuation allowance increased by \$862,000 in 2011 due to a decline in market interest rates during the last few months of that year.

The valuation of MSR's, as well as the periodic amortization of MSR's, is significantly influenced by the level of market interest rates and loan prepayments. If market interest rates for one- to four-family loans increase and/or actual or expected loan prepayment expectations decrease in future periods, the Company could recover all or a portion of its previously established allowance on MSR's, as well as record reduced levels of MSR amortization expense. Alternatively, if interest rates continue to decrease and/or prepayment expectations increase, the Company could potentially record additional charges to earnings related to increases in the valuation allowance on its MSR's. In addition, amortization expense could increase further due to likely increases in loan prepayment activity. Lower interest rates also typically cause an increase in actual mortgage loan prepayment activity, which generally results in an increase in the amortization of MSR's.

Net gains on loan sales activities were \$13.2 million, \$6.0 million, and \$8.6 million during the years ended December 31, 2012, 2011, and 2010, respectively. The Company's policy is to sell substantially all of its fixed-rate, one- to four-family mortgage loan originations in the secondary market. During 2012, 2011, and 2010 sales of one- to four-family mortgage loans were \$454.6 million, \$292.7 million, and \$409.4 million, respectively. Loan sales were elevated in the 2012 and 2010 periods as a result of generally lower market interest rates for one- to four-family mortgage loans in those periods, which encouraged a larger number of borrowers to refinance higher-rate loans into lower-rate loans during those years. Also contributing to the increase in gains on sales of loans in 2012 was an increase in the Company's average gross profit margin on the sales of loans. In 2012 the average gross profit margin was 2.91% compared to 2.04% and 2.09% in 2011 and 2010, respectively. Management attributed this improvement to the burden that increased consumer demand has placed on the loan production capacity of the mortgage banking industry as a whole, which has caused gross profit margins to increase.

Market interest rates for one- to four-family mortgage loans have increased modestly in recent weeks and the pace of the Company's loan originations and sales has diminished compared to 2012. In addition, the Company has experienced a decline in its gross profit margin on individual loan sales in recent months as production capacity within the mortgage banking industry has become less constrained. Absent a further decline in market interest rates for one- to four-family mortgage in 2013, management believes the Company's gains on sales of loans will be substantially lower in 2013 than they were in 2012. However, management believes the impact of lower gains on sales will be partially offset by continued recovery of previously established MSR valuation allowances, as previously noted, as well as lower MSR amortization. However, there can be no assurances.

Net gain on sales of investments in 2012, 2011, and 2010 was \$543,000, \$1.1 million, and \$16.0 million, respectively. In 2012 the Company sold \$20.4 million in mortgage-related securities to provide additional liquidity to fund the repayment of \$100.0 million in borrowings from the FHLB of Chicago that matured in third quarter of the year. In 2011 the Company sold its remaining investment in a mutual fund that management did not expect would perform well in future periods. In 2010 the Company sold mortgage-related and certain other securities to provide liquidity to fund the repayment of \$756.0 million FHLB of Chicago borrowings in that year, as previously described.

The Company's operating results in 2012 and 2011 included \$400,000 and \$389,000 in net OTTI charges, respectively. These losses consisted of the credit portion of the total OTTI loss related to the Company's investment in certain private-label CMOs rated less than investment grade. Management attributes the net OTTI losses in these periods to low real estate values for residential properties on a nationwide basis. None of the Company's remaining private-label CMOs were deemed to be other-than-temporarily impaired as of December 31, 2012. However, the collection of the amounts due on private-label CMOs is subject to numerous factors outside of the Company's control and a future determination of OTTI could result in additional losses being recorded through earnings in future periods. As of December 31, 2012, the Company's total investment in private-label CMOs was \$50.6 million, of which \$35.9 million was rated less than investment grade. Refer to "Financial Condition—Available-for-Sale Securities," below, for additional discussion.

The Company's operating results in 2010 included a \$700,000 loss on a \$2.6 million investment in partially-developed land that is held for development and sale. In the judgment of management at the time, a decline in real estate values justified the recognition of the loss.

Increase in cash surrender value of life insurance investments was \$2.1 million, \$2.4 million, and \$2.4 million for the years ended December 31, 2012, 2011, and 2010, respectively. Management attributes the decrease in 2012 to a declining interest rate environment that has reduced the return on this type of investment, as well as lower payouts associated with excess death benefits.

Other non-interest income was \$5.8 million, \$5.2 million, and \$5.1 million for the years ended December 31, 2012, 2011, and 2010, respectively. The changes between years were due primarily to increases in the fair value of assets held in trust for certain non-qualifying employee benefit plans, due to the effects of changes in interest rates and equity markets.

**Non-Interest Expense** Total non-interest expense for the years ended December 31, 2012, 2011, and 2010 was \$76.1 million, \$124.9 million, and \$159.8 million, respectively. Results in 2011 included a \$52.6 million non-cash goodwill impairment recorded by the Company in the second quarter of that year. This impairment had no effect on the liquidity, operations, tangible capital, or regulatory capital of the Company or the Bank (for additional discussion refer to "Note 1. Basis of Presentation" of the Company's consolidated financial statements included in "Item 8. Financial Statements and Supplementary Data," below). Results in 2010 included a one-time prepayment penalty of \$89.3 million related to the Company's repayment of \$756.0 million in borrowings from the FHLB of Chicago prior to their scheduled maturities, as previously discussed. Excluding the goodwill impairment and prepayment penalty, total non-interest expense in 2012, 2011, and 2010 was \$76.1 million, \$72.3 million and \$70.5 million, respectively. The following paragraphs discuss the principal components of non-interest expense and the primary reasons for their changes from 2011 to 2012, as well as 2010 to 2011.

Compensation and related expenses were \$42.3 million, \$38.8 million, and \$36.0 million during the years ended December 31, 2012, 2011, and 2010, respectively. The increases in 2012 and 2011 were due principally to the Company's hiring in recent years of certain senior management personnel, a number of commercial relationship managers, and certain other key administrative personnel, as well as annual merit increases for all employees. Also contributing was an increase in certain incentive and bonus payments during these years, including stock based compensation. Finally, the increases in compensation-related expense in 2012 and 2011 were also caused by an increase in costs related to the Company's defined benefit pension plan, due to a decline in the discount rate used to determine the present value of the pension obligation. In 2011 these developments were partially offset by a decline in employee stock ownership plan ("ESOP") expense compared to 2010 (due to the end in 2010 of the 10-year commitment to the ESOP), as well as a decline in the overall number of employees employed by the Company.

Effective January 1, 2013, the Company's board of directors closed the qualified defined benefit pension plan to employees not eligible to participate in the plan as of that date, as well as any employees hired after that date. In addition, effective for service performed after March 1, 2013, the Company's board of directors reduced certain

future benefits formerly provided under the qualified and supplemental plans, but did not reduce all future benefits. Finally, effective January 1, 2013, employees that are not eligible to participate in the qualified plan will be eligible for an enhanced employer contribution in the Company's defined contribution savings plan. Management does not expect the Company's pension expense to be impacted significantly in the near term as a result of these actions, because it is anticipated that any cost savings from these actions will be substantially offset by the adverse impact of a continued decline in the discount rate used to determine the present value of the Company's remaining pension obligations. For additional discussion refer to "Note 10. Employee Benefit Plans" of the Company's consolidated financial statements included in "Item 8. Financial Statements and Supplementary Data," below.

As of December 31, 2012, the Company had 639 full-time associates and 81 part-time associates. This compared to 648 full-time and 71 part-time employees at December 31, 2011, and 682 full-time and 82 part-time associates at December 31, 2010.

Occupancy and equipment expense during the years ended December 31, 2012, 2011, and 2010 was \$11.4 million, \$11.5 million, and \$11.2 million, respectively. The decrease in 2012 was principally caused by lower utility and snow removal costs due to a mild winter, reduced expenditures for maintenance and repair, and lower rental expense due to the closure of three leased banking offices. The impact of these developments was partially offset by an increase in data processing costs due to certain product and system enhancements implemented in 2012. The increase in 2011 was primarily caused by higher levels of repair and maintenance costs and rent expense in 2011 compared to 2010.

Federal insurance premiums were \$3.3 million, \$3.2 million, and \$4.1 million during 2012, 2011, and 2010, respectively. In the second quarter of 2011 the FDIC implemented a new rule that changed the deposit insurance assessment base from an insured institution's domestic deposits (minus certain allowable exclusions) to an insured institution's average consolidated assets (minus average tangible equity and certain other adjustments). The Company benefited from the implementation of this new rule, which resulted in lower deposit insurance costs in 2012 and 2011 compared to 2010. Due to its improved operating results and financial condition, management believes the Company's federal insurance premiums could be up to 25% lower in 2013 than they were in 2012 under the FDIC's risk-based assessment system (for additional information, refer to "Regulation and Supervision of the Bank—Deposit Insurance" in Item 1. Business—Regulation and Supervision," above). However, there can be no assurances.

Advertising and marketing expenses were \$2.1 million, \$2.0 million, and \$2.1 million in 2012, 2011, and 2010, respectively. The Company has maintained its advertising and marketing expenses at approximately the same level since 2010. However, such expenditures depend on future management decisions and there can be no assurances that such expenditures will remain at this level in the future.

Net losses and expenses on foreclosed properties were \$6.7 million, \$7.1 million and \$8.3 million during 2012, 2011, and 2010, respectively. Although the Company's losses and expenses on foreclosed real estate have trended lower since 2010, such losses and expenses have remained elevated due to low real estate values and slow economic growth.

Other non-interest expense was \$10.2 million, \$9.7 million, and \$8.8 million during the years ended December 31, 2012, 2011, and 2010, respectively. The increases in 2012 and 2011 were caused by higher legal, consulting, and accounting fees related to loan workouts and related professional services. In recent months, however, these expenses have declined as the Company has reduced its level of non-performing loans.

**Income Tax Expense (Benefit)** Income tax expense (benefit) was \$3.3 million, \$1.8 million, and \$(49.9) million in 2012, 2011, and 2010, respectively. The large income tax benefit in 2010 was caused by the Company's pre-tax loss, which was primarily the result of the FHLB prepayment penalty and the large provision for loan losses in that year, as previously described. Excluding the impact of the goodwill impairment in 2011 (which was not deductible for income tax purposes), the Company's effective tax rate ("ETR") in 2012, 2011, and 2010 was 33.2%, 26.1%, and 40.7%, respectively. The Company's ETR will vary from period to period depending primarily on the impact of non-taxable revenue, such as earnings from bank-owned life insurance ("BOLI"). The ETR will generally be lower in periods in which non-taxable revenue comprises a larger portion of pre-tax income or loss, such as in 2011. For additional information related to an open issue related to the Company's income taxes in Wisconsin, refer to "Item 1A. Risk Factors."

## Financial Condition

**Overview** The Company's total assets decreased by \$80.2 million or 3.2% during the twelve months ended December 31, 2012. During the period the Company's securities available-for-sale declined by \$231.6 million, its cash and cash equivalents declined by \$33.9 million, its investment in common stock of the FHLB of Chicago (which is a component of other assets) declined by \$30.3 million, its foreclosed and repossessed assets declined by \$10.8 million, and its loans held-for-sale declined by \$8.5 million. These developments were partially offset by an \$82.6 million increase in the Company's loan portfolio. Net cash flows from the changes in these assets were used to fund a \$153.8 million decline in deposit liabilities during the year ended December 31, 2012, as well as the repayment of a \$100.0 million term advance from the FHLB of Chicago. In addition, during 2012 the Company funded a \$157.6 million increase in securities held-to-maturity using term advances from the FHLB of Chicago. The Company's total shareholders' equity increased from \$265.8 million at December 31, 2011, to \$271.9 million at December 31, 2012. Non-performing assets decreased from \$99.9 million or 4.00% of total assets at December 31, 2011, to \$39.8 million or 1.64% at December 31, 2012. The following paragraphs describe these changes in greater detail, as well as other changes in the Company's financial condition during the twelve months ended December 31, 2012.

**Cash and Cash Equivalents** Cash and cash equivalents decreased from \$120.9 million at December 31, 2011, to \$87.1 million at December 31, 2012. This decrease was due to the funding of increases in the Company's loan portfolio, as well as decreases in its deposit liabilities, as previously described.

**Mortgage-Related Securities Available-for-Sale** The Company's portfolio of mortgage-related securities available-for-sale decreased by \$231.6 million or 29.6% during the year ended December 31, 2012. This decrease was principally caused by periodic repayments and security sales that exceeded the Company's purchase of new securities during the year.

The following table presents the carrying value of the Company's mortgage-related securities available-for-sale at the dates indicated (carrying value is equal to fair value for all securities and for all periods presented):

	December 31		
	2012	2011	2010
	(Dollars in thousands)		
Freddie Mac	\$343,682	\$548,944	\$314,067
Fannie Mae	155,895	170,020	30,810
Ginnie Mae	42	778	2,755
Private-label CMOs	50,566	62,028	87,602
Total	\$550,185	\$781,770	\$435,234

The following table presents the activity in the Company's portfolio of mortgage-related securities available-for-sale for the periods indicated:

	Year Ended December 31		
	2012	2011	2010
	(Dollars in thousands)		
Carrying value at beginning of period	\$781,770	\$435,234	\$866,848
Purchases	51,374	507,052	819,675
Sales	(20,395)	—	(1,058,055)
Principal repayments	(260,953)	(167,587)	(187,664)
Premium amortization, net	(4,152)	(3,922)	(2,383)
Other-than-temporary impairment	(400)	(389)	—
Increase (decrease) in net unrealized gain or loss	2,941	11,383	(3,187)
Net increase (decrease)	(231,585)	346,536	(431,614)
Carrying value at end of period	\$550,185	\$781,770	\$435,234

The table below presents information regarding the carrying values, weighted average yields, and contractual maturities of the Company's mortgage-related securities available-for-sale at December 31, 2012:

	One Year or Less		More Than One Year to Five Years		More Than Five Years to Ten Years		More Than Ten Years		Total	
	Carrying Value	Weighted Average Yield	Carrying Value	Weighted Average Yield	Carrying Value	Weighted Average Yield	Carrying Value	Weighted Average Yield	Carrying Value	Weighted Average Yield
Securities by issuer and type:	(Dollars in thousands)									
Freddie Mac, Fannie Mae, and Ginnie Mae pass-throughs	\$17	6.42%	\$887	7.03%	\$27,815	2.60%	\$41	6.71%	\$28,760	2.74%
Freddie Mac, Fannie Mae, and Ginnie Mae REMICs	—	—	—	—	32,611	1.79	438,248	2.35	470,859	2.31
Private-label CMOs	—	—	—	—	18,698	5.11	31,868	3.17	50,566	3.86
Total	\$17	6.42%	\$887	7.03%	\$79,124	2.86%	\$470,157	2.41%	\$550,185	2.47%
Securities by coupon:										
Adjustable-rate coupon	—	—	—	—	—	—	\$54,710	2.04%	\$54,710	2.04%
Fixed-rate coupon	\$17	6.42%	\$887	7.03%	\$79,124	2.86%	415,447	2.46	495,475	2.53
Total	\$17	6.42%	\$887	7.03%	\$79,124	2.86%	\$470,157	2.41%	\$550,185	2.47%

Changes in the fair value of mortgage-related securities available-for-sale are recorded through accumulated other comprehensive income (loss), net of related income tax effect, which is a component of shareholders' equity. The fair value adjustment on the Company's mortgage-related securities available-for-sale was a net unrealized gain of \$10.7 million at December 31, 2012, compared to a net unrealized gain of \$7.7 million at December 31, 2011. This increase was primarily caused by lower market interest rates at December 31, 2012, compared to December 31, 2011. Lower market interest rates typically result in higher fair values for the types of securities owned by the Company.

The Company maintains an investment in private-label CMOs that were purchased from 2004 to 2006 and are secured by prime residential mortgage loans. The securities were all rated "triple-A" by various credit rating agencies at the time of their purchase. However, all of the securities in the portfolio have been downgraded since their purchase. Securities rated less than investment grade are adversely classified as substandard in accordance with regulatory guidelines (refer to "Item 1. Business—Asset Quality"). The following table presents the credit ratings, carrying values, and unrealized losses of the Company's private-label CMO portfolio as of the dates indicated (in instances of split ratings, each security has been classified according to its lowest rating):

	December 31, 2012		December 31, 2011	
	Carrying Value	Net Unrealized Gain (Loss)	Carrying Value	Net Unrealized Gain (Loss)
(Dollars in thousands)				
Credit rating:				
AAA/Aaa	—	—	\$5,386	\$210
AA/Aa	—	—	2,512	58
A	\$7,400	\$228	6,951	(271)
BBB/Baa	7,248	175	10,428	(366)
Less than investment grade	35,918	(33)	36,751	(5,357)
Total private-label CMOs	\$50,566	\$370	\$62,028	\$(5,726)

During 2012 and 2011 management determined that it was unlikely the Company would collect all amounts due according to the contractual terms on certain of its securities rated less than investment grade. Accordingly, the Company recorded \$400,000 and \$389,000 in net OTTI loss on such securities in those periods, respectively (for additional discussion refer to "Results of Operations—Non-Interest Income," above). As of December 31, 2012, management determined that none of the Company's private-label CMOs had incurred additional OTTI as of that date. The Company does not intend to sell these securities and it is unlikely it would be required to sell them before recovery of their amortized cost. However, collection is subject to numerous factors outside of the Company's control and a future determination of OTTI could result in significant losses being recorded through earnings in future periods. For additional discussion refer to "Critical Accounting Policies—Other-Than-Temporary Impairment," below, and "Item 1. Business—Investment Activities" and "Item 1A. Risk Factors," above.

**Mortgage-Related Securities Held-to-Maturity** During the twelve months ended December 31, 2012, the Company purchased \$158.9 million in held-to-maturity securities that consisted of fixed-rate mortgage-backed securities issued and guaranteed by Fannie Mae and backed by multi-family residential loans. The Company funded the purchase of these securities with \$158.9 million in term advances from the FHLB of Chicago. The securities had a

an original weighted-average life of 7.7 years, an original weighted-average yield of 2.31%, and yield-maintenance fees that discourage the underlying borrowers from prepaying the underlying loans. The term advances have a weighted-average life of 5.5 years and cost of 1.47%. The purpose of this transaction was to supplement growth in the Company's earning assets. The Company classified these securities as held-to-maturity because it has the ability and intent to hold them until they mature.

The following table presents the activity in the Company's portfolio of mortgage-related securities held-to-maturity for the periods indicated:

	Year Ended December 31		
	2012	2011	2010
	(Dollars in thousands)		
Carrying value at beginning of period	-	-	-
Purchases	\$158,915	-	-
Sales	-	-	-
Principal repayments	(902)	-	-
Premium amortization	(455)	-	-
Net increase	\$157,558	-	-
Carrying value at end of period	\$157,558	-	-

All of the Company's mortgage-related securities held-to-maturity as of December 31, 2012, had final maturities of five to ten years. The weighted-average yield on these securities was 2.20%.

**Investment Securities Available-for-Sale** In prior periods the Company has held investment securities available-for-sale, which have primarily consisted of mutual funds and U.S. government and federal agency obligations. However, the Company held no such securities as of December 31, 2012 or 2011. The following table presents the Company's investment securities and mortgage-related securities activities for the periods indicated.

	Year Ended December 31		
	2012	2011	2010
	(Dollars in thousands)		
Carrying value at beginning of period	-	\$228,024	\$614,104
Purchases	-	-	3,118,204
Sales	-	(20,837)	(709)
Calls	-	(205,825)	(3,506,718)
Discount accretion	-	-	314
Increase (decrease) in net unrealized loss	-	(1,362)	2,828
Net decrease in investment securities	-	(228,024)	(386,080)
Carrying value at end of period	-	-	\$228,024

As of December 31, 2010, the Company's investment securities available-for-sale consisted of mutual funds with a carrying value of \$22.1 million and U.S. government and federal agency obligations with a carrying value of \$206.0 million.

**Loans Held-for-Sale** The Company's policy is to sell substantially all of its fixed-rate, one- to four-family mortgage loan originations in the secondary market. The following table presents a summary of the activity in the Company's loans held-for-sale for the periods indicated:

	Year Ended December 31		
	2012	2011	2010
	(Dollars in thousands)		
Balance outstanding at beginning of period	\$19,192	\$37,819	\$13,534
Origination of loans intended for sale (1)	446,358	272,785	434,388
Principal balance of loans sold	(454,584)	(292,720)	(409,369)
Change in net unrealized gains or losses (2)	(227)	1,308	(734)
Total loans held-for-sale	\$10,739	\$19,192	\$37,819

- (1) Does not include one- to four-family loans originated for the Company's loan portfolio.  
(2) Refer to "Note 1. Basis of Presentation" in the Company's consolidated financial statements included in "Item 8. Financial Statements and Supplementary Data."

The origination of one- to four-family mortgage loans intended for sale and the corresponding sales of such loans were elevated in the 2012 and 2010 periods as a result of generally lower market interest rates in those periods, which encouraged a larger number of borrowers to refinance higher-rate loans into lower rate loans during those years. For additional discussion, refer to "Results of Operations—Non-Interest Income," above.

**Loans Receivable** Loans receivable increased by \$82.6 million or 6.3% as of December 31, 2012, compared to December 31, 2011. Total loans originated for portfolio increased by \$164.8 million or 41.5% during this year compared to 2011. A portion of this improvement came from increased originations of commercial business loans, which increased by \$40.5 million or 57.6% during the twelve months ended December 31, 2012, compared to 2011. Management attributed this increase to recent efforts to improve the Company's share of the mid-tier commercial banking market (defined as business entities with sales revenues of \$5 to \$100 million), which was a new market segment for the Company in 2011. In the past two years the Company has added experienced leaders to its senior management team and has hired a number of commercial relationship managers and support personnel experienced in managing and selling financial services to the mid-tier commercial banking market. In the near term the Company expects to add additional professionals capable of serving this market segment, although there can be no assurances as to the extent or timing of such staff additions or the impact on operating results.

Originations of multi-family mortgage loans, both permanent and construction, also increased substantially during the period, which management believes reflects a general decline in the level of home ownership in recent periods. Finally, originations of consumer loans, which consist principally of home equity term loans and lines of credit, increased by \$23.7 million or 25.8% during the twelve months ended December 31, 2012, due to more competitive pricing and increased marketing efforts for these types of loans.

The Company's portfolio of one- to four-family loans declined from \$508.5 million at December 31, 2011, to \$465.2 million at December 31, 2012. In 2012 loan repayments exceeded the Company's origination of one- to four-family loans that it retains in portfolio, which consists principally of adjustable-rate loans and, from time-to-time, fixed-rate loans with maturity terms of up to 15 years. The Company also retains certain 30-year, fixed-rate loans in its portfolio under an internal low-income lending program. Repayments of one- to four-family loans have been elevated in recent years due to lower market interest rates that encourage borrowers to refinance adjustable-rate loans, as well as higher-cost fixed-rate loans, into longer-term, fixed-rate loans that the Company sells in the secondary market. The Company's originations of one- to four-family loans that it retains in portfolio were \$89.0 million in 2012 compared to \$91.0 million in 2011.

The following table presents the composition of the Company's loan portfolio in dollar amounts and in percentages of the total portfolio at the dates indicated.

	December 31									
	2012		2011		2010		2009		2008	
	Amount	Percent of Total	Amount	Percent of Total	Amount	Percent of Total	Amount	Percent of Total	Amount	Percent of Total
(Dollars in thousands)										
Mortgage loans:										
Permanent mortgage loans:										
One- to four-family	\$465,170	30.98%	\$508,503	36.59%	\$531,874	37.87%	\$644,852	41.45%	\$867,810	45.82%
Multi-family	264,013	17.58	247,040	17.77	247,210	17.60	200,222	12.87	199,709	10.54
Commercial real estate	263,775	17.57	226,195	16.27	248,253	17.68	262,855	16.90	222,462	11.74
Total permanent mortgages	992,958	66.12	981,738	70.63	1,027,337	73.15	1,107,929	71.22	1,289,981	68.10
Construction and development:										
One- to four-family	18,502	1.23	16,263	1.17	13,479	0.96	11,441	0.74	17,517	0.92
Multi-family	86,904	5.79	29,409	2.12	19,308	1.37	52,323	3.36	74,208	3.92
Commercial real estate	11,116	0.74	19,907	1.43	24,939	1.78	27,040	1.74	82,795	4.37
Land	12,826	0.85	16,429	1.18	25,764	1.83	33,758	2.17	43,601	2.30
Total construction and development loans	129,348	8.61	82,008	5.90	83,490	5.94	124,562	8.01	218,121	11.51
Total mortgage loans	1,122,306	74.74	1,063,746	76.53	1,110,827	79.09	1,232,491	79.23	1,508,102	79.61
Consumer loans:										
Fixed term home equity	116,988	7.79	102,561	7.38	103,619	7.38	124,519	8.00	173,104	9.14
Home equity lines of credit	81,898	5.45	86,540	6.23	87,383	6.24	88,796	5.71	86,962	4.59
Student	12,915	0.86	15,711	1.13	17,695	1.25	19,793	1.27	21,469	1.13
Home improvement	24,910	1.66	24,237	1.74	24,551	1.76	28,441	1.83	36,023	1.90
Automobile	1,814	0.12	2,228	0.16	2,814	0.20	4,077	0.26	11,775	0.62
Other	8,388	0.56	7,177	0.52	7,436	0.52	9,871	0.63	8,740	0.46
Total consumer loans	246,913	16.44	238,454	17.16	243,498	17.35	275,497	17.71	338,073	17.84
Commercial business loans	132,436	8.82	87,715	6.31	50,123	3.56	47,708	3.07	48,277	2.55
Gross loans receivable	1,501,655	100.00%	1,389,915	100.00%	1,404,448	100.00%	1,555,696	100.00%	1,894,452	100.00%
Undisbursed loan proceeds	(76,703)		(41,859)		(32,345)		(32,690)		(54,187)	
Allowance for loan losses	(21,577)		(27,928)		(47,985)		(17,028)		(12,208)	
Deferred fees and costs, net	(1,129)		(492)		(549)		78		996	
Total loans receivable, net	<u>\$1,402,246</u>		<u>\$1,319,636</u>		<u>\$1,323,569</u>		<u>\$1,506,056</u>		<u>\$1,829,053</u>	

The following table presents a summary of the Company's activity in loans receivable for the periods indicated.

	Year Ended December 31		
	2012	2011	2010
	(Dollars in thousands)		
Balance outstanding at beginning of period	\$1,319,636	\$1,323,569	\$1,506,056
Originations:			
One- to four-family loans (1)	88,993	91,042	44,929
Multi-family loans	66,724	55,859	25,091
Commercial real estate loans	70,200	63,376	22,068
Construction and development loans	109,908	24,921	29,029
Total mortgage loan originations	335,825	235,198	121,117
Consumer loans	115,344	91,685	78,198
Commercial business loans	110,941	70,404	34,530
Total originations	562,110	397,287	233,845
Principal payments and repayments:			
Mortgage loans	(264,211)	(232,814)	(220,673)
Consumer loans	(106,885)	(96,729)	(110,197)
Commercial business loans	(66,220)	(32,812)	(32,115)
Total principal payments and repayments	(437,316)	(362,355)	(362,985)
Transfers to foreclosed properties, real estate owned, and repossessed assets	(13,054)	(49,465)	(22,108)
Net change in undisbursed loan proceeds, allowance for loan losses, and deferred fees and costs	(29,130)	10,600	(31,239)
Total loans receivable, net	\$1,402,246	\$1,319,636	\$1,323,569

(1) Does not include one- to four-family loans originated for sale.

The following table presents the contractual maturity of the Company's construction and development loans and its commercial business loans at December 31, 2012. The table does not include the effect of prepayments or scheduled principal amortization.

	December 31, 2012		
	Commercial Business Loans	Construction and Development Loans	Total
	(Dollars in thousands)		
Amounts due:			
Within one year or less	\$60,477	\$11,216	\$71,693
After one year through five years	69,821	92,535	162,356
After five years	2,138	25,597	27,735
Total due after one year	71,959	118,132	190,091
Total commercial and construction loans	\$132,436	\$129,348	\$261,784

The following table presents, as of December 31, 2012, the dollar amount of the Company's construction and development loans and its commercial loans due after one year and whether these loans have fixed interest rates or adjustable interest rates.

	Due After One Year		
	Fixed Rate	Adjustable Rate	Total
	(Dollars in thousands)		
Commercial business loans	\$45,346	\$26,613	\$71,959
Construction and development loans	49,741	68,391	118,132
Total loans due after one year	\$95,087	\$95,004	\$190,091

**Foreclosed Properties and Repossessed Assets** The following table summarizes the Company's foreclosed properties and repossessed assets as of the dates indicated:

	December 31		
	2012	2011	2010
	(Dollars in thousands)		
Commercial real estate	\$8,698	\$13,115	\$7,313
One- to four-family	1,710	6,557	5,554
Multi-family	146	3,890	4,079
Land	3,407	1,162	2,329
Consumer	-	-	18
Total	\$13,961	\$24,724	\$19,293

The decrease in the Company's foreclosed properties and repossessed assets during the twelve months ended December 31, 2012, was caused by increased sales of foreclosed real estate, as well as continued charge-offs of foreclosed properties as management worked to aggressively reduce the Company's level of non-performing assets. These developments were partially offset by foreclosures related to a number of smaller commercial real estate mortgage loans and, to a lesser extent, one- to four-family mortgage loans. The increase in foreclosed properties and repossessed assets in 2011 reflected management efforts to aggressively reduce the elevated level of non-performing loans held by the Company in 2011 and earlier periods. For additional discussion refer to "Financial Condition—Asset Quality," below.

**Mortgage Servicing Rights** The carrying value of the Company's MSRs was \$6.8 million at December 31, 2012, compared to \$7.4 million at December 31, 2011, net of valuation allowances of \$2.4 million and \$868,000, respectively. As of both December 31, 2012 and 2011, the Company serviced \$1.1 billion in loans for third-party investors. For additional information refer to "Results of Operations—Non-Interest Income" and "Item 1. Business—Lending Activities," above.

**Other Assets** Other assets consist of the following items on the dates indicated:

	December 31	
	2012	2011
	(Dollars in thousands)	
Accrued interest receivable:		
Mortgage-related securities	\$1,610	\$1,320
Investment securities	11	537
Loans receivable	4,636	4,664
Total accrued interest receivable	6,257	6,521
Bank-owned life insurance	58,609	56,604
Premises and equipment	50,536	50,423
Federal Home Loan Bank stock, at cost	15,841	46,092
Deferred tax asset, net	34,211	37,454
Prepaid FDIC insurance premiums	2,477	5,673
Other assets	21,764	22,059
Total other assets	\$189,695	\$224,826

BOLI is long-term life insurance on the lives of certain current and past employees where the insurance policy benefits and ownership are retained by the employer. Its cash surrender value is an asset that the Company uses to partially offset the future cost of employee benefits. The cash value accumulation on BOLI is permanently tax deferred if the policy is held to the insured person's death and certain other conditions are met. The increase in BOLI in 2012 was a result of the increase in the accumulated cash value of the insurance policies during the period.

The Company and its subsidiaries conduct their business through an executive office and 76 banking offices, which had an aggregate net book value of \$48.1 million as of December 31, 2012, excluding furniture, fixtures, and equipment. As of December 31, 2012, the Company owned the building and land for 69 of its office locations and leased the space for eight.

The FHLB of Chicago requires its members to own its common stock as a condition of membership, which is redeemable at par (for additional information refer to "Regulation and Supervision of the Bank—Federal Home Loan Bank System" in "Item 1. Business—Regulation and Supervision"). In 2012 the FHLB of Chicago redeemed \$30.3 million of the common stock owned by the Company that was in excess of the amount the Company was

required to own under the minimum guidelines established by the FHLB of Chicago. As of December 31, 2012, the Company continued to own approximately \$5.3 million more in such common stock than required under the minimum guidelines. The Company anticipates that the FHLB of Chicago will redeem this remaining amount in 2013, although there can be no assurances. For additional discussion refer to the section entitled "Federal Home Loan Bank System" in "Item 1. Business—Regulation and Supervision."

The Company's net deferred tax asset decreased by \$3.2 million or 8.7% during the year ended December 31, 2012. Management evaluates this asset on an on-going basis to determine if a valuation allowance is required. Management determined that no valuation allowance was required as of December 31, 2012. The evaluation of the net deferred tax asset requires significant management judgment based on positive and negative evidence. Such evidence includes the Company's cumulative three-year net loss, the nature of the components of such cumulative loss, recent trends in earnings, expectations for the Company's future earnings, the duration of federal and state net operating loss carryforward periods, and other factors. There can be no assurance that future events, such as adverse operating results, court decisions, regulatory actions or interpretations, changes in tax rates and laws, or changes in positions of federal and state taxing authorities will not differ from management's current assessments. The impact of these matters could be significant to the consolidated financial condition, results of operations, and capital of the Company.

Prepaid FDIC insurance premiums declined from \$5.7 million at December 31, 2011, to \$2.5 million at December 31, 2012. In 2009 the FDIC required insured financial institutions to prepay a certain amount of their estimated FDIC deposit insurance premiums. The regular quarterly payments to the FDIC that are otherwise required from the Company were applied against this amount and expensed on a quarterly basis, which is the reason for the decline in the prepaid balance during 2012.

**Deposit Liabilities** Deposit liabilities decreased by \$153.8 million or 7.6% during the twelve months ended December 31, 2012, to \$1.9 billion compared to \$2.0 billion at December 31, 2011. Core deposits, consisting of checking, savings and money market accounts, increased by \$77.3 million or 7.9% during the period while certificates of deposits declined by \$231.0 million or 22.2%. The Company continues to closely manage the rates it offers on certificates of deposit to control its overall liquidity position, which has resulted in a decline in certificates of deposit in recent periods. Core deposits have increased in recent years in response to management's efforts to increase sales of such products and related services to commercial businesses, as well as efforts to focus its retail sales efforts on such products and related services. Also contributing to the increase in core deposits in recent periods, however, is customer reaction to the low interest rate environment. Management believes that this environment has encouraged some customers to switch to core deposits in an effort to retain flexibility in the event interest rates rise in the future.

The following table presents the distribution of the Company's deposit accounts at the dates indicated by dollar amount and percent of portfolio, and the weighted average rate.

	December 31								
	2012			2011			2010		
	Amount	Percent of Total Deposit Liabilities	Weighted Average Nominal Rate	Amount	Percent of Total Deposit Liabilities	Weighted Average Nominal Rate	Amount	Percent of Total Deposit Liabilities	Weighted Average Nominal Rate
	(Dollars in thousands)								
Non-interest-bearing demand	\$143,684	7.69%	0.00%	\$112,211	5.55%	0.00%	\$94,446	4.54%	0.00%
Interest-bearing demand	236,380	12.65	0.01	229,990	11.38	0.01	219,136	10.54	0.02
Money market savings	458,762	24.56	0.19	432,248	21.38	0.19	423,923	20.40	0.57
Savings accounts	217,170	11.63	0.03	204,263	10.10	0.03	210,334	10.12	0.04
Total demand accounts	1,055,996	56.53	0.09	978,712	48.41	0.09	947,839	45.60	0.27
Certificates of deposit:									
With original maturities of:									
Three months or less	9,259	0.50	0.07	9,988	0.49	0.11	12,922	0.62	0.25
Over three to 12 months	184,194	9.86	0.20	162,949	8.06	0.50	194,458	9.36	0.94
Over 12 to 24 months	315,189	16.87	0.77	569,485	28.17	1.10	663,576	31.93	1.60
Over 24 to 36 months	148,503	7.95	1.94	138,677	6.86	1.98	92,268	4.44	2.10
Over 36 to 48 months	-	0.00	0.00	1,282	0.06	4.31	5,137	0.25	4.36
Over 48 to 60 months	154,758	8.29	3.48	160,570	7.95	3.68	162,110	7.81	3.81
Total certificates of deposit	811,903	43.47	1.36	1,042,951	51.59	1.51	1,130,471	54.40	1.84
Total deposit liabilities	\$1,867,899	100.00%	0.64%	\$2,021,663	100.00%	0.82%	\$2,078,310	100.00%	1.12%

At December 31, 2012, the Company had certificates of deposit with balances of \$100,000 and over maturing as follows:

	Amount
	(In thousands)
Maturing in:	
Three months or less	\$53,926
Over three months through six months	54,785
Over six months through 12 months	58,891
Over 12 months through 24 months	47,169
Over 24 months through 36 months	2,693
Over 36 months	3,459
Total certificates of deposits greater than \$100,000	<u>\$220,923</u>

The following table presents the Company's activity in its deposit liabilities for the periods indicated:

	Year Ended December 31		
	2012	2011	2010
	(Dollars in thousands)		
Total deposit liabilities at beginning of period	\$2,021,663	\$2,078,310	\$2,137,508
Net withdrawals	(167,096)	(74,632)	(85,039)
Interest credited, net of penalties	13,332	17,986	25,841
Total deposit liabilities at end of period	<u>\$1,867,899</u>	<u>\$2,021,663</u>	<u>\$2,078,310</u>

**Borrowings** Borrowings, which consist of advances from the FHLB of Chicago, increased by \$53.1 million or 37.7% during the twelve months ended December 31, 2012. As previously noted, during the period the Company borrowed \$158.9 million in term advances from the FHLB of Chicago to fund the purchase of held-to-maturity securities. This development was partially offset by the repayment of \$100.0 million in borrowings from the FHLB of Chicago that had a rate of 4.52% and that matured during the third quarter of the year.

Management believes that additional funds are available to be borrowed from the FHLB of Chicago or other sources in the future to fund loan originations or security purchases or to fund existing advances as they mature if needed or desirable. However, there can be no assurances of the future availability of borrowings or any particular level of future borrowings. For additional information refer to "Item 1. Business—Borrowings."

The following table sets forth certain information regarding the Company's borrowings at the end of and during the periods indicated:

	At or For the Year Ended December 31				
	2012	2011	2010	2009	2008
	(Dollars in thousands)				
Balance outstanding at end of year:					
FHLB term advances	\$210,786	\$153,091	\$149,934	\$906,979	\$907,971
Overnight borrowings from FHLB	-	-	-	-	-
Weighted average interest rate at end of year:					
FHLB term advances	2.34%	4.69%	4.79%	4.26%	4.26%
Overnight borrowings from FHLB	-	-	-	-	-
Maximum amount outstanding during the year:					
FHLB term advances	\$311,419	\$199,493	\$906,979	\$907,971	\$912,459
Overnight borrowings from FHLB	5,000	-	-	-	5,000
Other borrowings	-	-	-	-	1,103
Average amount outstanding during the year:					
FHLB term advances	\$227,573	\$156,521	\$871,212	\$907,443	\$910,517
Overnight borrowings from FHLB	14	-	-	-	22
Other borrowings	-	-	-	-	3
Weighted average interest rate during the year:					
FHLB term advances	3.07%	4.59%	4.32%	4.32%	4.34%
Overnight borrowings from FHLB	0.30%	-	-	-	3.75%
Other borrowings	-	-	-	-	1.92%

**Shareholders' Equity** The Company's shareholders' equity increased from \$265.8 million at December 31, 2011, to \$271.9 million at December 31, 2012. This increase was caused by net income during the period, as well as lower accumulated other comprehensive loss due to an increase in the fair value of available-for-sale securities. These developments were partially offset by the payment of cash dividends to shareholders during the year. The book

value of the Company's common stock was \$5.87 per share at December 31, 2012, compared to \$5.75 per share at December 31, 2011.

The Company's ratio of shareholders' equity to total assets was 11.24% at December 31, 2012, compared to 10.64% at December 31, 2011. The increase in this ratio was due primarily to a decrease in Bank Mutual's total assets, as well as an increase in shareholders' equity, as described in the previous paragraph. The Company is not currently required to maintain minimum capital for regulatory purposes. However, the Bank is required to maintain specified amounts of regulatory capital pursuant to regulations promulgated by the OCC and the FDIC. The Bank is "well capitalized" for regulatory capital purposes. As of December 31, 2012, the Bank had a total risk-based capital ratio of 18.02% and a Tier 1 capital ratio of 10.28%. The minimum ratios to be considered "well capitalized" under current supervisory regulations are 10% for total risk-based capital and 6% for Tier 1 capital. The minimum ratios to be considered "adequately capitalized" are 8% and 4%, respectively. For additional discussion refer to "Note 8. Shareholders' Equity" in "Item 8. Financial Statements and Supplementary Data," as well as "Item 1. Business—Regulation and Supervision."

On February 4, 2013, the Company's board of directors announced that it had declared a \$0.02 per share dividend payable on March 1, 2013, to shareholders of record on February 15, 2013. In 2012 the Company did not repurchase any shares of its common stock and the Company does not currently have a program authorizing the purchase of shares.

The payment of dividends or the repurchase of common stock by the Company is highly dependent on the ability of the Bank to pay dividends or otherwise distribute capital to the Company. Such payments are subject to any requirements imposed by law or regulations and to the application and interpretation thereof by the OCC and FRB, which have become increasingly strict as to the amount of capital it expects financial institutions to maintain. The Company cannot provide any assurances that dividends will continue to be paid, the amount of any such dividends, or the possible future resumption of share repurchases. For further information about factors which could affect the Company's payment of dividends, refer to "Item 1. Business—Regulation and Supervision," as well as "Item 5. Market for Registrant's Common Equity, Related Stockholder Matters, and Issuer Purchase of Equity Securities," above.

**Asset Quality** The following table presents information regarding non-accrual mortgage loans, consumer loans, commercial business loans, accruing loans delinquent 90 days or more, and foreclosed properties and repossessed assets as of the dates indicated.

	December 31				
	2012	2011	2010	2009	2008
	(Dollars in thousands)				
Non-accrual mortgage loans:					
One- to four-family	\$8,192	\$14,868	\$18,684	\$12,126	\$8,185
Multi-family	6,824	22,905	31,660	3,357	13,255
Commercial real estate	6,994	23,997	41,244	18,840	5,573
Construction and development	937	9,368	26,563	4,859	2,847
Total non-accrual mortgage loans	<u>22,947</u>	<u>71,138</u>	<u>118,151</u>	<u>39,182</u>	<u>29,860</u>
Non-accrual consumer loans:					
Secured by real estate	1,514	1,457	1,369	1,433	759
Other consumer loans	59	207	275	212	400
Total non-accrual consumer loans	<u>1,573</u>	<u>1,664</u>	<u>1,644</u>	<u>1,645</u>	<u>1,159</u>
Non-accrual commercial business loans	693	1,642	2,779	923	1,494
Total non-accrual loans	<u>25,213</u>	<u>74,444</u>	<u>122,574</u>	<u>41,750</u>	<u>32,513</u>
Accruing loans delinquent 90 days or more (1)	584	696	373	834	576
Total non-performing loans	<u>25,797</u>	<u>75,140</u>	<u>122,947</u>	<u>42,584</u>	<u>33,089</u>
Foreclosed real estate and repossessed assets	13,961	24,724	19,293	17,689	4,768
Total non-performing assets	<u>\$39,758</u>	<u>\$99,864</u>	<u>\$142,240</u>	<u>\$60,273</u>	<u>\$37,857</u>
Non-performing loans to total loans	1.84%	5.69%	9.29%	2.83%	1.81%
Non-performing assets to total assets	1.64%	4.00%	5.49%	1.72%	1.08%
Interest income that would have been recognized if non-accrual loans had been current	\$1,998	\$4,535	\$4,734	\$2,671	\$2,519

(1) Consists of student loans that are guaranteed under programs sponsored by the U.S. government.

The Company's non-performing loans were \$25.8 million or 1.84% of loans receivable as of December 31, 2012, compared to \$75.1 million or 5.69% of loans receivable as of December 31, 2011. Non-performing assets, which includes non-performing loans, were \$39.8 million or 1.64% of total assets and \$99.9 million or 4.00% of total assets as of these same dates, respectively. The decline in non-performing loans in 2012 was due principally to a \$41.5 million or 73.8% aggregate decrease in non-performing commercial real estate, multi-family, and construction loans. This decrease was primarily attributable to eight larger loans that aggregated \$25.2 million that were paid off, six larger loans that aggregated \$6.6 million that were transferred to foreclosed real estate, and one loan for \$2.5 million that was returned to performing status due to the improved condition of the borrower. All of these loans were secured by commercial and multi-family real estate. In addition, non-performing one- to four-family loans declined by \$6.7 million or 44.9% and non-performing commercial business loans declined by \$949,000 or 57.8% during the twelve months ended December 31, 2012. In addition, foreclosed properties and repossessed assets, which is a component of non-performing assets, declined by \$10.8 million or 43.5% during the twelve months ended December 31, 2012, for reasons previously described.

In 2011 the Company's non-performing loans declined by \$47.8 million or 38.9%. Most of this decline was attributable to a \$43.2 million aggregate decrease in non-performing commercial real estate, multi-family, and construction loans. In 2011 six larger loan relationships that aggregated \$14.5 million were paid off, six larger loan relationships that aggregated \$17.8 million were foreclosed, and the Company recorded \$8.9 million in charge-offs related to seven larger loan relationships that continued to be classified as non-performing as of the end of that year. The aggregate balance for these latter loans was \$19.4 million (prior to the charge-offs). Finally, non-performing one- to four-family loans and non-performing commercial business loans declined by \$3.8 million and \$1.1 million, respectively, during the twelve months ended December 31, 2011. Also in 2011, the Company's foreclosed properties and repossessed assets, which is a component of non-performing assets, increased by \$5.4 million or 28.2%, due principally to the aforementioned foreclosures during the year. This development was partially offset by sales of foreclosed real estate, as well as continued charge-offs of foreclosed properties.

In 2010 the Company's non-performing assets increased by \$82.0 million or 136%. This increase was due in part to 15 unrelated loan relationships that aggregated \$38.1 million that were current with respect to principal and interest payments. Management determined that these loans should be classified as non-performing as of December 31, 2010, in light of underlying difficulties with the properties that secure the loans, as well as an increasingly strict regulatory environment. These loans were secured by commercial real estate, multi-family real estate, undeveloped land, and commercial business assets. Also contributing to the increase in non-performing assets in 2010 were 16 larger loan relationships that aggregated \$49.2 million that defaulted during the year. These loans were secured by commercial real estate, multi-family real estate, single-family real estate, undeveloped land, and commercial business assets. Also in 2010, non-performing one- to four-family loans increased by \$4.0 million, smaller non-performing commercial business loans increased by \$5.8 million, smaller non-performing commercial and multi-family real estate loans increased by \$2.0 million, and foreclosed real estate and repossessed assets increased by \$1.6 million. These developments were partially offset by the combined effects of loan charge-offs and a small decline in non-performing student loans during the year.

In 2009 the Company's non-performing assets increased by \$22.4 million or 59.2%. This increase was primarily caused by the default of \$15.4 million in loans to seven borrowers that were secured by office and retail buildings, townhomes, and improved land. Also contributing was a \$3.9 million increase in non-performing one- to four-family residential loans and a \$744,000 increase in non-performing consumer and student loans. Foreclosed real estate and repossessed assets also increased by \$12.9 million during 2009, due primarily to the foreclosure of a \$9.1 million loan secured by a completed condominium development project that had defaulted in the prior year. These developments were partially offset by the combined effects of loan charge-offs and a small decline in non-performing commercial business loans during the year.

Non-performing assets are classified as "substandard" in accordance with the Company's internal risk rating policy. In addition to non-performing assets, at December 31, 2012, management was closely monitoring \$31.8 million in additional loans that were adversely classified as "substandard" and \$37.7 million in additional loans that were classified as "special mention" in accordance with the Company's internal risk rating policy. These amounts compared to \$28.5 million and \$51.6 million, respectively, as of December 31, 2011. The substantial decrease in loans classified as "special mention" during 2012 was due to loans that were further downgraded during the year to "substandard" or were upgraded because of improved performance. As of December 31, 2012, most of the additional loans classified as "substandard" or "special mention" were secured by commercial real estate, multi-family real estate, land, and certain commercial business assets. Although these additional loans were performing in accordance with their contractual terms and were not included in non-performing assets, management deemed their

classification as “substandard” or “special mention” to be prudent in light of deterioration in the financial strength of the borrowers and/or the performance of the collateral, including an assessment of occupancy rates, lease rates, unit sales, and/or estimated changes in the value of the collateral. Further deterioration in the borrowers or related collateral could result in these additional loans becoming non-performing assets in future periods. The Company does not expect to incur a loss on these additional loans at this time, although there can be no assurance.

The Company’s classified loans and non-performing assets have declined substantially in recent periods. However, this trend is subject to many factors that are outside of Company’s control, such as economic and market conditions. As such, there can be no assurances that Company’s classified loans and non-performing loans and assets will continue to decline in future periods or that there will not be significant variability in the Company’s provision for loan losses from period to period.

In the third quarter of 2012 the OCC issued accounting and reporting guidance related to instances in which borrowers on one- to four-family mortgage loans have had debt discharged in bankruptcy and have not reaffirmed obligations related to their mortgage debt. The Company does not have a material exposure to one- to four-family mortgage loans that meet the criteria specified in the OCC guidance.

Loans considered to be impaired by the Company at December 31, 2012, totaled \$25.8 million as compared to \$75.1 million at December 31, 2011, \$131.4 million at December 31, 2010, \$42.6 million at December 31, 2009, and \$33.1 million at December 31, 2008. The average annual balance of loans impaired as of December 31, 2012, was \$52.4 million and the interest received and recognized on these loans while they were impaired was \$1.2 million.

The following table presents the activity in the Company’s allowance for loan losses at or for the periods indicated.

	At or For the Year Ended December 31				
	2012	2011	2010	2009	2008
	(Dollars in thousands)				
Balance at beginning of period	\$27,928	\$47,985	\$17,028	\$12,208	\$11,774
Provision for loan losses	4,545	6,710	49,619	12,413	1,447
Charge-offs:					
One- to four-family	(3,182)	(3,047)	(528)	(397)	(167)
Multi-family	(857)	(5,035)	(140)	(4,523)	–
Commercial real estate	(4,894)	(15,286)	(11,621)	(1,989)	(446)
Construction and development	(2,693)	(2,737)	(3,515)	–	–
Consumer	(812)	(1,036)	(776)	(527)	(411)
Commercial business	(136)	(551)	(2,140)	(210)	(34)
Total charge-offs	(12,574)	(27,692)	(18,720)	(7,646)	(1,058)
Recoveries:					
One- to four-family	86	49	20	1	–
Multi-family	568	248	–	–	–
Commercial real estate	956	40	1	19	–
Construction and development	1	550	–	–	–
Consumer	41	20	37	33	45
Commercial business	26	18	–	–	–
Total recoveries	1,678	925	58	53	45
Net charge-offs	(10,896)	(26,768)	(18,662)	(7,593)	(1,013)
Balance at end of period	\$21,577	\$27,928	\$47,985	\$17,028	\$12,208
Net charge-offs to average loans	0.78%	1.96%	1.26%	0.45%	0.05%
Allowance for loan losses to total loans	1.54%	2.12%	3.63%	1.13%	0.67%
Allowance for loan losses to non-performing loans	83.64%	37.17%	39.03%	39.99%	36.89%

The changes in the Company’s allowance for loan losses in recent years has been consistent with overall changes in the Company’s level of non-performing loans, changes in loan charge-off activity, and industry trends. The changes are also consistent with changes in management’s assessment of overall economic conditions, unemployment, and real estate values during the periods. The Company’s ratio of allowance for loan losses as a percent of non-performing loans increased from 37.2% at December 31, 2011, to 83.6% at December 31, 2012. This increase was caused by a substantial decline in non-performing loans relative to the allowance for loan losses. This change is to

be expected when non-performing loans (which are generally evaluated for impairment on an individual basis) decline in a period and, as a result, a larger portion of the allowance for loan losses relates to loans that are evaluated for impairment on a collective basis (refer to “Note 3. Loans Receivable” in “Item 8. Financial Statements and Supplementary Data”).

Although management believes the Company’s present level of allowance for loan losses is adequate, there can be no assurances that future adjustments to the allowance will not be necessary, which could adversely affect the Company’s results of operations. For additional discussion, refer to “Item 1. Business—Asset Quality,” above, and “Critical Accounting Policies—Allowance for Loan Losses,” below.

The following table represents the Company’s allocation of its allowance for loan losses by loan category on the dates indicated:

Loan category:	December 31									
	2012		2011		2010		2009		2008	
	Amount	Percentage in Category to Total	Amount	Percentage in Category to Total	Amount	Percentage in Category to Total	Amount	Percentage in Category to Total	Amount	Percentage in Category to Total
	(Dollars in thousands)									
Mortgage loans:										
One- to four-family	\$3,267	15.14%	\$3,201	11.46%	\$3,726	7.76%	\$2,806	16.47%	\$3,038	24.89%
Multi-family	5,195	24.08	7,442	26.65	9,265	19.31	3,167	18.60	4,197	34.38
Commercial real estate	7,354	34.08	9,467	33.90	21,885	45.61	5,715	33.56	1,113	9.12
Construction/development	2,617	12.13	4,506	16.13	10,141	21.13	1,172	6.88	400	3.28
Total mortgage loans	18,433	85.43	24,616	88.14	45,017	93.81	12,860	75.52	8,748	71.66
Consumer	1,458	6.76	1,214	4.35	1,427	2.97	2,243	13.17	2,125	17.41
Commercial business	1,686	7.81	2,098	7.51	1,541	3.21	1,925	11.31	1,335	10.94
Total allowance for loan losses	\$21,577	100.00%	\$27,928	100.00%	\$47,985	100.00%	\$17,028	100.00%	\$12,208	100.00%

### Critical Accounting Policies

There are a number of accounting policies that the Company has established which require a significant amount of management judgment. A number of the more significant policies are discussed in the following paragraphs.

**Allowance for Loan Losses** Establishing the amount of the allowance for loan losses requires the use of management judgment. The allowance for loan losses is maintained at a level believed adequate by management to absorb probable losses inherent in the loan portfolio and is based on factors such as the size and current risk characteristics of the portfolio, an assessment of individual problem loans and pools of homogenous loans within the portfolio, and actual loss, delinquency, and/or risk rating experience within the portfolio. The Company also considers current economic conditions and/or events in specific industries and geographical areas, including unemployment levels, trends in real estate values, peer comparisons, and other pertinent factors, to include regulatory guidance. Finally, as appropriate, the Company also considers individual borrower circumstances and the condition and fair value of the loan collateral, if any.

Determination of the allowance is inherently subjective as it requires significant estimates, including the amounts and timing of expected future cash flows on loans, the fair value of underlying collateral (if any), estimated losses on pools of homogeneous loans based on historical loss experience, changes in risk characteristics of the loan portfolio, and consideration of current economic trends, all of which may be susceptible to significant change. Higher rates of loan defaults than anticipated would likely result in a need to increase provisions in future years. Loan losses are charged off against the allowance, 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. Evaluations are conducted at least quarterly and more often if deemed necessary. If management misjudges a major component of the allowance and the Company experiences an unanticipated loss, it will likely affect earnings. Developments affecting loans can also cause the allowance to vary significantly between quarters. Management consistently challenges itself in the review of the risk components to identify any changes in trends and their causes.

**Other-Than-Temporary Impairment** Generally accepted accounting principles require enterprises to determine whether a decline in the fair value of an individual debt security below its amortized cost is other than temporary. If the decline is deemed to be other than temporary, the cost basis of the security must be written down through a charge to earnings. Determination of OTTI requires significant management judgment relating to the probability of future cash flows, the financial condition and near-term prospects of the issuer of the security, and/or the collateral

for the security, the duration and extent of the decline in fair value, and the ability and intent of the Company to retain the security, among other things. Future changes in management's assessment of OTTI on its securities could result in significant charges to earnings in future periods.

**Income Taxes** The assessment of the Company's tax assets and liabilities involves the use of estimates, forecasts, assumptions, interpretations, and judgment concerning the Company's estimated future results of operations, as well as certain accounting pronouncements and federal and state tax codes. Management evaluates the Company's net deferred tax asset on an on-going basis to determine if a valuation allowance is required. This evaluation requires significant management judgment based on positive and negative evidence. Such evidence includes the Company's cumulative three-year net loss, the nature of the components of such cumulative loss, recent trends in earnings excluding one-time charges (such as the FHLB prepayment penalty in 2010 and the goodwill impairment in 2011), expectations for the Company's future earnings, the duration of federal and state net operating loss carryforward periods, and other factors. There can be no assurance that future events, such as adverse operating results, court decisions, regulatory actions or interpretations, changes in tax rates and laws, or changes in positions of federal and state taxing authorities will not differ from management's current assessments. The impact of these matters could be significant to the consolidated financial conditions and results of operations.

The Company describes all of its significant accounting policies in "Note 1. Basis of Presentation" in "Item 8. Financial Statements and Supplementary Data."

### **Contractual Obligations, Commitments, Contingent Liabilities, and Off-Balance Sheet Arrangements**

The Company has various financial obligations, including contractual obligations and commitments, that may require future cash payments.

The following table presents, as of December 31, 2012, significant fixed and determinable contractual obligations to third parties by payment date. All amounts in the table exclude interest costs to be paid in the periods indicated, if applicable.

	Payments Due In				Total
	One Year Or Less	One to Three Years	Three to Five Years	Over Five Years	
	(Dollars in thousands)				
Deposit liabilities without a stated maturity	\$1,055,996	—	—	—	\$1,055,996
Certificates of deposit	618,487	\$176,337	\$17,079	—	811,903
Borrowed funds	217	23,450	61,273	\$125,846	210,786
Operating leases	964	1,740	1,123	2,986	6,813
Purchase obligations	1,680	3,360	3,360	2,940	11,340
Deferred retirement plans and deferred compensation plans	1,080	2,041	2,155	6,211	11,487

The Company's operating lease obligations represent short- and long-term lease and rental payments for facilities, certain software and data processing and other equipment. Purchase obligations represent obligations under agreements to purchase goods or services that are enforceable and legally binding on the Company and that specify all significant terms, including: fixed or minimum quantities to be purchased; fixed, minimum or variable price provisions; and the approximate timing of the transaction. The purchase obligation amounts presented above primarily relate to certain contractual payments for services provided for information technology.

The Company also has obligations under its deferred retirement plan for directors as described in "Note 10. Employee Benefit Plans" in "Item 8. Financial Statements and Supplementary Data."

The following table details the amounts and expected maturities of significant off-balance sheet commitments as of December 31, 2012.

	Payments Due In				Total
	One Year Or Less	One to Three Years	Three to Five Years	Over Five Years	
Commitments to extend credit:	(Dollars in thousands)				
Commercial real estate	\$13,430	–	–	–	\$13,430
Residential real estate	22,518	–	–	–	22,518
Revolving home equity and credit card lines	152,109	–	–	–	152,109
Standby letters of credit	256	\$1,250	–	\$6	1,512
Commercial lines of credit	75,354	–	–	–	75,354
Undisbursed commercial loans	2,740	10	\$250	–	3,000
Net commitments to sell mortgage loans	75,750	–	–	–	75,750

Commitments to extend credit, including loan commitments, standby letters of credit, unused lines of credit and commercial letters of credit do not necessarily represent future cash requirements, since these commitments often expire without being drawn upon.

## Quarterly Financial Information

The following table sets forth certain unaudited quarterly data for the periods indicated:

	2012 Quarter Ended			
	March 31	June 30	September 30	December 31
	(Dollars in thousands, except per share amounts)			
Interest income	\$20,777	\$21,079	\$20,697	\$20,467
Interest expense	5,879	6,226	5,098	4,437
Net interest income	14,898	14,853	15,599	16,030
Provision for loan losses	51	1,730	657	2,107
Total non-interest income	7,271	6,934	6,845	8,209
Total non-interest expense	20,517	18,140	18,790	18,608
Income before taxes	1,601	1,917	2,997	3,524
Income tax expense	462	601	1,044	1,229
Net loss attributable to non-controlling interest	16	13	13	10
Net income	\$1,155	\$1,329	\$1,966	\$2,305
Earnings per share-basic	\$0.03	\$0.03	\$0.04	\$0.05
Earnings per share-diluted	\$0.03	\$0.03	\$0.04	\$0.05
Cash dividend paid per share	\$0.01	\$0.01	\$0.01	\$0.02
	2011 Quarter Ended			
	March 31	June 30	September 30	December 31
	(Dollars in thousands, except per share amounts)			
Interest income	\$23,063	\$22,906	\$22,017	\$21,359
Interest expense	7,240	6,801	6,531	6,183
Net interest income	15,823	16,105	15,486	15,176
Provision for loan losses	3,180	805	1,093	1,632
Total non-interest income	5,795	4,759	5,474	7,130
Total non-interest expense (1)	17,050	71,184	17,920	18,746
Income (loss) before taxes	1,388	(51,125)	1,947	1,928
Income tax expense	361	266	610	516
Net loss attributable to non-controlling interest	13	14	12	10
Net income (loss)	\$1,040	\$(51,377)	\$1,349	\$1,422
Earnings (loss) per share-basic	\$0.02	\$(1.12)	\$0.02	\$0.03
Earnings (loss) per share-diluted	\$0.02	\$(1.12)	\$0.02	\$0.03
Cash dividend paid per share	\$0.03	\$0.01	\$0.01	\$0.01

(1) Non-interest expense in the quarter ended June 30, 2011, included a \$52.6 million goodwill impairment.

## **Item 7A. Quantitative and Qualitative Disclosures About Market Risk**

The Company's ability to maintain net interest income depends upon earning a higher yield on assets than the rates it pays on deposits and borrowings. Fluctuations in market interest rates will ultimately impact both the level of income and expense recorded on a large portion of the Company's assets and liabilities. Fluctuations in interest rates will also affect the market value of all interest-earning assets and interest-bearing liabilities, other than those with a very short term to maturity.

Interest rate sensitivity is a measure of the difference between amounts of interest-earning assets and interest-bearing liabilities which either reprice or mature during a given period of time. The difference, or the interest rate sensitivity "gap," provides an indication of the extent to which the Company's interest rate spread will be affected by changes in interest rates. Refer to "Gap Analysis," below. Interest rate sensitivity is also measured through analysis of changes in the present value of the Company's equity. Refer to "Present Value of Equity," below.

To achieve the objectives of managing interest rate risk, the Company's executive management meets periodically to discuss and monitor the market interest rate environment and provides reports to the board of directors. Management seeks to coordinate asset and liability decisions so that, under changing interest rate scenarios, the Company's earnings will remain within an acceptable range. The primary objectives of the Company's interest rate management strategy are to:

- maintain earnings and capital within self-imposed parameters over a range of possible interest rate environments;
- coordinate interest rate risk policies and procedures with other elements of the Company's business plan, all within the context of the current business environment and regulatory capital and liquidity requirements; and
- manage interest rate risk in a manner consistent with the approved guidelines and policies set by the board of directors.

The Company has employed certain strategies to manage the interest rate risk inherent in the asset/liability mix, including:

- emphasizing the origination of adjustable-rate mortgage loans and mortgage loans that mature or reprice within five years for portfolio, and selling most fixed-rate residential mortgage loans with maturities of 15 years or more in the secondary market;
- emphasizing variable-rate and/or short- to medium-term, fixed-rate consumer and commercial business loans;
- maintaining a significant level of mortgage-related and other investment securities available-for-sale that have weighted average life of less than five years or interest rates that reprice in less than five years; and
- managing deposits and borrowings to provide stable funding.

Management believes these strategies reduce the Company's interest rate risk exposure to acceptable levels.

**Gap Analysis** Repricing characteristics of assets and liabilities may be analyzed by examining the extent to which such assets and liabilities are "interest rate sensitive" and by monitoring a financial institution's interest rate sensitivity "gap." An asset or liability is said to be "interest rate sensitive" within a specific time period if it will mature or reprice within that time period. The interest rate sensitivity gap is defined as the difference between the amount of interest-earning assets maturing or repricing within a specific time period and the amount of interest-bearing liabilities maturing or repricing within that same time period.

A gap is considered positive when the amount of interest-earning assets maturing or repricing within a specific time period exceeds the amount of interest-bearing liabilities maturing or repricing within that specific time period. A gap is considered negative when the amount of interest-bearing liabilities maturing or repricing within a specific time period exceeds the amount of interest-earning assets maturing or repricing within the same period. During a period of rising interest rates, a financial institution with a negative gap position would be expected, absent the effects of other factors, to experience a greater increase in the costs of its liabilities relative to the yields of its assets and thus a decrease in the

institution's net interest income. An institution with a positive gap position would be expected, absent the effect of other factors, to experience the opposite result. Conversely, during a period of falling interest rates, a negative gap would tend to result in an increase in net interest income while a positive gap would tend to reduce net interest income.

The following table presents the amounts of the Company's interest-earning assets and interest-bearing liabilities outstanding at December 31, 2012, which management anticipates to reprice or mature in each of the future time periods shown. The information presented in the following table is based on the following assumptions:

- Loans—based upon contractual maturities, repricing date, if applicable, scheduled repayments of principal, and projected prepayments of principal based upon the Company's historical experience or anticipated prepayments. Actual cash flows may differ substantially from these assumptions.
- Mortgage-related securities—based upon known repricing dates (if applicable) and an independent outside source for determining estimated prepayment speeds. Actual cash flows may differ substantially from these assumptions.
- Deposit liabilities—based upon contractual maturities and the Company's historical decay rates. Actual cash flows may differ from these assumptions.
- Borrowings—based upon final maturity.

	December 31, 2012					Total
	Within Three Months	Three to Twelve Months	More than 1 Year to 3 Years	More than 3 Years - 5 Years	Over 5 Years	
	(Dollars in thousands)					
Loans receivable:						
Mortgage loans:						
Fixed	\$39,832	\$72,752	\$164,205	\$144,137	\$107,303	\$528,229
Adjustable	106,604	223,891	91,642	61,681	28,672	512,490
Consumer loans	98,009	46,009	48,225	27,033	25,079	244,355
Commercial business loans	69,055	22,027	24,498	19,786	323	135,689
Interest-earning deposits	37,029	—	—	—	—	37,029
Mortgage-related securities:						
Fixed	52,518	148,842	223,029	58,182	159,580	642,151
Adjustable	54,938	—	—	—	—	54,938
Other interest-earning assets	15,841	—	—	—	—	15,841
Total interest-earning assets	473,826	513,521	551,599	310,819	320,957	2,170,722
Deposit liabilities:						
Non-interest-bearing demand accounts	861	2,551	6,581	6,273	127,418	143,684
Interest-bearing demand accounts	1,413	4,189	10,808	10,301	209,669	236,380
Savings accounts	1,443	4,269	10,959	10,368	190,131	217,170
Money market accounts	458,762	—	—	—	—	458,762
Certificates of deposit	331,310	368,185	95,329	17,079	—	811,903
Advance payments by borrowers for taxes and insurance	—	4,956	—	—	—	4,956
Borrowings	322	1,182	26,228	64,182	118,871	210,786
Total non-interest- and interest-bearing liabilities	794,111	385,332	149,905	108,203	646,089	2,083,640
Interest rate sensitivity gap	<u>\$(320,285)</u>	<u>\$128,189</u>	<u>\$401,694</u>	<u>\$202,616</u>	<u>\$(325,132)</u>	<u>\$87,082</u>
Cumulative interest rate sensitivity gap	<u>\$(320,285)</u>	<u>\$(192,096)</u>	<u>\$209,598</u>	<u>\$411,214</u>	<u>\$87,082</u>	
Cumulative interest rate sensitivity gap as a percent of total assets	-13.26%	-7.94%	8.67%	17.05%	3.60%	
Cumulative interest-earning assets as a percentage of non-interest- and interest-bearing liabilities	59.67%	83.69%	115.73%	128.64%	104.18%	

Based on the above gap analysis, at December 31, 2012, the Company's interest-bearing liabilities maturing or repricing within one year exceeded its interest-earning assets maturing or repricing within the same period. Based on this information, over the course of the next year the Company's net interest income could be adversely impacted by an increase in market interest rates. Alternatively, the Company's net interest income could be favorably impacted by a decline in market interest rates. However, it should be noted that the Company's future net interest income is affected by more than just future market interest rates. Net interest income is also affected by absolute and relative levels of earning assets and interest-bearing liabilities, the level of non-performing loans and other investments, and by other

factors outlined in “Item 1. Business—Cautionary Statement,” “Item 1A. Risk Factors,” and “Item 7. Management Discussion of Financial Condition and Results of Operations.”

In addition to not anticipating all of the factors that could impact future net interest income, gap analysis has certain shortcomings. For example, although certain assets and liabilities may mature or reprice in similar periods, the interest rates on such react by different degrees to changes in market interest rates, especially in instances where changes in rates are limited by contractual caps or floors or instances where rates are influenced by competitive forces. Interest rates on certain types of assets and liabilities may fluctuate in advance of changes in market interest rates, while interest rates on other types may lag behind changes in market rates. For example, it is the Company’s past experience that rate changes on most of its deposit liabilities generally lag changes in market interest rates. Certain assets, such as adjustable-rate loans, have features which limit changes in interest rates on a short term basis and over the life of the loan. If interest rates change, prepayment, and early withdrawal levels would likely deviate significantly from those assumed in calculating the table. Finally, the ability of borrowers to make payments on their adjustable-rate loans may decrease if interest rates increase. Because of these shortcomings, management of the Company believes that gap analysis is a better indicator of the relative change in the Company’s interest rate risk exposure from period to period than it is an indicator of the direction or amount of future change in net interest income.

**Present Value of Equity** In addition to the gap analysis table, management also uses simulation models to monitor interest rate risk. The models report the present value of equity (“PVE”) in different interest rate environments, assuming an instantaneous and permanent interest rate shock to all interest rate sensitive assets and liabilities. The PVE is the difference between the present value of expected cash flows of interest rate sensitive assets and liabilities. The changes in market value of assets and liabilities due to changes in interest rates reflect the interest rate sensitivity of those assets and liabilities as their values are derived from the characteristics of the asset or liability (i.e., fixed rate, adjustable rate, caps, and floors) relative to the current interest rate environment. For example, in a rising interest rate environment, the fair market value of a fixed-rate asset will decline whereas the fair market value of an adjustable-rate asset, depending on its repricing characteristics, may not decline. Increases in the market value of assets will increase the PVE whereas decreases in market value of assets will decrease the PVE. Conversely, increases in the market value of liabilities will decrease the PVE whereas decreases in the market value of liabilities will increase the PVE.

The following table presents the estimated PVE over a range of interest rate change scenarios at December 31, 2012. The present value ratio shown in the table is the PVE as a percent of the present value of total assets in each of the different rate environments. For purposes of this table, management has made assumptions such as prepayment rates and decay rates similar to those used for the gap analysis table.

Change in Interest Rates (Basis Points)	Present Value of Equity			Present Value of Equity as Percent of Present Value of Assets	
	Dollar Amount	Dollar Change	Percent Change	Present Value Ratio	Percent Change
	(Dollars in thousands)				
+400	\$212,497	\$(138,752)	(39.5)%	9.50%	(33.6)%
+300	243,564	(107,685)	(30.7)	10.64	(25.7)
+200	279,983	(71,266)	(20.3)	11.93	(16.6)
+100	315,026	(36,223)	(10.3)	13.11	(8.4)
0	351,249	—	—	14.31	—
-100	340,042	(11,207)	(3.2)	13.58	(5.1)

Based on the above analysis, the Company’s PVE could be adversely affected by an increase in interest rates. The decline in the PVE as a result of an increase in rates is attributable to the combined effects of a decline in the present value of the Company’s earning assets (which is further impacted by an extension in duration in rising rate environments due to slower prepayments on loan and mortgage-related securities and reduced likelihood of calls on certain investment securities), partially offset by a decline in the present value of deposit liabilities and FHLB of Chicago advances. Also based on the above analysis, the Company’s PVE could be adversely impacted by a decrease in interest rates. However, it should be noted that the Company’s PVE is impacted by more than changes in market interest rates. Future PVE is also affected by management’s decisions relating to reinvestment of future cash flows, decisions relating to funding sources, and by other factors outlined in “Item 1. Business—Cautionary Statement,” “Item 1A. Risk Factors,” and “Item 7. Management Discussion of Financial Condition and Results of Operations.”

As is the case with gap analysis, PVE analysis also has certain shortcomings. PVE modeling requires management to make assumptions about future changes in market interest rates that are unlikely to occur, such as immediate, sustained, and parallel (or equal) changes in all market rates across all maturity terms. PVE modeling also requires that management make assumptions which may not reflect the manner in which actual yields and costs respond to changes in market interest rates. For example, it is the Company's past experience that rate changes on most of its deposit liabilities generally lag changes in market interest rates. In addition, management makes assumptions regarding the changes in prepayment speeds of mortgage loans and securities. Prepayments will accelerate in a falling rate environment and the reverse will occur in a rising rate environment. Management also assumes that decay rates on core deposits will accelerate in a rising rate environment and the reverse in a falling rate environment. The model assumes that the Company will take no action in response to the changes in interest rates, when in practice rate changes on most deposit liabilities lag behind market changes and/or may be limited by competition. In addition, prepayment estimates and other assumptions within the model are subjective in nature, involve uncertainties, and therefore cannot be determined with precision. Accordingly, although the PVE model may provide an estimate of the Company's interest rate risk at a particular point in time, such measurements are not intended to and do not provide a precise forecast of the effect of changes in interest rates on the Company's PVE. Because of these shortcomings, management of the Company believes that PVE analysis is a better indicator of the relative change in the Company's interest rate risk exposure from period to period than it is an indicator of the direction or amount of future change in net interest income.

**Item 8. Financial Statements and Supplementary Data**

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders of  
Bank Mutual Corporation  
Milwaukee, Wisconsin

We have audited the accompanying consolidated statements of financial condition of Bank Mutual Corporation and subsidiaries (the “Company”) as of December 31, 2012 and 2011, and the related consolidated statements of income, total comprehensive income, equity, and cash flows for each of the three years in the period ended December 31, 2012. 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, such consolidated financial statements present fairly, in all material respects, the financial position of Bank Mutual Corporation and subsidiaries as of December 31, 2012 and 2011, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2012, in conformity with accounting principles generally accepted in the United States of America.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company’s internal control over financial reporting as of December 31, 2012, based on the criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 8, 2013, expressed an unqualified opinion on the Company’s internal control over financial reporting.

/s/ Deloitte & Touche LLP

Milwaukee, Wisconsin  
March 8, 2013

**Bank Mutual Corporation and Subsidiaries**  
**Consolidated Statements of Financial Condition**

	December 31	
	2012	2011
	<i>(Dollars in thousands)</i>	
<b>Assets</b>		
Cash and due from banks	\$50,030	\$52,306
Interest-earning deposits in banks	37,029	68,629
Cash and cash equivalents	87,059	120,935
Mortgage-related securities available-for-sale, at fair value	550,185	781,770
Mortgage-related securities held-to-maturity, at amortized cost (fair value of \$163,589 in 2012)	157,558	—
Loans held-for-sale	10,739	19,192
Loans receivable (net of allowance for loan losses of \$21,577 in 2012 and \$27,928 in 2011)	1,402,246	1,319,636
Foreclosed properties and repossessed assets	13,961	24,724
Mortgage servicing rights, net	6,821	7,401
Other assets	189,695	224,826
	<b>\$2,418,264</b>	<b>\$2,498,484</b>
<b>Liabilities and equity</b>		
<b>Liabilities:</b>		
Deposit liabilities	\$1,867,899	\$2,021,663
Borrowings	210,786	153,091
Advance payments by borrowers for taxes and insurance	4,956	3,192
Other liabilities	59,837	51,842
Total liabilities	2,143,478	2,229,788
<b>Equity:</b>		
Preferred stock—\$0.01 par value:		
Authorized—20,000,000 shares in 2012 and 2011		
Issued and outstanding—none in 2012 and 2011	—	—
Common stock—\$0.01 par value:		
Authorized—200,000,000 shares in 2012 and 2011		
Issued—78,783,849 shares in 2012 and 2011		
Outstanding—46,326,484 shares in 2012 and 46,228,984 in 2011	788	788
Additional paid-in capital	489,960	490,159
Retained earnings	145,231	140,793
Accumulated other comprehensive income (loss)	(4,717)	(5,379)
Treasury stock—32,457,365 shares in 2012 and 32,554,865 in 2011	(359,409)	(360,590)
Total shareholders' equity	271,853	265,771
Non-controlling interest in real estate partnership	2,933	2,925
Total equity including non-controlling interest	274,786	268,696
	<b>\$2,418,264</b>	<b>\$2,498,484</b>

Refer to Notes to Consolidated Financial Statements

**Bank Mutual Corporation and Subsidiaries**

**Consolidated Statements of Income**

	Year Ended December 31		
	2012	2011	2010
	<i>(Dollars in thousands, except per share data)</i>		
Interest income:			
Loans	\$65,478	\$69,936	\$79,266
Mortgage-related securities	17,309	16,374	17,445
Investment securities	73	2,877	15,428
Interest-earning deposits	162	158	430
Total interest income	<u>83,022</u>	<u>89,345</u>	<u>112,569</u>
Interest expense:			
Deposit liabilities	14,655	19,568	28,606
Borrowings	6,984	7,183	37,664
Advance payments by borrowers for taxes and insurance	2	5	6
Total interest expense	<u>21,641</u>	<u>26,756</u>	<u>66,276</u>
Net interest income	<u>61,381</u>	<u>62,589</u>	<u>46,293</u>
Provision for loan losses	4,545	6,710	49,619
Net interest income (loss) after provision for loan losses	<u>56,836</u>	<u>55,879</u>	<u>(3,326)</u>
Non-interest income:			
Service charges on deposits	6,903	6,429	6,126
Brokerage and insurance commissions	3,009	2,844	3,067
Loan related fees and servicing revenue, net	(1,911)	(402)	103
Gain on loan sales activities, net	13,206	5,963	8,571
Gain on sales of investments, net	543	1,113	15,966
Other-than-temporary impairment ("OTTI") losses:			
Total OTTI losses	(889)	(1,794)	-
Non-credit portion of OTTI losses	489	1,405	-
Net OTTI losses	<u>(400)</u>	<u>(389)</u>	<u>-</u>
Loss on real estate held for investment	-	-	(700)
Increase in cash surrender value of life insurance	2,118	2,374	2,405
Other non-interest income	5,791	5,226	5,065
Total non-interest income	<u>29,259</u>	<u>23,158</u>	<u>40,603</u>
Non-interest expense:			
Compensation, payroll taxes, and other employee benefits	42,304	38,844	36,009
Occupancy and equipment	11,363	11,514	11,221
Federal insurance premiums	3,308	3,224	4,069
Advertising and marketing	2,139	2,008	2,114
Losses and expenses on foreclosed real estate, net	6,725	7,059	8,266
Other non-interest expense	10,218	9,681	8,798
Total non-interest expense	<u>76,057</u>	<u>72,330</u>	<u>70,477</u>
Goodwill impairment	-	52,570	-
Loss on early prepayment of FHLB borrowings	-	-	89,348
Total non-interest expense	<u>76,057</u>	<u>124,900</u>	<u>159,825</u>
Income (loss) before income taxes	<u>10,038</u>	<u>(45,863)</u>	<u>(122,548)</u>
Income tax expense (benefit)	3,336	1,752	(49,909)
Net income (loss) before non-controlling interest	<u>6,702</u>	<u>(47,615)</u>	<u>(72,639)</u>
Net loss (income) attributable to non-controlling interests	52	50	(1)
Net income (loss)	<u>\$6,754</u>	<u>\$(47,565)</u>	<u>\$(72,640)</u>
Per share data:			
Earnings (loss) per share—basic	\$0.15	\$(1.03)	\$(1.59)
Earnings (loss) per share—diluted	\$0.15	\$(1.03)	\$(1.59)
Cash dividends per share paid	\$0.05	\$0.06	\$0.20

Refer to Notes to Consolidated Financial Statements

**Bank Mutual Corporation and Subsidiaries**

**Consolidated Statements of Total Comprehensive Income**

	Year Ended December 31		
	2012	2011	2010
	<i>(Dollars in thousands)</i>		
Net income (loss) before non-controlling interest	\$6,702	\$(47,615)	\$(72,639)
Other comprehensive income (loss), net of income taxes:			
Unrealized holding gains (losses) during the period:			
Non-credit portion of OTTI on securities available-for sale, net of deferred income taxes of \$(196) in 2012 and \$(563) in 2011	(293)	(842)	-
Change in net unrealized gain on securities available-for-sale, net of deferred income taxes of \$1,593 in 2012, \$5,028 in 2011, and \$6,259 in 2010	2,378	7,511	9,347
Reclassification adjustment for gain on securities included in income, net of income taxes of \$(218) in 2012, \$(446) in 2011, and \$(6,403) in 2010	(325)	(667)	(9,563)
	<u>1,760</u>	<u>6,002</u>	<u>(216)</u>
Defined benefit pension plans:			
Pension asset, net of deferred income taxes of \$(732) in 2012, \$(2,990) in 2011, and \$(2,850) in 2010	(1,098)	(4,484)	(4,275)
	<u>(1,098)</u>	<u>(4,484)</u>	<u>(4,275)</u>
Total other comprehensive income, net of income taxes	662	1,518	(4,491)
Total comprehensive income before non-controlling interest	7,364	(46,097)	(77,130)
Comprehensive loss (income) attributable to non-controlling interest	52	50	(1)
	<u>52</u>	<u>50</u>	<u>(1)</u>
 Total comprehensive income (loss)	 <u>\$7,416</u>	 <u>\$(46,047)</u>	 <u>\$(77,131)</u>

Refer to Notes to Consolidated Financial Statements

**Bank Mutual Corporation and Subsidiaries**

**Consolidated Statements of Equity**

	Common Stock	Additional Paid-In Capital	Retained Earnings	Unearned ESOP Shares	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Non- Controlling Interest in Real Estate Partnership	Total
<i>(Dollars in thousands, except per share data)</i>								
Balance at December 31, 2009	\$788	\$499,376	\$272,518	\$(347)	\$(2,406)	\$(367,452)	\$2,924	\$405,401
Net loss	-	-	(72,640)	-	-	-	-	(72,640)
Net income attributable to non-controlling interest	-	-	-	-	-	-	1	1
Other comprehensive loss	-	-	-	-	(4,491)	-	-	(4,491)
Purchase of treasury stock	-	-	-	-	-	(5,029)	-	(5,029)
Issuance of management recognition plan shares	-	(332)	-	-	-	332	-	-
Committed ESOP shares	-	408	-	347	-	-	-	755
Exercise of stock options	-	(5,212)	-	-	-	5,596	-	384
Share based payments	-	137	-	-	-	-	-	137
Cash dividends (\$0.20 per share)	-	-	(8,640)	-	-	-	-	(8,640)
Balance at December 31, 2010	\$788	\$494,377	\$191,238	-	\$(6,897)	\$(366,553)	\$2,925	\$315,878
Net loss	-	-	(47,565)	-	-	-	-	(47,565)
Net loss attributable to non-controlling interest	-	-	-	-	-	-	(50)	(50)
Other comprehensive income	-	-	-	-	1,518	-	-	1,518
Equity contribution by non-controlling interest	-	-	-	-	-	-	50	50
Issuance of management recognition plan shares	-	(123)	-	-	-	123	-	-
Exercise of stock options	-	(4,375)	-	-	-	5,840	-	1,465
Share based payments	-	280	-	-	-	-	-	280
Cash dividends (\$0.06 per share)	-	-	(2,880)	-	-	-	-	(2,880)
Balance at December 31, 2011	\$788	\$490,159	\$140,793	-	\$(5,379)	\$(360,590)	\$2,925	\$268,696
Net income	-	-	6,754	-	-	-	-	6,754
Net loss attributable to non-controlling interest	-	-	-	-	-	-	(52)	(52)
Other comprehensive income	-	-	-	-	662	-	-	662
Equity contribution by non-controlling interest	-	-	-	-	-	-	60	60
Issuance of management recognition plan shares	-	(1,181)	-	-	-	1,181	-	-
Share based payments	-	982	-	-	-	-	-	982
Cash dividends (\$0.05 per share)	-	-	(2,316)	-	-	-	-	(2,316)
Balance at December 31, 2012	\$788	\$489,960	\$145,231	-	\$(4,717)	\$(359,409)	\$2,933	\$274,786

Refer to Notes to Consolidated Financial Statements

**Bank Mutual Corporation and Subsidiaries**

**Consolidated Statements of Cash Flows**

	Year Ended December 31		
	2012	2011	2010
	<i>(Dollars in thousands)</i>		
Operating activities:			
Net income (loss)	\$6,754	\$(47,565)	\$(72,640)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:			
Provision for loan losses	4,545	6,710	49,619
Loss on foreclosed real estate, net	5,525	4,926	6,346
Provision for depreciation	2,569	2,576	2,600
Goodwill impairment	-	52,570	-
Net OTTI losses	400	389	-
Amortization of mortgage servicing rights	3,904	2,747	3,277
Increase (decrease) in valuation on MSRs	1,528	862	(281)
Net premium amortization on securities	4,608	3,923	2,068
Loans originated for sale	(446,358)	(272,785)	(434,388)
Proceeds from loan sales	463,165	294,134	414,808
Gain on loan sales activities, net	(13,206)	(5,963)	(8,571)
Gain on sales of investments, net	(543)	(1,113)	(15,966)
Loss on real estate held for investment	-	-	700
Loss on early repayment of FHLB borrowings	-	-	89,348
Deferred income tax expense (benefit)	3,286	1,830	(32,075)
Other, net	7,850	40,591	(28,689)
Net cash provided (used) by operating activities	<u>44,027</u>	<u>83,832</u>	<u>(23,844)</u>
Investing activities:			
Purchases of investment securities available-for-sale	-	-	(3,118,204)
Proceeds from maturities of investment securities available-for-sale	-	205,825	3,506,718
Proceeds from sale of investment securities available-for-sale	20,938	21,950	-
Purchases of mortgage-related securities available-for-sale	(51,374)	(507,052)	(819,675)
Principal payments on mortgage-related securities available-for-sale	260,953	167,587	187,664
Proceeds from sale of mortgage-related securities available-for-sale	-	-	1,074,730
Purchases of mortgage-related securities held-to-maturity	(158,915)	-	-
Principal payments on mortgage-related securities held-to-maturity	902	-	-
Redemption of FHLB stock	30,251	-	-
Net decrease (increase) in loans receivable	(100,209)	(47,661)	112,261
Proceeds from sale of foreclosed properties	18,801	19,822	6,259
Net purchases of premises and equipment	(2,689)	(1,840)	(2,049)
Net cash provided (used) by investing activities	<u>18,658</u>	<u>(141,369)</u>	<u>947,704</u>

(continued)

**Bank Mutual Corporation and Subsidiaries**

**Consolidated Statements of Cash Flows (continued)**

	Year Ended December 31		
	2012	2011	2010
	<i>(Dollars in thousands)</i>		
<b>Financing activities:</b>			
Net cash outflows from deposit liabilities	\$(153,764)	\$(56,647)	\$(59,198)
Proceeds from long-term borrowings	158,935	4,270	-
Repayments on long-term borrowings, including loss on prepayment	(101,240)	(1,113)	(846,393)
Net increase in advance payments by borrowers for taxes and insurance	1,764	495	189
Cash dividends	(2,316)	(2,880)	(8,640)
Purchase of treasury stock	-	-	(5,029)
Other, net	60	1,515	385
Net cash used in financing activities	<u>(96,561)</u>	<u>(54,360)</u>	<u>(918,686)</u>
Increase (decrease) in cash and cash equivalents	(33,876)	(111,897)	5,174
Cash and cash equivalents at beginning of year	<u>120,935</u>	<u>232,832</u>	<u>227,658</u>
Cash and cash equivalents at end of year	<u>\$87,059</u>	<u>\$120,935</u>	<u>\$232,832</u>
<b>Supplemental information:</b>			
Cash received (paid) in period for:			
Interest on deposits and borrowings	\$(21,915)	\$(28,434)	\$(68,070)
Income taxes	(173)	23,412	(5,062)
Non-cash transactions:			
Loans transferred to foreclosed properties and repossessed assets	13,054	49,465	22,407

Refer to Notes to Consolidated Financial Statements

## Bank Mutual Corporation and Subsidiaries

### Notes to Consolidated Financial Statements

December 31, 2012

*(Dollars in thousands, except share and per share amounts)*

#### 1. Summary of Significant Accounting Policies

**Business** Bank Mutual Corporation (the “Company”), a Wisconsin corporation, is a federally-registered unitary savings and loan holding company which holds all of the outstanding shares of Bank Mutual, a federal savings bank (the “Bank”).

The Bank is a federal savings bank offering a full range of financial services to customers who are primarily located in the state of Wisconsin. The Bank is principally engaged in the business of attracting deposits from the general public and using such deposits to originate residential and commercial real estate loans, consumer loans, and commercial and industrial loans.

**Principles of Consolidation** The consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States. The consolidated financial statements include the accounts and transactions of the Company and its wholly-owned subsidiaries. The Bank has the following wholly-owned subsidiaries: BancMutual Financial & Investment Services, Inc., Mutual Investment Corporation, First Northern Investments, Inc., and MC Development Ltd. MC Development Ltd. owns a 50% interest in Arrowood Development LLC, which is a variable interest entity and is consolidated into the financial statements. All intercompany accounts and transactions have been eliminated in consolidation.

In preparing the consolidated financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the statement of financial condition and revenues and expenses for the period. Actual results could differ from those estimates.

**Cash and Cash Equivalents** The Company considers interest-bearing deposits in banks and federal funds sold that have original maturities of three months or less to be cash equivalents. Under Regulation D, the Bank is required to maintain cash and reserve balances with the Federal Reserve Bank of Chicago. The average amount of required reserve balances for each of the years ended December 31, 2012 and 2011, was approximately \$25.

**Federal Home Loan Bank Stock** Stock of the Federal Home Loan Bank of Chicago (“FHLB of Chicago”) is owned due to membership requirements and is carried at cost, which is its redemption value, and is included in other assets. FHLB stock is periodically reviewed for impairment based on management’s assessment of the ultimate recoverability of the investment rather than temporary declines in its estimated fair value.

**Securities Available-for-Sale and Held-to-Maturity** Available-for-sale securities are stated at fair value, with the unrealized gains and losses, net of tax, reported as a separate component of accumulated other comprehensive income (loss) in shareholders’ equity. Held-to-maturity securities are stated at amortized cost.

The amortized cost of securities classified as available-for-sale or held-to-maturity is adjusted for amortization of premiums and accretion of discounts to maturity, or in the case of mortgage-related securities, over the estimated life of the securities. Such accretion or amortization is included in interest income from investments. Interest and dividends are included in interest income from investments. Realized gains and losses and declines in value judged to be other-than-temporary are included in net gain or loss on sales of securities and are based on the specific identification method.

Impairment of available-for-sale and held-to-maturity securities is evaluated considering numerous factors, and their relative significance varies case-by-case. Factors considered include the length of time and extent to which the market value has been less than cost; the financial condition and near-term prospects of the issuer of a security; and the Company’s intent and/or likely need to sell the security before its anticipated recovery in fair value. Further, if the Company does not expect to recover the entire amortized cost of the security (i.e., a credit loss is expected), the Company will be unable to assert that it will recover its cost basis even if it does not intend to sell the security. If, based upon an analysis of each of these factors, it is determined that the impairment is other-than-temporary, the carrying value of the security is written down through earnings by the amount of the expected credit loss.

**Bank Mutual Corporation and Subsidiaries**

**Notes to Consolidated Financial Statements**

**December 31, 2012**

*(Dollars in thousands, except share and per share amounts)*

**1. Summary of Significant Accounting Policies (continued)**

***Loans Receivable and Loans Held-for-Sale*** Loans receivable are recorded at cost, net of undisbursed loan proceeds, allowance for loan losses, unamortized deferred fees and costs, and unamortized purchase premiums or discounts, if any. Loan origination and commitment fees and certain direct loan origination costs are deferred and amortized as an adjustment of loan yield. Purchase premiums and discounts are also amortized as an adjustment of yield.

Loans held-for-sale, which generally consists of recently originated fixed-rate residential mortgage loans, are recorded at market value determined on an individual loan basis. Fees received from the borrower are deferred and recorded as an adjustment of the carrying value.

***Accrued Interest on Loans*** Interest on loans receivable is accrued and credited to income as earned. The Company measures the past due status of a loan by the number of days that have elapsed since the borrower has failed to make a contractual loan payment. Accrual of interest is generally discontinued when either (i) reasonable doubt exists as to the full, timely collection of interest or principal or (ii) when a loan becomes past due by more than 90 days. At that time, the loan is considered impaired and any accrued but uncollected interest is reversed. Additional interest income is recorded only to the extent that payments are received, collection of the principal is reasonably assured, and/or the net recorded investment in the loan is deemed to be collectible. Loans are generally restored to accrual status when the obligation is brought to a current status by the borrower.

***Allowance for Loan Losses and Impaired Loans*** The Company classifies its loan portfolio into six segments for purposes of determining its allowance for loan losses: one- to four-family, multi-family, commercial real estate, construction and development, consumer, and commercial business loans. This segmentation is based on the nature of the loan collateral and the purpose of the loan, which in the judgment of management are the primary risk characteristics that determine the allowance for loan loss. Loans in the one- to four-family, multi-family, and commercial real estate segments are secured principally by real estate. Loans in the consumer segment may be secured by real estate (such as of home equity loans and lines of credit), by personal property (such as automobiles), or may be unsecured. Loans in the commercial business segment are typically secured by equipment, inventory, receivables, other business assets, and in some instances, business and personal real estate, or may be unsecured. The commercial real estate segment consists of non-residential loans secured by office, retail/wholesale, industrial/warehouse, and other properties. The construction and development segment consists of loans secured by one- to four-family, multi-family, commercial real estate, and developed and undeveloped land.

The allowance for loan losses for each segment is maintained at a level believed adequate by management to absorb probable losses inherent in each segment and is based on factors such as the size and current risk characteristics of the segments, an assessment of individual problem loans and pools of homogenous loans within the segments, and actual loss, delinquency, and/or risk rating experience within the segments. The Company also considers current economic conditions and/or events in specific industries and geographical areas, including unemployment levels, trends in real estate values, peer comparisons, and other pertinent factors, to include regulatory guidance. Finally, as appropriate, the Company also considers individual borrower circumstances and the condition and fair value of the loan collateral, if any.

The allowance for loan losses for each segment is determined using a combined approach. Individual loans in the segments that have been identified as impaired are analyzed individually to determine an appropriate allowance for loan loss. In addition, the allowance for loan losses for each segment is augmented using a homogenous pool approach for loans in each segment that are current and/or have not been individually identified as impaired loans. The homogenous approach utilizes loss rates that are developed by management using the qualitative factors and other considerations outlined in the previous paragraph.

Loans are considered impaired when they are identified as such by the Company's internal risk rating and loss evaluation process or when contractually past due 90 days or more with respect to interest or principal. Factors that

## Bank Mutual Corporation and Subsidiaries

### Notes to Consolidated Financial Statements

December 31, 2012

*(Dollars in thousands, except share and per share amounts)*

#### 1. Summary of Significant Accounting Policies (continued)

indicate impairment include, but are not limited to, deterioration in a borrower's financial condition, performance, or outlook, decline in the condition, performance, or fair value of the collateral for the loan (if any), payment or other default on the loan, and adverse economic or market developments in the borrower's region or business segment. Accrual of interest is typically discontinued on impaired loans, although from time-to-time the Company may continue to accrue interest and/or recognize interest income on impaired loans when payments are being received and, in the judgment of management, collection of the principal is reasonably assured and/or the net recorded investment in the loan is deemed to be collectible.

The Company has various policies and procedures in place to monitor its exposure to credit risk including, but not limited to, a formal risk rating process, periodic loan delinquency reporting, periodic loan file reviews, financial updates from and visits to borrowers, and established past-due loan collection procedures. The Company formally evaluates its allowance for loan losses on a quarterly basis or more often as deemed necessary. A provision for loan loss is charged to operations based on this periodic evaluation. Actual loan losses are charged off against the allowance for loan losses, while recoveries of amounts previously charged off are credited to the allowance.

Determination of the allowance is inherently subjective as it requires significant estimates, including the amounts and timing of expected future cash flows on loans, the fair value of underlying collateral (if any), estimated losses on pools of homogeneous loans based on historical loss experience, changes in risk characteristics of the loan portfolio, and consideration of current economic trends, all of which may be susceptible to significant change.

***Mortgage Servicing Rights*** Mortgage servicing rights are recorded as an asset when loans are sold with servicing rights retained. The total cost of loans sold is allocated between the loan balance and their servicing asset based on their relative fair values. The capitalized value of mortgage servicing rights is amortized in proportion to, and over the period of, estimated net future servicing revenue. Mortgage servicing rights are carried at the lower of the initial carrying value, adjusted for amortization, or estimated fair value. The carrying values are periodically evaluated for impairment. For purposes of measuring impairment, the servicing rights are stratified into pools based on term and interest rate. Impairment represents the excess of the remaining capitalized cost of a stratified pool over its fair value, and is recorded through a valuation allowance. The fair value of each servicing rights pool is calculated based on the present value of estimated future cash flows using a discount rate, given current market conditions. Estimates of fair value include assumptions about prepayment speeds, 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, if any, to change significantly in the future.

***Mortgage Banking Loan Commitments*** In connection with its mortgage banking activities, the Company enters into loan commitments to fund residential mortgage loans at specified interest rates and within specified periods of time, generally up to 60 days from the time of rate lock. A loan commitment whose loan arising from exercise of the loan commitment will be held for sale upon funding is a derivative instrument, which must be recognized at fair value on the consolidated balance sheet in other assets and other liabilities with changes in its value recorded in income from mortgage banking operations.

In determining the fair value of its derivative loan commitments for economic purposes, the Company considers the value that would be generated when the loan arising from exercise of the loan commitment is sold in the secondary mortgage market. That value includes the price that the loan is expected to be sold for in the secondary mortgage market.

***Foreclosed Properties and Repossessed Assets*** Foreclosed properties acquired through, or in lieu of, loan foreclosure are recorded at the lower of cost or fair value less estimated costs to sell. Costs related to the development and improvement of property are capitalized provided such costs do not result in a carrying value in excess of the property's fair value less estimated costs to sell, in which case such costs are expensed.

## Bank Mutual Corporation and Subsidiaries

### Notes to Consolidated Financial Statements

December 31, 2012

*(Dollars in thousands, except share and per share amounts)*

#### 1. Summary of Significant Accounting Policies (continued)

Costs related to holding the property are expensed. Gains and losses on sales are recognized based on the carrying value upon closing of the sale.

**Premises and Equipment** Land, buildings, leasehold improvements and equipment are carried at amortized cost. Buildings and equipment are depreciated over their estimated useful lives (office buildings 40 to 44 years and furniture and equipment 3 to 10 years) using the straight-line method. Leasehold improvements are amortized over the shorter of their useful lives or expected lease terms. The Company reviews buildings, leasehold improvements and equipment for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Impairment exists when the estimated undiscounted cash flows for the property are less than its carrying value. If identified, an impairment loss is recognized through a charge to earnings based on the fair value of the property.

**Goodwill** In 2011 the Company determined that goodwill recorded as a result of the purchase of financial institutions in 1997 and 2000 was impaired. The Company performed an interim goodwill impairment test during that period as a result of a number of developments including the decline in the Company's stock price and market capitalization and the announcement that the Company and Bank had each entered into a separate MOU with their primary regulators (these MOUs were terminated in 2013). To determine the fair value of goodwill, as well as the amount of the impairment, the Company obtained a third-party independent appraisal of the Company, which consists of a single reporting unit, and its assets and liabilities. The fair value of the Company was estimated using a weighted average of three valuation methodologies, including a public market peers approach, a comparable transactions approach, and a discounted cash flow approach. A comparison of the weighted average value from these approaches to the net carrying value of the Company indicated that potential impairment existed. The weighted average value of the Company was subsequently compared to the estimated net fair value of the Company's individual assets and liabilities. As a result of this comparison, the Company concluded that goodwill was impaired and recorded an impairment charge of \$52,570 in 2011, which represented the total amount of the Company's goodwill. The goodwill impairment was not deductible for income tax purposes.

**Life Insurance Policies** Investments in life insurance policies owned by the Company are carried at the amount that could be realized under the insurance contract if the Company cashed them in on the respective dates.

**Income Taxes** The Company files consolidated federal and combined state income tax returns. A deferred tax asset or liability is determined based on the enacted tax rates that will be in effect when the differences between the financial statement carrying amounts and tax basis of existing assets and liabilities are expected to be reported in the Company's income tax returns. The effect on deferred taxes of a change in tax rates is recognized in income in the period that includes the enactment date of the change. A valuation allowance is provided for any deferred tax asset for which it is more likely than not that the asset will not be realized. Changes in valuation allowances are recorded as a component of income taxes.

**Earnings (Loss) Per Share** Basic and diluted earnings (loss) per share ("EPS") are computed by dividing net income (loss) by the weighted-average number of common shares outstanding for the period. ESOP shares committed to be released are considered outstanding for basic EPS calculations. Vested shares of restricted stock which have been awarded under the management recognition plan ("MRP") provisions of the Company's 2004 Stock Incentive Plan are also considered outstanding for basic EPS. Non-vested MRP and stock option shares are considered dilutive potential common shares and are included in the weighted-average number of shares outstanding for diluted EPS.

**Pension Costs** The Company has both defined benefit and defined contribution plans. The Company's net periodic pension cost of the defined benefit plans consist of the expected cost of benefits earned by employees during the current period and an interest cost on the projected benefit obligation, reduced by the expected earnings on assets

## Bank Mutual Corporation and Subsidiaries

### Notes to Consolidated Financial Statements

December 31, 2012

*(Dollars in thousands, except share and per share amounts)*

#### 1. Summary of Significant Accounting Policies (continued)

held by the plans, amortization of prior service cost, and amortization of recognized actuarial gains and losses over the estimated future service period of existing plan participants. The costs associated with the defined contribution plan consist of a predetermined percentage of compensation, which is determined by the Company's board of directors.

**Segment Information** The Company has determined that it has one reportable segment—community banking. The Company offers a range of financial products and services to external customers, including: accepting deposits from the general public; originating residential, consumer and commercial loans; and marketing annuities and other insurance products.

**Recent Accounting Changes** In July 2010 the FASB issued new accounting guidance related to certain disclosures about the credit quality of financing receivables, allowances for credit losses, and troubled debt restructurings. Certain aspects of the new guidance were effective for reporting periods ending after December 15, 2010, which for the Company was the fourth quarter of 2010. Certain other aspects of the new guidance, as subsequently amended, were not effective until the accounting periods beginning after June 15, 2011, which for the Company was the third quarter of 2011. The Company's adoption of this new guidance had no impact on its financial condition, results of operations or liquidity, although it does affect matters that are disclosed in the financial statements related to the Company's loans receivable.

In December 2010 the FASB issued new accounting guidance clarifying the presentation of pro forma information required for business combinations when a public company presents comparative financial information. The amendments in this guidance were effective prospectively for business combinations for which the acquisition date was on or after the first annual reporting period beginning on or after December 15, 2010, which for the Company was the first quarter of 2011. This new accounting guidance did not have an impact on the Company's financial condition, results of operations, or liquidity, but it may impact future financial disclosures if the Company were to engage in a future business combination.

During the second quarter of 2011 the FASB issued new accounting guidelines related to (i) accounting for repurchase agreements, (ii) certain fair value measurements of assets, liability, and instruments classified in shareholders' equity, and (iii) presentation of net income, other comprehensive income, and total comprehensive income (certain aspects the adoption of which were deferred indefinitely in the fourth quarter of 2011). These new guidelines were effective for the first interim period beginning on or after December 15, 2011, which was the first quarter of 2012 for the Company. The Company's adoption of these guidelines did not have a material impact on its financial condition, results of operations, or liquidity. However, the guidelines do affect how matters are disclosed in the financial statements.

During the fourth quarter of 2011 the FASB issued new accounting guidelines related to (i) the determination of whether a parent should derecognize the in-substance real estate of a subsidiary that is in-substance real estate when the parent ceases to have a controlling financial interest in the subsidiary and (ii) the disclosure of both gross information and net information about instruments eligible for offset in the statement of financial position and instruments and transactions subject to an agreement similar to a master netting agreement. Item (i) was effective for the Company in the third quarter of 2012. The adoption of this item did not have a material impact on its financial condition, results of operation, or liquidity. Item (ii) will be effective for interim and fiscal periods beginning on or after January 1, 2013, which for the Company will be the first quarter of 2013. The Company's adoption of item (ii) is not expected to have a material impact on its financial condition, results of operations, or liquidity. However, the new guidelines may affect matters that will be disclosed in the financial statements.

During the third quarter of 2012 the FASB issued new accounting guidance related to testing indefinite-lived intangible assets for impairment. This new guidance is effective for years beginning after September 15, 2012,

**Bank Mutual Corporation and Subsidiaries**

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**1. Summary of Significant Accounting Policies (continued)**

which will be the first quarter of 2013 for the Company. The Company's adoption of this new guidance is not expected to have a material impact in its financial condition, results of operations, or liquidity.

During the fourth quarter of 2012 the FASB issued new accounting guidance related to subsequent measurement of an indemnification asset recognized in a government-assisted acquisition of a financial institution. This new guidance is effective for fiscal years beginning on or after December 15, 2012, which is the first quarter of 2013 for the Company. The Company has not engaged in these types of transactions. As such, the Company's adoption of this new guidance is not expected to have a material impact in its financial condition, results of operations, or liquidity.

**2. Mortgage-Related Securities Available-for-Sale and Held-to-Maturity**

The amortized cost and fair value of mortgage-related securities available-for-sale and held-to-maturity are as follows:

	December 31, 2012			Estimated Fair Value
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	
<b>Securities available-for-sale:</b>				
Federal Home Loan Mortgage Corporation	\$336,289	\$7,393	–	\$343,682
Federal National Mortgage Association	153,010	2,885	–	155,895
Government National Mortgage Association	36	6	–	42
Private-label CMOs	50,196	1,108	\$(738)	50,566
Total available-for-sale	<u>\$539,531</u>	<u>\$11,392</u>	<u>\$(738)</u>	<u>\$550,185</u>
<b>Securities held-to-maturity:</b>				
Federal National Mortgage Association	\$157,558	\$6,031	–	\$163,589
Total held-to-maturity	<u>\$157,558</u>	<u>\$6,031</u>	<u>–</u>	<u>\$163,589</u>
	December 31, 2011			Estimated Fair Value
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	
<b>Securities available-for-sale:</b>				
Federal Home Loan Mortgage Corporation	\$537,935	\$11,009	–	\$548,944
Federal National Mortgage Association	167,601	2,476	\$(57)	170,020
Government National Mortgage Association	767	10	–	777
Private-label CMOs	67,754	540	(6,265)	62,029
Total available-for-sale	<u>\$774,057</u>	<u>\$14,035</u>	<u>\$(6,322)</u>	<u>\$781,770</u>

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**2. Mortgage-Related Securities Available-for-Sale and Held-to-Maturity (continued)**

The following tables identify mortgage-related securities by amount of time the securities have had a gross unrealized loss as of the dates indicated:

	December 31, 2012							
	Less Than 12 Months in an Unrealized Loss Position			Greater Than 12 Months in an Unrealized Loss Position			Gross Unrealized Loss Amount	Total Estimated Fair Value
	Unrealized Loss Amount	Number of Securities	Estimated Fair Value	Unrealized Loss Amount	Number of Securities	Estimated Fair Value		
Securities available-for-sale: Private-label CMOs	\$500	4	\$9,703	\$238	5	\$7,578	\$738	\$17,281
Total mortgage-related securities	\$500	4	\$9,703	\$238	5	\$7,578	\$738	\$17,281

	December 31, 2011							
	Less Than 12 Months in an Unrealized Loss Position			Greater Than 12 Months in an Unrealized Loss Position			Gross Unrealized Loss Amount	Total Estimated Fair Value
	Unrealized Loss Amount	Number of Securities	Estimated Fair Value	Unrealized Loss Amount	Number of Securities	Estimated Fair Value		
Securities available-for-sale: Federal National Mortgage Association	\$57	1	\$9,603	—	—	—	\$57	\$9,603
Private-label CMOs	1	1	448	\$6,264	20	\$40,523	6,265	40,971
Total mortgage-related securities	\$58	2	\$10,051	\$6,264	20	\$40,523	\$6,322	\$50,574

Certain of the Company's available-for-sale securities that were in an unrealized loss position at December 31, 2011, consisted of mortgage-related securities issued by government-sponsored entities. As of those dates, the Company believed that it was probable that it would receive all future contractual cash flows related to such securities. The Company does not intend to sell the securities and it is unlikely that it would be required to sell the securities before the recovery of their amortized cost. Accordingly, the Company determined that the unrealized loss on mortgage-related securities issued by government-sponsored entities was temporary as of December 31, 2011.

Except as noted below, the Company also determined that the unrealized loss on its private-label CMOs was temporary as of December 31, 2012 and 2011. The Company does not intend to sell these securities and it is unlikely that it will be required to sell these securities before the recovery of their amortized cost. The Company believes it is probable that it will receive all future contractual cash flows related to these securities. This determination was based on management's judgment regarding the nature of the loan collateral that supports the securities, a review of the current ratings issued on the securities by various credit rating agencies, a review of the actual delinquency and/or default performance of the loan collateral that supports the securities, and recent trends in the fair market values of the securities.

As of December 31, 2012 and 2011, the Company had private-label CMOs with a fair value of \$35,918 and \$36,751 respectively, and unrealized losses of \$33 and \$5,357, respectively, that were rated less than investment grade. These private-label CMOs were analyzed using modeling techniques that considered the priority of cash flows in the

**Bank Mutual Corporation and Subsidiaries**

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**2. Mortgage-Related Securities Available-for-Sale and Held-to-Maturity (continued)**

CMO structure and various default and loss rate scenarios that management considered appropriate given the nature of the loan collateral. In 2012 and 2011 the Company recognized \$400 and \$389, respectively, in net OTTI losses related to its investment on a number of private-label CMOs. The determination of these net OTTI losses was based on modeling techniques that considered the priority of cash flows in the CMO structure and various default and loss rate scenarios that management considered appropriate given the nature of the loan collateral. The following assumptions were used in determining the amount of the credit loss in 2012: (i) prepayment speeds with a range of 5.5% to 16.5% and a weighted average rate of 9.9%, (ii) default rates with a range of 4.0% to 5.5% and a weighted average rate of 4.4%, (iii) loss severity rates with a range of 40.0% to 52.0% and a weighted average rate of 42.1%, and (iv) current credit enhancements with a range of 0.5% to 4.6% and a weighted average rate of 3.0%. The following assumptions were used in determining the amount of the credit loss in 2011: (i) prepayment speeds with a range of 6.1% to 14.9% and a weighted average rate of 11.6%, (ii) default rates with a range of 3.7% to 5.2% and a weighted average rate of 4.4%, (iii) loss severity rates with a range of 40.0% to 43.0% and a weighted average rate of 40.8%, and (iv) current credit enhancements with a range of 5.1% to 6.7% and a weighted average rate of 5.6%.

The following table contains a summary of OTTI related to credit losses that have been recognized in earnings as of the dates indicated, as well as the end of period values for securities that have experienced such losses:

	Year Ended December 31		
	2012	2011	2010
Beginning balance of unrealized OTTI related to credit losses	\$389	–	–
Additional unrealized OTTI related to credit losses for which OTTI was not previously recognized	146	\$389	–
Additional unrealized OTTI related to credit losses for which OTTI was previously recognized	254	–	–
Net OTTI losses recognized in earnings	400	389	–
Ending balance of unrealized OTTI related to credit losses	\$789	\$389	–
Adjusted cost at end of period	\$9,541	\$8,275	–
Estimated fair value at end of period	\$9,908	\$6,871	–

Results of operations included gross realized gains on the sale of securities available-for-sale of \$543, \$1,113, and \$16,041, 2012, 2011, and 2010, respectively. Gross realized losses on the sale of securities available-for-sale was zero for and 2012 and 2011, and \$75 for 2010.

Mortgage-related securities with a fair value of approximately \$80,274 and \$91,731 at December 31, 2012 and 2011, respectively, were pledged to secure deposits, FHLB advances, and for other purposes as permitted or required by law.

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**3. Loans Receivable**

Loans receivable is summarized as follows:

	December 31	
	2012	2011
Permanent mortgage loans:		
One- to four-family	\$465,170	\$508,503
Multi-family	264,013	247,040
Commercial real estate	263,775	226,195
Total permanent mortgages	<u>992,958</u>	<u>981,738</u>
Construction and development loans:		
One- to four-family	18,502	16,263
Multi-family	86,904	29,409
Commercial real estate	11,116	19,907
Land	12,826	16,429
Total construction and development	<u>129,348</u>	<u>82,008</u>
Total mortgage loans	<u>1,122,306</u>	<u>1,063,746</u>
Consumer loans:		
Fixed term home equity	116,988	102,561
Home equity lines of credit	81,898	86,540
Student	12,915	15,711
Home improvement	24,910	24,237
Automobile	1,814	2,228
Other	8,388	7,177
Total consumer loans	<u>246,913</u>	<u>238,454</u>
Commercial business loans	<u>132,436</u>	<u>87,715</u>
Gross loans receivable	1,501,655	1,389,915
Undisbursed loan proceeds	(76,703)	(41,859)
Allowance for loan losses	(21,577)	(27,928)
Deferred fees and costs, net	(1,129)	(492)
Total loans receivable, net	<u>\$1,402,246</u>	<u>\$1,319,636</u>

The Company's first mortgage loans and home equity lines of credit are primarily secured by properties that are located in the Company's local lending areas in Wisconsin, Illinois, Michigan, and Minnesota.

At December 31, 2012 and 2011, certain one- to four-family mortgage loans, multi-family mortgage loans, and home equity loans with aggregate carrying values of approximately \$281,000 and \$204,000, respectively, were pledged to secure FHLB advances.

The unpaid principal balance of loans serviced for others was \$1,147,722 and \$1,102,126 at December 31, 2012 and 2011, respectively. These loans are not reflected in the consolidated financial statements.

**Bank Mutual Corporation and Subsidiaries**

**Notes to Consolidated Financial Statements**

**December 31, 2012**

*(Dollars in thousands, except share and per share amounts)*

**3. Loans Receivable (continued)**

The following tables summarize the allowance for loan losses by loan portfolio segment during the periods indicated. The tables also summarize the allowance for loan loss and loans receivable as of the dates indicated by the nature of the impairment evaluation, either individually or collectively (the loans receivable amounts in the table are net of undisbursed loan proceeds).

	December 31, 2012						
	One- to Four- Family	Multi- Family	Commercial Real Estate	Construction and Development	Consumer	Commercial Business	Total
Allowance for loan losses:							
Beginning balance	\$3,201	\$7,442	\$9,467	\$4,506	\$1,214	\$2,098	\$27,928
Provision	3,162	(1,958)	1,825	803	1,015	(302)	4,545
Charge-offs	(3,182)	(857)	(4,894)	(2,693)	(812)	(136)	(12,574)
Recoveries	86	568	956	1	41	26	1,678
Ending balance	\$3,267	\$5,195	\$7,354	\$2,617	\$1,458	\$1,686	\$21,577
Loss allowance individually evaluated for impairment	\$191	\$914	\$123	\$295	\$456	\$62	\$2,041
Loss allowance collectively evaluated for impairment	\$3,076	\$4,281	\$7,231	\$2,322	\$1,002	\$1,624	\$19,536
Loan receivable balances at December 31, 2012:							
Loans individually evaluated for impairment	\$8,344	\$6,967	\$24,130	\$14,825	\$1,631	\$1,741	\$57,638
Loans collectively evaluated for impairment	451,154	257,046	239,645	43,492	245,282	130,695	1,367,314
Total loans receivable	\$459,498	\$264,013	\$263,775	\$58,317	\$246,913	\$132,436	\$1,424,952
	December 31, 2011						
	One- to Four- Family	Multi- Family	Commercial Real Estate	Construction and Development	Consumer	Commercial Business	Total
Allowance for loan losses:							
Beginning balance	\$3,726	\$9,265	\$21,885	\$10,141	\$1,427	\$1,541	\$47,985
Provision	2,473	199	802	1,343	803	1,090	6,710
Charge-offs	(3,047)	(5,035)	(15,286)	(2,737)	(1,036)	(551)	(27,692)
Recoveries	49	248	40	550	20	18	925
Transfers	-	2,765	2,026	(4,791)	-	-	-
Ending balance	\$3,201	\$7,442	\$9,467	\$4,506	\$1,214	\$2,098	\$27,928
Loss allowance individually evaluated for impairment	\$364	\$2,357	\$1,884	\$3,196	\$376	\$128	\$8,305
Loss allowance collectively evaluated for impairment	\$2,837	\$5,085	\$7,583	\$1,310	\$838	\$1,970	\$19,623
Loan receivable balances at December 31, 2011:							
Loans individually evaluated for impairment	\$16,075	\$24,108	\$37,006	\$20,075	\$1,695	\$4,668	\$103,627
Loans collectively evaluated for impairment	486,456	222,711	187,230	28,226	236,759	83,047	1,244,429
Total loans receivable	\$502,531	\$246,819	\$224,236	\$48,301	\$238,454	\$87,715	\$1,348,056

**Bank Mutual Corporation and Subsidiaries**

**Notes to Consolidated Financial Statements**

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**3. Loans Receivable (continued)**

	December 31, 2010						
	One- to Four- Family	Multi- Family	Commercial Real Estate	Construction and Development	Consumer	Commercial Business	Total
Allowance for loan losses:							
Beginning balance	\$2,806	\$3,167	\$5,715	\$1,172	\$2,243	\$1,925	\$17,028
Provision	1,428	6,238	27,790	12,484	(77)	1,756	49,619
Charge-offs	(528)	(140)	(11,621)	(3,515)	(776)	(2,140)	(18,720)
Recoveries	20	-	1	-	37	-	58
Ending balance	\$3,726	\$9,265	\$21,885	\$10,141	\$1,427	\$1,541	\$47,985
Loss allowance individually evaluated for impairment	\$1,122	\$7,134	\$12,853	\$9,384	\$641	\$437	\$31,571
Loss allowance collectively evaluated for impairment	\$2,604	\$2,131	\$9,032	\$757	\$786	\$1,104	\$16,414
Loan receivable balances at December 31, 2010:							
Loans individually evaluated for impairment	\$18,972	\$40,675	\$55,849	\$27,607	\$1,763	\$4,799	\$149,665
Loans collectively evaluated for impairment	505,100	206,034	189,536	34,442	241,673	45,653	1,222,438
Total loans receivable	\$524,072	\$246,709	\$245,385	\$62,049	\$243,336	\$50,452	\$1,372,103

The Company adjusts certain factors used to determine the allowance for loan losses on loans that are collectively evaluated for impairment. Management considered these adjustments necessary and prudent in light of trends in real estate values, economic conditions, and unemployment. The Company estimates that these changes, as well as overall changes in the balance of loans to which the various factors were applied, resulted in a reduction of \$87 in 2012 and an increase of \$3,209 and \$7,636 in 2011 and 2010, respectively, in the total allowance for loan losses. The transfers noted in 2011 were the result of reclassifying certain construction loans to permanent loans as a result of completed construction.

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**3. Loans Receivable (continued)**

The following tables present information regarding impaired loans that have a related allowance for loan loss and those that do not as of the dates indicated (the loans receivable amounts in the tables are net of undisbursed loan proceeds):

	December 31, 2012				
	Loans Receivable Balance, Net	Unpaid Principal Balance	Related Allowance for Loss	Average Loan Receivable Balance, Net	Interest Income Recognized
Impaired loans with an allowance recorded:					
One- to four-family	\$797	\$797	\$191	\$2,528	-
Multi-family	3,875	4,038	914	12,701	\$106
Commercial real estate:					
Office	132	143	74	992	1
Retail/wholesale/mixed	516	535	49	1,833	19
Industrial/warehouse	-	-	-	379	-
Other	-	-	-	240	-
Total commercial real estate	648	678	123	3,444	20
Construction and development:					
One- to four-family	-	-	-	69	-
Multi-family	-	-	-	1,117	-
Commercial real estate	-	-	-	689	-
Land	500	530	295	2,069	3
Total construction and development	500	530	295	3,944	3
Consumer:					
Home equity	424	424	397	354	-
Student	-	-	-	-	-
Other	59	59	59	77	-
Total consumer	483	483	456	431	-
Commercial business:					
Term loans	102	108	62	207	1
Lines of credit	-	-	-	37	-
Total commercial business	102	108	62	244	1
Total with an allowance recorded	\$6,405	\$6,634	\$2,041	\$23,292	\$130
Impaired loans with no allowance recorded:					
One- to four-family	\$7,395	\$8,897	-	\$9,426	\$219
Multi-family	2,949	4,952	-	4,286	478
Commercial real estate:					
Office	1,328	2,005	-	3,163	41
Retail/wholesale/mixed	4,790	8,861	-	6,704	270
Industrial/warehouse	228	325	-	609	16
Other	-	292	-	978	-
Total commercial real estate	6,346	11,483	-	11,454	327
Construction and development:					
One- to four-family	-	-	-	19	-
Multi-family	-	107	-	29	-
Commercial real estate	-	-	-	685	-
Land	437	1,936	-	1,019	8
Total construction and development	437	2,043	-	1,752	8
Consumer:					
Home equity	1,090	1,090	-	1,041	42
Student	-	-	-	-	-
Other	-	13	-	87	4
Total consumer	1,090	1,103	-	1,128	46
Commercial business:					
Term loans	533	684	-	632	29
Lines of credit	58	173	-	382	4
Total commercial business	591	857	-	1,014	33
Total with no allowance recorded	\$18,808	\$29,335	-	\$29,060	\$1,111

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**3. Loans Receivable (continued)**

	December 31, 2011				
	Loans Receivable Balance, Net	Unpaid Principal Balance	Related Allowance for Loss	Average Loan Receivable Balance, Net	Interest Income Recognized
Impaired loans with an allowance recorded:					
One- to four-family	\$2,606	\$2,606	\$364	\$3,916	\$51
Multi-family	19,006	19,106	2,357	23,158	851
Commercial real estate:					
Office	2,474	2,474	746	7,917	30
Retail/wholesale/mixed	3,220	3,225	570	16,931	78
Industrial/warehouse	1,250	1,250	250	1,286	-
Other	959	964	318	1,175	67
Total commercial real estate	7,903	7,913	1,884	27,309	175
Construction and development:					
One- to four-family	-	-	-	-	-
Multi-family	4,466	4,488	678	4,482	248
Commercial real estate	152	153	84	1,908	11
Land	2,993	2,995	2,434	2,944	58
Total construction and development	7,611	7,636	3,196	9,334	317
Consumer:					
Home equity	413	413	327	446	-
Student	-	-	-	-	-
Other	67	67	49	126	-
Total consumer	480	480	376	572	-
Commercial business:					
Term loans	164	165	83	690	15
Lines of credit	117	117	45	324	5
Total commercial business	281	282	128	1,014	20
Total with an allowance recorded	\$37,887	\$38,023	\$8,305	\$65,303	\$1,414
Impaired loans with no allowance recorded:					
One- to four-family	\$12,262	\$13,645	-	\$12,382	\$264
Multi-family	3,899	4,413	-	7,117	306
Commercial real estate:					
Office	6,580	8,520	-	2,937	375
Retail/wholesale/mixed	8,716	15,318	-	7,797	712
Industrial/warehouse	530	754	-	1,146	25
Other	268	1,044	-	673	9
Total commercial real estate	16,094	25,636	-	12,553	1,121
Construction and development:					
One- to four-family	-	-	-	-	-
Multi-family	-	-	-	20	-
Commercial real estate	-	-	-	2,459	-
Land	1,757	1,967	-	3,219	28
Total construction and development	1,757	1,967	-	5,698	28
Consumer:					
Home equity	1,044	1,044	-	962	43
Student	-	-	-	-	-
Other	140	140	-	110	4
Total consumer	1,184	1,184	-	1,072	47
Commercial business:					
Term loans	787	896	-	825	44
Lines of credit	574	699	-	268	40
Total commercial business	1,361	1,595	-	1,094	84
Total with no allowance recorded	\$36,557	\$48,440	-	\$39,915	\$1,850

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*(Dollars in thousands, except share and per share amounts)*

**3. Loans Receivable (continued)**

The following tables present information relating to the Company's internal risk ratings of its loans receivable as of the dates indicated (all amounts in the tables are net of undisbursed loan proceeds):

	December 31, 2012				
	Pass	Watch	Special Mention	Substandard	Total
One- to four-family	\$450,078	\$948	\$128	\$8,344	\$459,498
Multi-family	218,918	36,126	2,002	6,967	264,013
Commercial real estate:					
Office	44,678	10,938	15,471	5,605	76,692
Retail/wholesale/mixed use	90,668	11,102	15,949	14,657	132,376
Industrial/warehouse	39,758	5,031	1,292	1,266	47,347
Other	4,758	-	-	2,602	7,360
Total commercial real estate	179,862	27,071	32,712	24,130	263,775
Construction and development:					
One- to four-family	10,259	-	-	-	10,259
Multi-family	14,656	-	-	12,621	27,277
Commercial real estate	7,425	-	621	-	8,046
Land	10,392	139	-	2,204	12,735
Total construction/development	42,732	139	621	14,825	58,317
Consumer:					
Home equity	222,282	-	-	1,514	223,796
Student	12,915	-	-	-	12,915
Other	10,085	-	-	117	10,202
Total consumer	245,282	-	-	1,631	246,913
Commercial business:					
Term loans	67,879	1,651	280	943	70,753
Lines of credit	56,127	2,772	1,986	798	61,683
Total commercial business	124,006	4,423	2,266	1,741	132,436
Total	\$1,260,878	\$68,707	\$37,729	\$57,638	\$1,424,952

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**3. Loans Receivable (continued)**

	December 31, 2011				
	Pass	Watch	Special Mention	Substandard	Total
One- to four-family	\$482,271	\$4,044	\$141	\$16,075	\$502,531
Multi-family	196,231	18,123	8,357	24,108	246,819
Commercial real estate:					
Office	49,324	1,853	20,405	9,054	80,636
Retail/wholesale/mixed use	50,108	9,376	19,870	19,849	99,203
Industrial/warehouse	24,431	3,237	2,230	5,698	35,596
Other	4,897	1,318	181	2,405	8,801
Total commercial real estate	128,760	15,784	42,686	37,006	224,236
Construction and development:					
One- to four-family	7,704	—	—	—	7,704
Multi-family	4,503	—	—	14,347	18,850
Commercial real estate	4,411	—	—	908	5,319
Land	11,125	299	184	4,820	16,428
Total construction/development	27,743	299	184	20,075	48,301
Consumer:					
Home equity	211,834	—	—	1,505	213,339
Student	15,711	—	—	—	15,711
Other	9,214	—	—	190	9,404
Total consumer	236,759	—	—	1,695	238,454
Commercial business:					
Term loans	35,433	1,342	—	2,823	39,598
Lines of credit	44,291	1,729	252	1,845	48,117
Total commercial business	79,724	3,071	252	4,668	87,715
Total	\$1,151,488	\$41,321	\$51,620	\$103,627	\$1,348,056

Loans rated “pass” or “watch” are generally current on contractual loan and principal payments and comply with other contractual loan terms. Pass loans generally have no noticeable credit deficiencies or potential weaknesses. Loans rated watch, however, will typically exhibit early signs of credit deficiencies or potential weaknesses that deserve management’s close attention. Loans rated “special mention” do not currently expose the Company to a sufficient degree of risk to warrant a lower rating, but possess clear trends in credit deficiencies or potential weaknesses that deserve management’s close attention. The allowance for loan losses on loans rated pass, watch, or special mention is typically evaluated collectively for impairment using a homogenous pool approach. This approach utilizes quantitative factors developed by management from its assessment of historical loss experience, qualitative factors, and other considerations.

Loans rated “substandard” involve a distinct possibility that the Company could sustain some loss if deficiencies associated with the loan are not corrected. Loans rated “doubtful” indicate that full collection is highly questionable or improbable. The Company did not have any loans that were rated doubtful at December 31, 2012 and 2011. Loans rated substandard or doubtful that are also considered in management’s judgment to be impaired are generally analyzed individually to determine an appropriate allowance for loan loss. A loan rated “loss” is considered uncollectible, even if a partial recovery could be expected in the future. The Company generally charges off loans that are rated as a loss. As such, the Company did not have any loans that were rated loss at December 31, 2012 and 2011.

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**3. Loans Receivable (continued)**

The following tables contain information relating to the past due and non-accrual status of the Company's loans receivable as of the dates indicated (all amounts in the table are net of undisbursed loan proceeds):

	December 31, 2012				Total Current	Total Loans	Total Non- Accrual
	Past Due Status			Total Past Due			
	30-59 Days	60-89 Days	> 90 Days				
One- to four-family	\$6,083	\$3,412	\$6,311	\$15,806	\$443,692	\$459,498	\$8,192
Multi-family	661	-	2,734	3,396	260,617	264,013	6,824
Commercial real estate:							
Office	-	-	719	719	75,973	76,692	1,460
Retail/wholesale/mixed	3,262	189	2,118	5,568	126,808	132,376	5,306
Industrial/warehouse	-	2,325	160	2,485	44,861	47,347	228
Other	-	-	-	-	7,360	7,360	-
Total commercial real estate	3,262	2,514	2,997	8,772	255,002	263,775	6,994
Construction and development:							
One- to four-family	-	-	-	-	10,259	10,259	-
Multi-family	563	-	-	563	26,715	27,277	-
Commercial real estate	-	-	-	-	8,046	8,046	-
Land	44	-	147	191	12,544	12,735	937
Total construction	607	-	147	754	57,564	58,317	937
Consumer:							
Home equity	851	192	1,514	2,556	221,240	223,796	1,514
Student	210	196	584	990	11,925	12,915	-
Other	49	17	59	124	10,078	10,202	59
Total consumer	1,110	405	2,157	3,670	243,243	246,913	1,573
Commercial business:							
Term loans	-	184	261	445	70,308	70,753	635
Lines of credit	191	-	58	249	61,434	61,683	58
Total commercial	191	184	319	694	131,742	132,436	693
Total	\$11,914	\$6,515	\$14,665	\$33,092	\$1,391,860	\$1,424,952	\$25,213

**Bank Mutual Corporation and Subsidiaries**

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**3. Loans Receivable (continued)**

	December 31, 2011						
	Past Due Status				Total Current	Total Loans	Total Non- Accrual
	30-59 Days	60-89 Days	> 90 Days	Total Past Due			
One- to four-family	\$10,713	\$2,491	\$12,890	26,094	\$476,437	\$502,531	\$14,868
Multi-family	7,692	–	9,949	17,640	229,179	246,819	22,905
Commercial real estate:							
Office	745	–	3,743	4,488	76,147	80,636	9,054
Retail/wholesale/mixed	695	154	7,214	8,063	91,139	99,203	11,936
Industrial/warehouse	2,230	–	1,474	3,704	31,892	35,596	1,780
Other	–	–	560	560	8,241	8,801	1,227
Total commercial real estate	3,670	154	12,991	16,815	207,419	224,236	23,997
Construction and development:							
One- to four-family	–	–	–	–	7,704	7,704	–
Multi-family	–	4,466	–	4,466	14,384	18,850	4,466
Commercial real estate	–	–	–	–	5,319	5,319	152
Land	238	1,046	3,310	4,594	11,834	16,428	4,750
Total construction	238	5,512	3,310	9,060	39,241	48,301	9,368
Consumer:							
Home equity	1,172	439	1,457	3,067	210,271	213,339	1,457
Student	396	310	696	1,403	14,309	15,711	–
Other	137	64	202	404	9,000	9,404	207
Total consumer	1,705	813	2,355	4,874	233,580	238,454	1,664
Commercial business:							
Term loans	86	169	412	668	38,930	39,598	951
Lines of credit	58	–	608	665	47,452	48,117	691
Total commercial	144	169	1,020	1,333	86,382	87,715	1,642
Total	\$24,162	\$9,139	\$42,515	\$75,816	\$1,272,238	\$1,348,056	\$74,444

As of December 31, 2012 and 2011, \$584 and \$696 in student loans, respectively, were 90-days past due, but remained on accrual status. No other loans 90-days past due were in accrual status as of either date.

The Company classifies a loan modification as a troubled debt restructuring (“TDR”) when it has granted a borrower experiencing financial difficulties a concession that it would otherwise not consider. Loan modifications that result in insignificant delays in the receipt of payments (generally six months or less) are not considered TDRs under the Company’s TDR policy. TDRs are relatively insignificant and/or infrequent in the Company and generally consist of loans placed in interest-only status for a short period of time or payment forbearance for greater than six months. There were two commercial real estate loans with balances of \$183, and eleven one-to-four family loans with balances of \$2,448 added to TDRs during the year ended December 31, 2012. There were no loans that had a payment default in the twelve months ended December 31, 2012, that were restructured during that period. TDRs are evaluated for impairment and appropriate credit losses are recorded in accordance with the Company’s accounting policies and GAAP.

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**4. Mortgage Servicing Rights**

The activity in mortgage servicing rights during the years ended December 31 is presented in the following table.

	2012	2011	2010
Mortgage servicing rights at beginning of year	\$8,269	\$7,775	\$7,186
Additions	4,852	3,241	3,866
Amortization	(3,904)	(2,747)	(3,277)
Mortgage servicing rights at end of year	9,217	8,269	7,775
Valuation allowance	(2,396)	(868)	(6)
Mortgage servicing rights at end of year	<u>\$6,821</u>	<u>\$7,401</u>	<u>\$7,769</u>

The following table shows the estimated future amortization expense for mortgage servicing rights for the years ended December 31:

2013	\$1,097
2014	1,077
2015	1,060
2016	1,038
2017	948
Thereafter	<u>1,601</u>
Total	<u>\$6,821</u>

The projection of amortization for mortgage servicing rights is based on existing asset balances and the interest rate environment as of December 31, 2012. Future amortization expense may be significantly different depending upon changes in the mortgage servicing portfolio, mortgage interest rates, loan prepayments, and market conditions.

**Bank Mutual Corporation and Subsidiaries**

**Notes to Consolidated Financial Statements**

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**5. Other Assets**

Other assets are summarized as follow:

	December 31	
	2012	2011
Accrued interest:		
Loans receivable	\$4,636	\$4,664
Mortgage-related securities	1,610	1,851
Interest-bearing deposits in banks	11	6
Total accrued interest	<u>6,257</u>	<u>6,521</u>
Bank-owned life insurance	58,609	56,604
Premises and equipment, net	50,536	50,423
Federal Home Loan Bank stock, at cost	15,841	46,092
Deferred tax asset, net	34,211	37,454
Prepaid FDIC insurance premiums	2,477	5,673
Other assets	21,764	22,059
Total other assets	<u>\$189,695</u>	<u>\$224,826</u>

Premises and equipment are summarized as follows:

	December 31	
	2012	2011
Land and land improvements	\$17,787	\$17,655
Office buildings	54,438	53,139
Furniture and equipment	18,576	18,951
Leasehold improvements	940	1,208
Total cost	<u>91,741</u>	<u>90,953</u>
Accumulated depreciation and amortization	<u>(41,205)</u>	<u>(40,530)</u>
Total premises and equipment, net	<u>\$50,536</u>	<u>\$50,423</u>

Depreciation expense for 2012, 2011, and 2010 was \$2,569, \$2,576, and \$2,600, respectively.

The Company leases various branch offices, office facilities and equipment under non-cancelable operating leases which expire on various dates through 2033. Future minimum payments under non-cancelable operating leases with initial or remaining terms of one year or more for the years indicated are as follows at December 31, 2012:

	Amount
2013	964
2014	908
2015	832
2016	703
2017	420
Thereafter	<u>2,986</u>
Total	<u>\$6,813</u>

Rent expense was \$955, \$1,002, and \$969, in 2012, 2011, and 2010, respectively.

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**6. Deposits Liabilities**

Deposit liabilities are summarized as follows:

	December 31	
	2012	2011
Checking accounts:		
Non-interest-bearing	\$143,684	\$112,211
Interest-bearing	236,380	229,990
Total checking accounts	<u>380,064</u>	<u>342,201</u>
Money market accounts	458,762	432,248
Savings accounts	<u>217,170</u>	<u>204,263</u>
Certificate of deposits:		
Due within one year	618,487	709,362
After one but within two years	159,340	250,613
After two but within three years	16,997	61,291
After three but within four years	7,994	13,301
After four but within five years	9,085	8,384
Total certificates of deposit	<u>811,903</u>	<u>\$1,042,951</u>
Total deposit liabilities	<u>\$1,867,899</u>	<u>\$2,021,663</u>

The aggregate amount of certificate accounts with balances of one hundred thousand dollars or more was \$220,923 and \$291,385 at December 31, 2012 and 2011, respectively.

Interest expense on deposits was as follows:

	Year Ended December 31		
	2012	2011	2010
Interest-bearing checking accounts	\$51	\$85	\$107
Money market accounts	716	1,696	2,075
Savings accounts	63	78	104
Certificate of deposits	13,825	17,710	26,320
Total interest expense on deposit liabilities	<u>\$14,655</u>	<u>\$19,568</u>	<u>\$28,606</u>

**Bank Mutual Corporation and Subsidiaries**

**Notes to Consolidated Financial Statements**

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**7. Borrowings**

Borrowings consist of the following:

	December 31, 2012		December 31, 2011	
	Balance	Weighted-Average Rate	Balance	Weighted-Average Rate
Federal Home Loan Bank advances maturing in:				
2012	-	-	\$100,000	4.52%
2013	\$217	4.17%	233	4.17
2014	-	-	-	-
2015	23,450	0.80	-	-
2016	23,450	1.04	-	-
2017 and thereafter	163,669	2.74	52,858	5.00
Total borrowings	<u>\$210,786</u>	2.34%	<u>\$153,091</u>	4.69%

All of the Company's FHLB advances are subject to prepayment penalties if voluntarily repaid prior to their stated maturity.

The Company is required to pledge certain unencumbered mortgage loans and mortgage-related securities as collateral against its outstanding advances from the FHLB of Chicago. Advances are also collateralized by the shares of capital stock of the FHLB of Chicago that are owned by the Company. The Company's borrowings at the FHLB of Chicago are limited to the lesser of: (i) 35% of total assets; (ii) twenty (20) times the FHLB of Chicago capital stock owned by the Company; or (iii) the total of 60% of the book value of certain multi-family mortgage loans, 75% of the book value of one- to four-family mortgage loans, and 95% of certain mortgage-related securities.

At December 31, 2012 and 2011, the Company had lines of credit with two financial institutions that totaled \$10,000 as of both dates. At December 31, 2012 and 2011, there were no amounts outstanding on these lines of credit.

**8. Shareholders' Equity**

The Bank is subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory, and possible additional discretionary, actions by regulators, that, if undertaken, could have a direct material effect on the Company's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of its assets, liabilities and certain off-balance-sheet items as calculated under regulatory accounting practices. The Bank'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 federal regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the following table) of total and Tier I capital to risk-weighted assets, and of Tier I capital to average assets (as these terms are defined in regulations). Management believes, as of December 31, 2012, that the Bank met all capital adequacy requirements. Management is not aware of any conditions or events, which would change the Bank's status as well capitalized.

**Bank Mutual Corporation and Subsidiaries**

**Notes to Consolidated Financial Statements**

**December 31, 2012**

*(Dollars in thousands, except share and per share amounts)*

**8. Shareholders' Equity (continued)**

The Bank's actual and required regulatory capital amounts and ratios as of December 31, 2012 and 2011, are presented in the following table:

	Actual		For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2012:						
Total capital (to risk-weighted assets)	\$264,012	18.02%	\$117,195	8.00%	\$146,494	10.00%
Tier 1 capital (to risk-weighted assets)	245,660	16.77	58,598	4.00	87,897	6.00
Tier 1 capital (to adjusted total assets)	245,660	10.28	95,553	4.00	119,441	5.00
As of December 31, 2011:						
Total capital (to risk-weighted assets)	\$253,815	18.34%	\$110,714	8.00%	\$138,392	10.00%
Tier 1 capital (to risk-weighted assets)	236,516	17.09	55,354	4.00	83,035	6.00
Tier 1 capital (to adjusted total assets)	236,516	9.59	98,601	4.00	123,252	5.00

The following table presents reconciliations of the Bank's equity under generally accepted accounting principles to capital as determined by regulators:

	December 31, 2012		December 31, 2011	
	Risk-Based Capital	Tier 1 (Core) Capital	Risk-Based Capital	Tier 1 (Core) Capital
Stockholder's equity according to the Bank's records	\$269,446	\$269,446	\$264,928	\$264,928
Net unrealized gain on securities available for sale, net of taxes	(6,380)	(6,380)	(4,619)	(4,619)
Additional minimum pension asset, net of taxes	11,098	11,098	9,998	9,998
Goodwill and intangibles	(395)	(395)	(594)	(594)
Investment in "non-includable" subsidiaries	(3,109)	(3,109)	(3,197)	(3,197)
Disallowed deferred tax assets	(25,000)	(25,000)	(30,000)	(30,000)
Allowance for loan losses	18,352	-	17,299	-
Regulatory capital	<u>\$264,012</u>	<u>\$245,660</u>	<u>\$253,815</u>	<u>\$236,516</u>

The following table summarizes the components of accumulated other comprehensive income (loss), net of related income tax effects, as of the dates shown:

	December 31	
	2012	2011
Net unrealized gain on securities available-for-sale	\$6,380	\$4,619
Qualified and supplemental defined benefit plans	(10,998)	(9,908)
Other post-retirement benefit plans	(99)	(90)
Accumulated other comprehensive loss	<u>\$(4,717)</u>	<u>\$(5,379)</u>

## Bank Mutual Corporation and Subsidiaries

### Notes to Consolidated Financial Statements

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#### 9. Earnings (Loss) Per Share

The computation of the Company's basic and diluted earnings (loss) per share is presented in the following table.

	Year Ended December 31		
	2012	2011	2010
Basic earnings (loss) per share:			
Net income (loss)	\$6,754	\$(47,565)	\$(72,640)
Weighted average shares outstanding	46,184,264	46,038,686	45,529,126
Allocated ESOP shares during the period	—	—	63,088
Vested MRP shares during the period	7,104	6,978	4,276
Basic shares outstanding	46,191,368	46,045,664	45,596,490
Basic earnings (loss) per share	\$0.15	\$(1.03)	\$(1.59)
Diluted earnings (loss) per share:			
Net income (loss)	\$6,754	\$(47,565)	\$(72,640)
Weighted average shares outstanding used in basic earnings (loss) per share	46,191,368	46,045,664	45,569,490
Net dilutive effect of:			
Stock option shares	8,654	—	—
Non-vested MRP shares	9,557	—	—
Diluted shares outstanding	46,209,579	46,045,664	45,569,490
Diluted earnings (loss) per share	\$0.15	\$(1.03)	\$(1.59)

The Company had stock options for 2,268,500, 2,382,500, and 1,974,000 shares outstanding at December 31, 2012, 2011, and 2010, respectively, which were not included in the computation of diluted earnings (loss) per share because they were anti-dilutive. These shares had weighted average exercise prices of \$9.37, \$9.46, and \$10.56, as of those same dates, respectively.

#### 10. Employee Benefit Plans

The Company has a discretionary, defined contribution savings plan (the "Savings Plan"). The Savings Plan is qualified under Sections 401 and 401(k) of the Internal Revenue Code and provides employees meeting certain minimum age and service requirements the ability to make contributions to the Savings Plan on a pretax basis. The Company then matches a percentage of the employee's contributions. Matching contributions made by the Company were \$198 in 2012, \$173 in 2011 and \$169 in 2010.

The Company also has a qualified defined benefit pension plan covering employees meeting certain minimum age and service requirements and a supplemental defined benefit pension plan for certain eligible employees. The supplemental pension plan is funded through a "rabbi trust" arrangement. The benefits under these plans are generally based on years of service and the employee's average annual compensation for five consecutive calendar years in the last ten calendar years which produces the highest average. The Company's funding policy is to contribute annually the amount necessary to satisfy the requirements of the Employee Retirement Income Security Act of 1974.

Effective January 1, 2013, the Company closed the qualified defined benefit pension plan to employees that were not eligible to participate in the plan as of that date, as well as any employees hired after that date. In addition, effective for service performed after March 1, 2013, the Company reduced certain benefits paid under the qualified and supplemental plans related to any employee service performed after that date.

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**10. Employee Benefit Plans (continued)**

The changes in plan assets and benefit obligations at December 31, 2012 and 2011, are presented in the following table.

	Qualified Pension Plan		Supplemental Pension Plan	
	2012	2011	2012	2011
<b>Change in plan assets:</b>				
Fair value of plan assets at beginning of year	\$47,107	\$40,658	-	-
Actual return on plan assets	5,476	2,489	-	-
Employer contributions	-	5,000	\$297	\$297
Benefits paid	(1,171)	(1,040)	(297)	(297)
Fair value of plan assets at end of year	51,412	47,107	-	-
<b>Change in benefit obligation:</b>				
Benefit obligation at beginning of year	54,144	43,404	9,102	7,959
Service cost	2,898	2,505	116	46
Interest cost	2,254	2,275	377	417
Actuarial loss	4,713	7,000	1,326	977
Benefits paid	(1,171)	(1,040)	(297)	(297)
Benefit obligation at end of year	62,838	54,144	10,624	9,102
Funded status at the end of the year	\$(11,426)	\$(7,037)	\$(10,624)	\$(9,102)

The underfunded status of the qualified and supplemental pension plans at December 31, 2012, are recognized in the statement of condition as accrued pension liability, which is included as a component of other liabilities.

The following tables summarize the changes in pension plan assets and benefit obligations recognized in accumulated other comprehensive income (loss), net of related income tax effect, for the periods indicated:

	Qualified Pension Plan		Supplemental Pension Plan	
	2012	2011	2012	2011
Balance in accumulated other comprehensive income (loss) at the beginning of year	\$(9,542)	\$(5,792)	\$(366)	\$217
Change in unrecognized loss	(302)	(3,750)	(796)	(549)
Change in prior service cost	-	-	8	(34)
Total recognized in other comprehensive loss	(302)	(3,750)	(788)	(583)
Balance in accumulated other comprehensive loss at the end of year	\$(9,844)	\$(9,542)	\$(1,154)	\$(366)

The \$1,154 in accumulated other comprehensive loss as of December 31, 2012, for the supplemental pension plan consisted of \$1,128 in unrecognized loss and \$26 in prior service costs. All other period-end balances in the table consisted of unrecognized loss.

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**10. Employee Benefit Plans (continued)**

The estimated net of tax costs that will be amortized from accumulated other comprehensive income (loss) into net periodic cost over the next fiscal year is \$1,732 for the qualified plan. The accumulated benefit obligations for the defined benefit pension plan were \$58,965 at December 31, 2012, and \$50,874 at December 31, 2011.

The assumptions used to determine the benefit obligation as of December 31 is as follows:

	2012	2011
Discount rate	3.70%	4.21%
Rate of increase in compensation levels	3.00%	3.00%
Expected long-term rate of return on plan assets (qualified plan)	6.50%	6.50%

The assumptions used to determine the net cost for the years ended December 31 is as follows:

	2012	2011	2010
Discount rate	4.21%	5.32%	5.84%
Rate of increase in compensation levels	3.00%	3.50%	3.50%
Expected long-term rate of return on plan assets (qualified plan)	6.50%	6.50%	6.50%

The expected long-term rate of return was estimated using a combination of the expected rate of return for immediate participation contracts and the historical rate of return for immediate participation contracts.

Using an actuarial measurement date of December 31, 2012, 2011, and 2010, components of net periodic benefit cost follow:

	2012	2011	2010
<b>Qualified pension plan:</b>			
Interest cost	\$2,254	\$2,275	\$2,023
Service cost	2,898	2,505	1,939
Expected return on plan assets	(3,022)	(2,601)	(2,291)
Amortization of net loss	1,759	865	-
Net periodic cost	<u>\$3,889</u>	<u>\$3,044</u>	<u>\$1,671</u>
<b>Supplemental pension plan:</b>			
Interest cost	\$377	\$417	\$426
Service cost	116	46	-
Amortization of prior service cost	13	6	-
Net periodic cost	<u>\$506</u>	<u>\$469</u>	<u>\$426</u>

At December 31, 2012, the projected benefit payments for each of the plans are as follows:

	Qualified Pension Plan	Supplemental Pension Plan	Total
2013	\$1,368	\$297	\$1,665
2014	1,898	1,139	3,037
2015	2,162	968	3,130
2016	2,419	946	3,365
2017	2,667	915	3,582
2018 – 2022	17,204	4,238	21,442
Total	<u>\$27,718</u>	<u>\$8,503</u>	<u>\$36,221</u>

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**10. Employee Benefit Plans (continued)**

The following tables summarize the fair value of the Company's qualified pension plan assets as of the dates indicated:

Asset category:	December 31, 2012			
	Amount	Fair Value Hierarchy		
		Level 1	Level 2	Level 3
Money market fund	\$325	–	\$325	–
Equity security	808	\$808	–	–
Immediate participation guarantee contract	50,279	–	–	\$50,279
<b>Total</b>	<b>\$51,412</b>	<b>\$808</b>	<b>\$325</b>	<b>\$50,279</b>

Asset category:	December 31, 2011			
	Amount	Fair Value Hierarchy		
		Level 1	Level 2	Level 3
Money market fund	\$293	–	\$293	–
Equity security	632	\$632	–	–
Immediate participation guarantee contract	46,182	–	–	\$46,182
<b>Total</b>	<b>\$47,107</b>	<b>\$632</b>	<b>\$293</b>	<b>\$46,182</b>

The investment objective is to minimize risk. The assets of the qualified pension plan are concentrated in a group annuity contract issued by a life insurance company. Pension plan contributions are maintained in the general account of the insurance company, which invests primarily in corporate and government notes and bonds with ten to fifteen years to maturity. The group annuity contract is valued at fair value by discounting the related cash flows based on current yields of similar instruments with comparable durations and considering the credit worthiness of the issuer.

The equity securities are shares of stock issued by the life insurance company when it demutualized. This investment is valued at the closing price reported in the active market in which the security is traded. The money market fund, which invests in short-term U.S. government securities, is based on a \$1 net asset value ("NAV") specified by the fund manager. The fund is not traded in an active market. The fund manager bases its estimate of the NAV on quoted prices for similar assets in active markets.

The following table presents a summary of the changes in the fair value of the pension plan's Level 3 asset during the periods indicated. As noted above, the Company's Level 3 asset consists entirely of a group annuity contract issued by an insurance company.

	2012	2011
Fair value at the beginning of the period	\$46,182	\$39,374
Actual return on plan assets	5,268	2,848
Employer contribution	–	5,000
Benefits paid	(1,171)	(1,040)
<b>Fair value at the end of the period</b>	<b>\$50,279</b>	<b>\$46,182</b>

The Company has a deferred retirement plan for certain non-officer directors who have provided at least five years of service. All eligible directors' benefits have vested. In the event a director dies prior to completion of these payments, payments will go to the director's heirs. The Company has funded these arrangements through "rabbi trust" arrangements and, based on actuarial analyses, believes these obligations are adequately funded. The

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**10. Employee Benefit Plans (continued)**

Company also has supplemental retirement plans for certain executives of a financial institution it acquired in 2000. The liabilities related to these plans were \$3,453 and \$3,362 at December 31, 2012 and 2011 respectively. The net expense related to these plans for the years ended December 31, 2012, 2011, and 2010 was \$189, \$194, and \$221, respectively.

**11. Stock-Based Benefit Plans**

In 2004 the Company's shareholders approved the 2004 Stock Incentive Plan (the "2004 Plan"), which provides for stock option awards of up to 4,106,362 shares. Options granted under the 2004 Plan vest over five years and have expiration terms of ten years. The 2004 Plan also provides for MRP awards of up to 1,642,521 shares. MRP shares awarded under the 2004 Plan vest over five years. As of December 31, 2012, options for 621,362 shares and 520,221 MRP shares remain eligible for award under the 2004 Plan.

MRP grants are amortized to compensation expense as the Company's employees and directors become vested in the granted shares. The amount amortized to expense was \$186 for 2012, \$120 for 2011, and \$91 for 2010. Outstanding non-vested MRP grants had a fair value of \$436 and an unamortized cost of \$417 at December 31, 2012. The cost of these shares is expected to be recognized over a weighted-average period of 1.7 years.

The Company recorded stock option compensation expenses of \$232, \$161, and \$46, for 2012, 2011, and 2010 respectively. As of December 31, 2012, there was \$676 in total unrecognized stock option compensation expense related to non-vested options. This cost is expected to be recognized over a weighted-average period of 1.7 years.

The following schedule reflects activity in the Company's vested and non-vested stock options and related weighted average exercise prices for the periods indicated.

	Year Ended December 31					
	2012		2011		2010	
	Stock Options	Weighted Average Exercise	Stock Options	Weighted Average Exercise	Stock Options	Weighted Average Exercise
Outstanding at beginning of year	2,382,500	\$9.4637	2,462,464	\$9.0184	3,129,398	\$8.1823
Granted	412,500	3.3999	438,500	4.9730	120,000	5.7733
Exercised	-	-	(488,464)	3.2056	(576,934)	3.2056
Forfeited	(124,000)	10.6730	(30,000)	9.1735	(210,000)	10.673
Outstanding at end of year	<u>2,671,000</u>	<u>\$8.4711</u>	<u>2,382,500</u>	<u>\$9.4637</u>	<u>2,462,464</u>	<u>\$9.0184</u>

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**11. Stock-Based Benefit Plans (continued)**

The following table provides additional information regarding the Company's outstanding options as of December 31, 2012.

	Remaining Contractual Life	Non-Vested Options		Vested Options	
		Stock Options	Intrinsic Value	Stock Options	Intrinsic Value
Exercise price:					
\$10.6730	1.3	-	-	1,576,000	-
\$12.2340	3.5	-	-	50,000	-
\$11.1600	5.3	6,400	-	25,600	-
\$12.0250	5.6	10,000	-	40,000	-
\$7.2260	7.3	30,000	-	20,000	-
\$4.7400	8.0	42,000	-	28,000	-
\$5.0500	8.0	310,400	-	77,600	-
\$4.3000	8.2	20,000	-	5,000	-
\$3.7200	8.6	14,000	\$8	3,500	\$2
\$3.3900	9.0	402,500	366	-	-
\$3.8000	9.3	10,000	5	-	-
Total		<u>845,300</u>	<u>\$379</u>	<u>1,825,700</u>	<u>\$2</u>
Weighted average remaining contractual life		<u>8.4 years</u>		<u>2.0 years</u>	
Weighted average exercise price		<u>\$4.3954</u>		<u>\$10.3536</u>	

The total intrinsic value of options exercised was \$296 and \$1,844 during 2011 and 2010, respectively. There were no options exercised in 2012. The weighted average grant date fair value of non-vested options at December 31, 2012, was \$1.06 per share. In 2012 no non-vested options were forfeited, 412,500 options were granted, and 126,500 options vested.

The Company uses the Black-Scholes option-pricing model to estimate the fair value of granted options. This model was developed for use in estimating the fair value of traded options that have no vesting restrictions and are fully transferable. However, the Company's stock options have characteristics significantly different from traded options and changes in the subjective input assumptions can materially affect the fair value estimate. Option valuation models such as Black-Scholes require the input of highly subjective assumptions including the expected stock price volatility, which is computed using five-years of actual price activity in the Company's stock. The Company uses historical data of employee behavior as a basis to estimate the expected life of the options, as well as forfeitures due to employee terminations. The Company also uses its actual dividend yield at the time of the grant, as well as actual U.S. Treasury yields in effect at the time of the grant to estimate the risk-free rate. The following weighted-average assumptions were used to value 412,500 options granted during 2012: risk free interest rate of 1.50%, dividend yield of 1.18%, expected stock volatility of 25%, and expected term to exercise of 7.5 years. The following weighted-average assumptions were used to value 438,500 options granted during 2011: risk free interest rate of 2.06%, dividend yield of 2.00%, expected stock volatility of 25%, and expected term to exercise of 7.5 years. The following weighted-average assumptions were used to value 120,000 options granted during 2010: risk free interest rate of 2.42%, dividend yield of 2.44%, expected stock volatility of 25.0%, and expected term to exercise of 7.5 years.

The Company maintains an ESOP for employees that had attained at least 21 years of age and completed one year of service as of December 31, 2010. The ESOP is a qualifying plan under Internal Revenue Service guidelines. In 2000 and 2001, the ESOP borrowed a total of \$8,999 and purchased 3,271,946 of the Company's common shares on various dates in 2000, 2001, and 2002. ESOP expense was recognized based on the fair value (average stock price) of shares scheduled to be released from the ESOP trust. Beginning in 2001, one-tenth of the shares were scheduled to be released each year. Also, additional shares could have been released as the ESOP trust received cash dividends

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**11. Stock-Based Benefit Plans (continued)**

from the unallocated shares held in the trust. As of December 31, 2011, no shares remained to be allocated in the ESOP. ESOP expense was zero for both of the years ended December 31, 2012 and 2011, and was \$782 for the year ended December 31, 2010.

The Company has no stock compensation plans that have not been approved by shareholders.

**12. Income Taxes**

The Company and its subsidiaries file income tax returns in the U.S. federal jurisdiction and Wisconsin and Minnesota. The Company is no longer subject to U.S. federal and Minnesota income tax examinations by tax authorities for years prior to 2007 and, for Wisconsin, years prior to 1997. If any interest and/or penalties would be imposed by an appropriate taxing authority, the Company would report the interest component through other non-interest expense and penalties through income tax expense. The Company had no material uncertain tax positions and had not recorded a liability for unrecognized tax benefits as of or during the three years ended December 31, 2012.

The provision for income taxes consists of the following:

	Year Ended December 31		
	2012	2011	2010
Current income tax expense (benefit):			
Federal	\$47	\$45	\$(17,924)
State	3	(123)	90
Current income tax expense (benefit)	50	(78)	(17,834)
Deferred income tax expense (benefit):			
Federal	2,629	1,475	(22,388)
State	657	355	(9,687)
Deferred income tax expense (benefit)	3,286	1,830	(32,075)
Income tax expense (benefit)	\$3,336	\$1,752	\$(49,909)

Income tax expense (benefit) differs from the provision computed at the federal statutory corporate rate as follows:

	Year Ended December 31		
	2012	2011	2010
Income (loss) before income taxes	\$10,038	\$(45,863)	\$(122,548)
Tax expense (benefit) at federal statutory rate	\$3,531	\$(16,035)	\$(42,892)
Increase (decrease) in taxes resulting from:			
State income taxes, net of federal tax benefit	429	239	(6,269)
Bank-owned life insurance	(741)	(831)	(842)
Goodwill impairment	-	18,399	-
Reversal of valuation allowance, net of federal benefit	-	(135)	-
Other	117	115	94
Income tax expense (benefit)	\$3,336	\$1,752	\$(49,909)

**Bank Mutual Corporation and Subsidiaries**

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**12. Income Taxes (continued)**

Deferred 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. The significant components of the Company's deferred tax assets and liabilities are summarized as follows:

	December 31	
	2012	2011
Deferred tax assets:		
Federal net operating losses and AMT credits	\$18,441	\$18,914
Pension	9,400	10,588
Loan loss reserves	8,662	11,211
State net operating losses	6,172	6,229
Non-deductible losses on foreclosed real estate	2,836	3,365
Deferred compensation	1,558	1,460
Other-than-temporary impairment of investment securities	258	156
Restricted stock amortization	205	154
Other	1,371	1,013
Total deferred tax assets	48,903	53,090
Deferred tax liabilities:		
Unrealized gain on investment securities	4,273	3,094
Purchase accounting adjustments	2,967	3,125
Mortgage servicing rights	2,737	2,970
FHLB stock dividends	2,592	5,130
Property and equipment depreciation	1,776	1,095
Other	347	222
Total deferred tax liabilities	14,692	15,636
Net deferred tax asset	\$34,211	\$37,454

As of December 31, 2012, the Company had \$49,623 and \$118,701 in net operating loss carryovers for federal and state income tax purposes, respectively, and \$1,073 in AMT credit carryovers available to offset against future income. The net operating loss carryovers expire in various years through 2031 if unused. The AMT credit carryovers have no expiration date.

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## Notes to Consolidated Financial Statements

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### 13. Financial Instruments with Off-Balance-Sheet Risk

The Company is party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments consist of commitments to extend credit and involve, to varying degrees, elements of credit and interest rate risk in excess of the amounts recognized in the consolidated statements of financial condition. The contract amounts reflect the extent of involvement the Company has in particular classes of financial instruments and also represents the Company's maximum exposure to credit loss.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and generally require payment of a fee. As some commitments expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Company evaluates the collateral needed and creditworthiness of each customer on a case by case basis. The Company generally extends credit only on a secured basis. Collateral obtained varies, but consists principally of one- to four-family residences.

Off-balance sheet financial instruments or obligations whose contract amounts represent credit risk and/or interest rate risk are summarized in the following table as of the dates indicated:

	December 31	
	2012	2011
Unused consumer lines of credit	\$152,109	\$151,807
Unused commercial lines of credit	75,354	43,518
Commitments to extend credit:		
Fixed rate	15,054	23,793
Adjustable rate	20,894	17,197
Undisbursed commercial loans	3,000	870
Standby letters of credit	1,512	410

The Company sells substantially all of its long-term, fixed-rate, one- to four-family loan originations in the secondary market. The Company uses derivative instruments to manage interest rate risk associated with these activities. Specifically, the Company enters into interest rate lock commitments ("IRLCs") with borrowers, which are considered to be derivative instruments. The Company manages its exposure to interest rate risk in IRLCs (as well as interest rate risk in its loans held-for-sale) by entering into forward commitments to sell loans to the Fannie Mae. Commitments to sell loans expose the Company to interest rate risk if market rates of interest decrease during the commitment period. Such forward commitments are considered to be derivative instruments. These derivatives are not designated as accounting hedges as specified in GAAP. As such, changes in the fair value of the derivative instruments are recognized currently through earnings.

As of December 31, 2012 and 2011, net unrealized gains of \$1,215 and \$243, respectively, were recognized in net gain on loan sales activities on the derivative instruments specified in the previous paragraph. These amounts were exclusive of net unrealized gains of \$277 and \$507 on loans held-for-sale as of those dates, respectively, which were also included in net gain on loan sales activities.

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**13. Financial Instruments with Off-Balance-Sheet Risk (continued)**

The following table summarizes the Company's derivative assets and liabilities as of the dates indicated.

	December 31, 2012		December 31, 2011	
	Notional Amount	Fair Value	Notional Amount	Fair Value
Interest rate lock commitments	\$83,882	\$1,414	\$52,699	\$1,012
Forward commitments	75,750	(199)	62,025	(769)
Net unrealized gains		<u>\$1,215</u>		<u>\$243</u>

The unrealized gains shown in the above table were included as a component of other assets as of the dates indicated. The unrealized losses were included in other liabilities as of the dates indicated.

**14. Fair Value Measurements**

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (exit price). The Company utilizes market data or assumptions that market participants would use in pricing the asset or liability, including assumptions about risk and the risks inherent in the inputs to the valuation technique. These inputs can be readily observable, market corroborated, or generally unobservable. The Company primarily applies the market approach for recurring value measurements and endeavors to utilize the best available information. Accordingly, the Company utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs. The Company is able to classify fair value balances based on the observability of those inputs. Accounting guidance establishes a fair value hierarchy that prioritizes the inputs used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1), the next highest priority is given to prices based on models, methodologies, and/or management judgments that rely on direct or indirect observable inputs (Level 2), and the lowest priority to prices derived from models, methodologies, and/or management judgments that rely on significant unobservable inputs (Level 3). There were no transfers of assets or liabilities between categories of the fair value hierarchy during the years ended December 31, 2012 and 2011.

The following methods and assumptions are used by the Company in estimating its fair value disclosures of financial instruments:

**Cash and Cash Equivalents** The carrying amounts reported in the statements of financial condition for cash and cash equivalents approximate those assets' fair values. The Company considers the fair value of cash and cash equivalents to be Level 1 in the fair value hierarchy.

**Mortgage-Related Securities Available-for-Sale and Held-to-Maturity** Fair values for these securities are based on price estimates obtained from a third-party independent pricing service. This service utilizes pricing models that vary by asset class and incorporate available trade, bid, ask and other market information of comparable instruments. For structured securities, such as CMOs, the pricing models include cash flow estimates that consider the impact of loan performance data, including, but not limited to, expectations relating to loan prepayments, default rates, and loss severities. Management has reviewed the pricing methodology used by its pricing service to verify that prices are determined in accordance with the fair value guidance specified in GAAP. The Company considers the fair value of mortgage-related securities to be Level 2 in the fair value hierarchy.

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**14. Fair Value Measurements (continued)**

**Loans Held-for-Sale** The fair value of loans held-for-sale is based on the current market price for securities collateralized by similar loans. The Company considers the fair value of loans held-for-sale to be Level 2 in the fair value hierarchy.

**Loans Receivable** Loans receivable are segregated by type such as one- to four-family, multi-family, and commercial real estate mortgage loans, consumer loans, and commercial business loans. The fair value of each type is calculated by discounting scheduled cash flows through the expected maturity of the loans using estimated market discount rates that reflect the credit and interest rate risk inherent in the loan type. The estimated maturity is based on the Company's historical experience with prepayments for each loan classification, modified, as required, by an estimate of the effect of current economic and lending conditions. The Company considers the fair value of loans receivable to be Level 3 in the fair value hierarchy.

**Mortgage Servicing Rights** The Company has calculated the fair market value of mortgage servicing rights for those loans that are sold with servicing rights retained. For valuation purposes, loans are stratified by product type and, within product type, by interest rates. The fair value of mortgage servicing rights is based upon the present value of estimated future cash flows using current market assumptions for prepayments, servicing cost and other factors. The Company considers the fair value of mortgage servicing rights to be Level 3 in the fair value hierarchy.

The following table summarizes the significant inputs utilized by the Company to estimate the fair value of its MSR as of December 31, 2012:

	Weighted- Average	Range
Loan size	\$126	\$2 - \$415
Contractual interest rate	4.02%	2.00% - 7.75%
Constant prepayment rate ("CPR")	22.32%	15.78% - 29.22%
Remaining maturity in months	259	39 - 417
Servicing fee	0.25%	—
Annual servicing cost per loan (not in thousands)	\$82.66	—
Annual ancillary income per loan (not in thousands)	\$54.81	—
Discount rate	3.07%	2.63% - 3.38%

MSR pools with an amortized cost basis greater than fair value are carried at fair value in the Company's financial statements. Pools determined to be impaired at December 31, 2012, had an amortized cost basis of \$8,523 and a fair value of \$6,127 as of that date. Accordingly, the Company recorded a valuation allowance of \$2,396 as of December 31, 2012, as well as a corresponding loss of \$1,528 during the twelve month period then ended, which was equal to the change in the valuation allowance during that period. Pools determined to be impaired at December 31, 2011, had an amortized cost basis of \$6,812 and a fair value of \$5,944 as of that date. Accordingly, the Company recorded a valuation allowance of \$868 as of December 31, 2011, as well as a corresponding loss of \$862 during the twelve month period then ended, which was equal to the change in the valuation allowance during that period.

**Federal Home Loan Bank Stock** FHLB of Chicago stock is carried at cost, which is its redeemable (fair) value, since the market for this stock is restricted. The Company considers the fair value of FHLB of Chicago stock to be Level 2 in the fair value hierarchy.

**Accrued Interest Receivable and Payable** The carrying values of accrued interest receivable and payable approximate their fair value. The Company considers the accrued interest receivable and payable to be Level 2 in the fair value hierarchy.

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**14. Fair Value Measurements(continued)**

***Deposit Liabilities and Advance Payments by Borrowers for Taxes and Insurance*** Fair value for demand deposits equal book value. The Company considers the fair value of demand deposits to be Level 2 in the fair value hierarchy. Fair values for certificate of deposits are estimated using a discounted cash flow calculation that applies current market borrowing interest rates to a schedule of aggregated expected monthly maturities on deposits. The Company considers the fair value of certificates of deposit to be Level 3 in the fair value hierarchy. The advance payments by borrowers for taxes and insurance are equal to their carrying amounts at the reporting date. The Company considers the fair value of advance payments by borrowers to be Level 2 in the fair value hierarchy.

***Borrowings*** The fair value of long-term borrowings is estimated using discounted cash flow calculations with the discount rates equal to interest rates currently being offered for borrowings with similar terms and maturities. The carrying value on short-term borrowings approximates fair value. The Company considers the fair value of borrowings to be Level 2 in the fair value hierarchy.

***Off-Balance Sheet Financial Instruments*** Off-balance sheet financial instruments consist of commitments to extend credit, IRLCs, and forward commitments to sell loans. Commitments to extend credit that are not IRLCs generally carry variable rates of interest. As such, the fair value of these instruments is not material. The Company considers the fair value of these instruments to be Level 2 in the fair value hierarchy. The carrying value of IRLCs and forward commitments to sell loans, which is equal to their fair value, is the difference between the current market prices for securities collateralized by similar loans and the notional amounts of the IRLCs and forward commitments. The Company considers the fair value of IRLCs and forward commitments to sell loans to be Level 2 in the fair value hierarchy.

The carrying values and fair values of the Company's financial instruments are presented in the following table as of the indicated dates.

	December 31, 2012		December 31, 2011	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Cash and cash equivalents	\$87,059	\$87,059	\$120,935	\$120,935
Mortgage related securities available-for-sale	550,185	550,185	781,770	781,770
Mortgage related securities held-to-maturity	157,558	163,589	—	—
Loans held-for-sale	10,739	10,739	19,192	19,192
Loans receivable, net	1,402,246	1,400,415	1,319,636	1,284,651
Mortgage servicing rights, net	6,821	7,032	7,401	7,577
Federal Home Loan Bank stock	15,841	15,841	46,092	46,092
Accrued interest receivable	6,257	6,257	6,521	6,521
Deposit liabilities	1,867,899	1,807,016	2,021,663	1,968,842
Borrowings	210,786	227,957	153,091	167,418
Advance payments by borrowers	4,956	4,956	3,192	3,192
Accrued interest payable	476	476	750	750
Unrealized gain (loss) on off-balance-sheet items:				
Interest rate lock commitments on loans	1,414	1,414	1,012	1,012
Forward commitments to sell loans	(199)	(199)	(769)	(769)

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**14. Fair Value Measurements (continued)**

The following table segregates by fair value hierarchy (i.e., Level 1, 2, or 3) all of the Company's assets and liabilities as of December 31, 2011 and 2010, that are measured at fair value on a recurring basis.

	December 31, 2012			Total
	Level 1	Level 2	Level 3	
Loans held-for-sale	–	\$10,739	–	\$10,739
Mortgage-related securities available-for-sale	–	550,185	–	550,185
<b>Total</b>	–	\$560,924	–	\$560,924

	December 31, 2011			Total
	Level 1	Level 2	Level 3	
Loans held-for-sale	–	\$19,192	–	\$19,192
Mortgage-related securities available-for-sale	–	781,770	–	781,770
<b>Total</b>	–	\$800,962	–	\$800,962

**Impaired Loans** For non-accrual loans greater than an established threshold and individually evaluated for impairment and all renegotiated loans, impairment is measured based on: (i) the fair value of the loan or the fair value of the collateral less estimated selling costs (collectively the “collateral value method”) or (ii) the present value of the estimated cash flows discounted at the loan’s original effective interest rate (the “discounted cash flow method”). The resulting valuation allowance, if any, is a component of the allowance for loan losses. The discounted cash flow method is a fair value measure. For the collateral value method, the Company generally obtains appraisals on a periodic basis to support the fair value of collateral underlying the loans. Appraisals are performed by independent certified and/or licensed appraisers that have been reviewed by the Company and incorporate information such as recent sales prices for comparable properties, costs of construction, and net operating income of the property or business. Selling costs are generally estimated at 10%. Appraised values may be further discounted based on management judgment regarding changes in market conditions and other factors since the time of the appraisal. A significant unobservable input in using net operating income to estimate fair value is the capitalization rate. At December 31, 2012, the range of capitalization rates utilized to determine the fair value of the underlying collateral on certain loans was 6% to 12%. The Company considers these fair values to be Level 3 in the fair value hierarchy. For those loans individually evaluated for impairment using the collateral value method, a valuation allowance of \$2,041 was recorded for loans with a recorded investment of \$57,638 at December 31, 2012. These amounts were \$8,305 and \$103,627 at December 31, 2011, respectively. Provision for loan losses related to these loans was \$428 and \$1,257 in 2012 and 2011, respectively.

**Foreclosed Properties** Foreclosed properties acquired through, or in lieu of, loan foreclosure are recorded at the lower of cost or fair value less estimated costs to sell. In determining fair value, the Company generally obtains appraisals to support the fair value of foreclosed properties, as described in the previous paragraph. In certain instances, the Company may also use the selling list price, less estimated costs to sell, as the fair value of foreclosed properties. In such instances, the list price is generally less than the appraised value. The Company considers these fair values to be Level 3 in the fair value hierarchy. As of December 31, 2012, \$12,170 in foreclosed properties were valued at collateral value compared to \$22,655 at December 31, 2011. Losses of \$2,497 and \$4,639 related to these foreclosed properties valued at collateral value were recorded during the twelve months ended December 31, 2012 and 2011, respectively.

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**15. Condensed Parent Company Only Financial Statements**

**STATEMENT OF FINANCIAL CONDITION**

	December 31	
	2012	2011
Assets		
Cash and cash equivalents	\$3,284	\$2,067
Investment in subsidiary	266,513	262,002
Other assets	2,056	1,807
	<hr/>	<hr/>
Total assets	\$271,853	\$265,876
	<hr/>	<hr/>
Liabilities and shareholders' equity		
Other liabilities	-	\$105
Shareholders' equity:		
Common stock—\$0.01 par value:		
Authorized—200,000,000 shares in 2012 and 2011		
Issued—78,783,849 shares in 2012 and 2011		
Outstanding—46,326,484 in 2012 and 46,228,984 shares in 2011	\$788	788
Additional paid-in capital	489,960	490,159
Retained earnings	145,231	140,793
Accumulated other comprehensive income (loss)	(4,717)	(5,379)
Treasury stock—32,457,365 shares in 2012 and 32,554,865 shares in 2011	(359,409)	(360,590)
Total shareholders' equity	<hr/>	<hr/>
	271,853	265,771
	<hr/>	<hr/>
Total liabilities and shareholders' equity	\$271,853	\$265,876
	<hr/>	<hr/>

**STATEMENT OF INCOME**

	Year Ended December 31		
	2012	2011	2010
Total income	\$3	\$17	\$43
Total expenses	796	863	846
Loss before income taxes	(793)	(846)	(803)
Income tax benefit	(306)	(464)	(313)
Loss before equity in earnings of subsidiary	(487)	(382)	(490)
Equity in earnings (loss) of subsidiary	<hr/>	<hr/>	<hr/>
	7,241	(47,183)	(72,150)
	<hr/>	<hr/>	<hr/>
Net income (loss)	\$6,754	\$(47,565)	\$(72,640)
	<hr/>	<hr/>	<hr/>

**Bank Mutual Corporation and Subsidiaries**

**Notes to Consolidated Financial Statements**

**December 31, 2012**

*(Dollars in thousands, except share and per share amounts)*

**15. Condensed Parent Company Only Financial Statements (continued)**

**STATEMENT OF TOTAL COMPREHENSIVE INCOME**

	Year Ended December 31		
	2012	2011	2010
Net income (loss)	\$6,754	\$(47,565)	\$(72,640)
Other comprehensive income (loss), net of income taxes:			
Unrealized holding gains (losses) during the period:			
Non-credit portion of OTTI on securities available-for sale, net of deferred income taxes of \$(196) in 2012 and \$(563) in 2011	(293)	(842)	-
Change in net unrealized gain on securities available-for-sale, net of deferred income taxes of \$1,593 in 2012, \$5,028 in 2011, and \$6,259 in 2010	2,378	7,511	9,347
Reclassification adjustment for gain on securities included in income, net of income taxes of \$(218) in 2012, \$(446) in 2011, and \$(6,403) in 2010	(325)	(667)	(9,563)
	<u>1,760</u>	<u>6,002</u>	<u>(216)</u>
Defined benefit pension plans:			
Pension asset, net of deferred income taxes of \$(732) in 2012, \$(2,990) in 2011, and \$(2,850) in 2010	(1,098)	(4,484)	(4,275)
	<u>(1,098)</u>	<u>(4,484)</u>	<u>(4,275)</u>
Total other comprehensive income, net of income taxes	662	1,518	(4,491)
Total comprehensive income (loss)	<u>\$7,416</u>	<u>\$(46,047)</u>	<u>\$(77,131)</u>

**STATEMENT OF CASH FLOWS**

	Year Ended December 31		
	2012	2011	2010
Operating activities:			
Net income (loss)	\$6,754	\$(47,565)	\$(72,640)
Adjustment to reconcile net income (loss) to net cash provided by operating activities:			
Equity in loss (earnings) of Bank subsidiary	(7,241)	47,183	72,150
Stock-based compensation	88	67	39
Change in other operating activities	(353)	(1,577)	1,547
Net cash provided (used) by operating activities	<u>(752)</u>	<u>(1,892)</u>	<u>1,096</u>
Investing activities:			
Dividends from Bank subsidiary	4,130	730	7,450
Other investing activities	(409)	170	78
Net cash provided by investing activities	<u>3,721</u>	<u>900</u>	<u>7,528</u>
Financing activities:			
Cash dividends	(2,316)	(2,880)	(8,640)
Purchase of treasury stock	-	-	(5,029)
Proceeds from exercise of stock options	-	1,416	359
Excess tax benefit from exercise of stock options	564	49	26
Payments received on ESOP	-	-	347
Net cash used in financing activities	<u>(1,752)</u>	<u>(1,415)</u>	<u>(12,937)</u>
Decrease in cash and cash equivalents	1,217	(2,407)	(4,313)
Cash and cash equivalents at beginning of year	<u>2,067</u>	<u>4,474</u>	<u>8,787</u>
Cash and cash equivalents at end of year	<u>\$3,284</u>	<u>\$2,067</u>	<u>\$4,474</u>

## **Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure**

Not applicable.

### **Item 9A. Controls and Procedures**

#### **Disclosure Controls and Procedures**

The management of the Company, including its Chief Executive Officer and Chief Financial Officer, has conducted an evaluation of the effectiveness of the Company's disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")) as of the end of the period covered by this report. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded as of December 31, 2012, that the disclosure controls and procedures were effective.

#### **Change in Internal Control Over Financial Reporting**

There have not been any changes in the Company's internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the final fiscal quarter of the year to which this report relates that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

#### **Management's Report on Internal Control Over Financial Reporting**

The 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 GAAP. The 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 GAAP, and that receipts and expenditures of the Company are being made only in accordance with authorization 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.

Management of the Company is responsible for establishing and maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. The Company's management, including its Chief Executive Officer and Chief Financial Officer, has assessed the effectiveness of its internal control over financial reporting as of December 31, 2012, based on the criteria established in "Internal Control—Integrated Framework" issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO"). Based upon its assessment and those criteria, management believes that as of December 31, 2012, the Company's internal control over financial reporting was effective.

Deloitte & Touche LLP, the Company's independent registered public accounting firm, has audited the consolidated financial statements included in this Annual Report on Form 10-K and, as a part of its audit, has audited the effectiveness of the Company's internal control over financial reporting. That report can be found on the following page as part of this Item 9A.

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders of  
Bank Mutual Corporation  
Milwaukee, Wisconsin

We have audited the internal control over financial reporting of Bank Mutual Corporation and subsidiaries (the "Company") as of December 31, 2012, based on criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. 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, included in the accompanying Management's Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on 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, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, 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 by, or under the supervision of, the company's principal executive and principal financial officers, or persons performing similar functions, and effected by the company's board of directors, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with 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 the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2012, based on the criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial statements as of and for the year ended December 31, 2012 of the Company and our report dated March 8, 2013 expressed an unqualified opinion on those financial statements.

/s/ Deloitte & Touche LLP

Milwaukee, Wisconsin  
March 8, 2013

**Item 9B. Other Information**

Not applicable.

### Part III

#### **Item 10. Directors, Executive Officers, and Corporate Governance**

Information in response to this item is incorporated herein by reference to “Election of Directors”, “Section 16(a) Beneficial Ownership Reporting Compliance”, and “Executive Officers” in the Company’s definitive Proxy Statement for its Annual Meeting of Shareholders on May 6, 2013 (the “2013 Annual Meeting Proxy Statement”).

#### **Item 11. Executive Compensation**

Information in response to this item is incorporated by reference to “Election of Directors—Board Meetings and Committees—Compensation Committee Interlocks and Insider Participation,” “Directors’ Compensation,” “Compensation Discussion and Analysis,” “Compensation Committee Report on Executive Compensation,” “Executive Compensation,” and “Risk Management and Compensation” in the 2013 Annual Meeting Proxy Statement.

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

Information in response to this item is incorporated by reference to “Security Ownership of Certain Beneficial Owners” in the 2013 Annual Meeting Proxy Statement.

The following chart gives aggregate information regarding grants under all equity compensation plans of the Company through December 31, 2012.

<u>Plan category</u>	<u>Number of securities to be issued upon exercise of outstanding options, warrants and rights</u>	<u>Weighted-average exercise price of outstanding options, warrants and rights</u>	<u>Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in 1st column)</u>
Equity compensation plans approved by security holders (1)	2,671,000	\$8.4711	1,141,583
Equity compensation plans not approved by security holders	None	None	None

(1) All amounts in these columns relate to the 2004 Plan, which was approved by the shareholders in 2004.

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

Information in response to this item is incorporated by reference to “Election of Directors—Board Meetings and Committees” and “Certain Transactions and Relationships with the Company” in the 2013 Annual Meeting Proxy Statement.

#### **Item 14. Principal Accountant Fees and Services**

Information in response to this item is incorporated by reference to “Independent Registered Public Accounting Firm” in the 2013 Annual Meeting Proxy Statement.

## Part IV

### **Item 15. Exhibits, Financial Statement Schedules**

(a) Documents filed as part of the Report:

1. and 2. Financial Statements and Financial Statement Schedules.

The following consolidated financial statements of the Company and subsidiaries are filed as part of this report under “Item 8. Financial Statements and Supplementary Data”:

- Report of Deloitte & Touche LLP, Independent Registered Public Accounting Firm, on the consolidated financial statements.
- Consolidated Statements of Financial Condition—As of December 31, 2012 and 2011.
- Consolidated Statements of Income—Years Ended December 31, 2012, 2011, and 2010.
- Consolidated Statements of Total Comprehensive Income—Years Ended December 31, 2012, 2011, and 2010
- Consolidated Statements of Equity—Years Ended December 31, 2012, 2011, and 2010.
- Consolidated Statements of Cash Flows—Years Ended December 31, 2012, 2011, and 2010.
- Notes to Consolidated Financial Statements.

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 inapplicable, and therefore have been omitted.

(b) Exhibits. Refer to the Exhibit Index following the signature page of this report, which is incorporated herein by reference. Each management contract or compensatory plan or arrangement required to be filed as an exhibit to this report is identified in the Exhibit Index by an asterisk following its exhibit number.

## SIGNATURES

Pursuant to the requirements of Section 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.

March 8, 2013

BANK MUTUAL CORPORATION

By: /s/ Michael T. Crowley, Jr.  
Michael T. Crowley, Jr.  
Chairman and Chief Executive Officer

## POWER OF ATTORNEY

Each person whose signature appears below hereby authorizes Michael T. Crowley, Jr., Michael W. Dosland, Richard L. Schroeder or any of them, as attorneys-in-fact with full power of substitution, to execute in the name and on behalf of such person, individually, and in each capacity stated below or otherwise, and to file, any and all amendments to this report.

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.\*

### Signature and Title

/s/ Michael T. Crowley, Jr.  
Michael T. Crowley, Jr., Chairman,  
Chief Executive Officer, and Director  
(Principal Executive Officer)

/s/ Thomas H. Buestrin  
Thomas H. Buestrin, Director

/s/ David A. Baumgarten  
David A. Baumgarten, President and Director

/s/ Mark C. Herr  
Mark C. Herr, Director

/s/ Michael W. Dosland  
Michael W. Dosland, Senior Vice President and  
Chief Financial Officer (Principal Financial Officer)

/s/ Thomas J. Lopina, Sr.  
Thomas J. Lopina, Sr., Director

/s/ Richard L. Schroeder  
Richard L. Schroeder, Vice President and  
Controller (Principal Accounting Officer)

/s/ William J. Mielke  
William J. Mielke, Director

/s/ David C. Boerke  
David C. Boerke, Director

/s/ Robert B. Olson  
Robert B. Olson, Director

/s/ Richard A. Brown  
Richard A. Brown, Director

/s/ Jelmer G. Swoboda  
Jelmer G. Swoboda, Director

\* Each of the above signatures is affixed as of March 8, 2013.

**BANK MUTUAL CORPORATION**  
**(“Bank Mutual Corporation” or the “Company”)**  
**Commission File No. 000-32107**

**EXHIBIT INDEX**  
**TO**  
**2012 REPORT ON FORM 10-K**

The following exhibits are filed with, or incorporated by reference in, this Report on Form 10-K for the year ended December 31, 2012:

<u>Exhibit</u>	<u>Description</u>	<u>Incorporated Herein by Reference To</u>	<u>Filed Herewith</u>
3(i)	Restated Articles of Incorporation, as last amended May 29, 2003, of Bank Mutual Corporation (the “Articles”)	Exhibit 3(i) to the Company's Registration Statement on Form S-1, Registration No. 333-105685	
3(ii)	Bylaws, as last amended May 7, 2007, of Bank Mutual Corporation	Exhibit 3.1 to the Company's Report on Form 8-K dated May 7, 2007	
4.1	The Articles	Exhibit 3(i) above	
10.1*	Bank Mutual Corporation Savings Restoration Plan and Bank Mutual Corporation ESOP Restoration Plan	Exhibit 10.1(b) to the Company's Annual Report on Form 10-K for the year ended December 31, 2003 (“2003 10-K”)	
10.2*	Bank Mutual Corporation Outside Directors' Retirement Plan	Exhibit 10.2 to the Company's Annual Report on Form 10-K for the year ended December 31, 2009 (“2009 10-K”)	
10.3*	Mutual Savings Bank Executive Excess Benefit Plan **	Exhibit 10.3 to Bank Mutual Corporation's Registration Statement on Form S-1, Registration No. 333-39362 (“2000 S-1”)	
10.4*	Agreement regarding deferred compensation dated May 16, 1988 between Mutual Savings Bank and Michael T. Crowley, Sr.	Exhibit 10.4 to 2000 S-1	
10.5(a)*	Employment Agreement between Mutual Savings Bank and Michael T. Crowley Jr. dated December 21, 1993 (continuing , as amended, through 2015)	Exhibit 10.5(a) to 2000 S-1	
10.5(b)*	Amendment thereto dated February 17, 1998	Exhibit 10.5(b) to 2000 S-1	
10.6*	Form of Employment Agreement (with Messrs. Anderegg, Dosland, Larson, and Mayne; continuing through 2013)	Exhibit 10.6(c) to the Company's Annual Report on Form 10-K for the year ended December 31, 2010 (“2010 10-K”)	

<u>Exhibit</u>	<u>Description</u>	<u>Incorporated Herein by Reference To</u>	<u>Filed Herewith</u>
10.7*	Employment Agreement of Mr. Baumgarten with Bank Mutual dated as of April 5, 2010 (continuing through 2014)	Exhibit 10.1 to the Company's Report on Form 8-K dated April 5, 2010	
10.8(a)*	Non-Qualified Deferred Retirement Plan for Directors of First Northern Savings Bank	Exhibit 10.10(a) to the Company's Annual Report on Form 10-K for the year ended December 31, 2000	
10.8(b)*	Amendment No. 1 thereto	Exhibit 10.3.2 to First Northern Capital Corp.'s Annual Report on Form 10-K for the fiscal year ended December 31, 1998	
10.9(a)*	Bank Mutual Corporation 2004 Stock Incentive Plan	Appendix A to Proxy Statement for 2004 Annual Meeting of Shareholders	
10.9(b)(i)*	Form of Option Agreement thereunder—Bank Mutual Corporation Director Stock Option Agreement (superseded)	Exhibit 10.1(b) to the Company's Report on Form 10-Q for the quarter ended June 30, 2004 ("6/30/04 10-Q")	
10.9(b)(ii)*	2011 updated Form of Bank Mutual Corporation Director Stock Option Agreement	Exhibit 10.11(b)(ii) to the 2010 10-K	
10.9(c)(i)*	Form of Option Agreement thereunder—Bank Mutual Corporation Incentive Stock Option Agreement (superseded)	Exhibit 10.1(c) to the 6/30/04 10-Q	
10.9(c)(ii)*	2010 updated Form of Bank Mutual Corporation Incentive Stock Option Agreement	Exhibit 10.11(c)(ii) to the 2010 10-K	
10.9(c)(iii)*	2012 alternate Form of Bank Mutual Corporation Incentive Stock Option Agreement	Exhibit 10.10(c)(iii) to the Company's Annual Report on Form 10-K for the year ended December 31, 2011 ("2011 10-K")	
10.9(d)*	Form of Restricted Stock Agreement thereunder - Bank Mutual Corporation Directors Management Recognition Award	Exhibit 10.1(d) to the 6/30/04 10-Q	
10.9(e)(i)*	Form of Restricted Stock Agreement thereunder—Bank Mutual Corporation Officers Management Recognition Award	Exhibit 10.1(e) to the 6/30/04 10-Q	
10.9(e)(ii)*	2011 updated Form of Bank Mutual Corporation Officers Management Recognition Award	Exhibit 10.11(e)(ii) to the 2010 10-K	

<u>Exhibit</u>	<u>Description</u>	<u>Incorporated Herein by Reference To</u>	<u>Filed Herewith</u>
10.9(e)(iii)*	2012 alternate Form of Bank Mutual Corporation Officers Management Recognition Award	Exhibit 10.10(e)(iii) to the 2011 10-K	
10.10*	Bank Mutual Corporation Management Incentive Plan updated for 2012	Exhibit 10.11(b) to the 2011 10-K	
21.1	List of Subsidiaries		X
23.1	Consent of Deloitte & Touche LLP		X
24.1	Powers of Attorney	Signature Page of this Report	
31.1	Sarbanes-Oxley Act Section 302 Certification signed by the Chairman and Chief Executive Officer of Bank Mutual Corporation		X
31.2	Sarbanes-Oxley Act Section 302 Certification signed by the Senior Vice President and Chief Financial Officer of Bank Mutual Corporation		X
32.1	Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 signed by the Chairman and Chief Executive Officer of Bank Mutual Corporation		X
32.2	Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 signed by the Senior Vice President and Chief Financial Officer of Bank Mutual Corporation		X
101+	The following materials are furnished from Bank Mutual Corporation's Annual Report on Form 10-K for the year ended December 31, 2012, formatted in Extensible Business Reporting Language ("XBRL"): (i) the Unaudited Condensed Consolidated Statements of Financial Condition, (ii) Unaudited Condensed Consolidated Statements of Income, (iii) Unaudited Condensed Consolidated Statements of Equity, (iv) Unaudited Condensed Consolidated Statements of Cash Flow, and (v) Notes to Unaudited Condensed Consolidated Financial Statements tagged as blocks of text.		
101.INS+	XBRL Instance Document		X
101.SCH+	XBRL Taxonomy Extension Schema Document		X
101.CAL+	XBRL Taxonomy Extension Calculation Linkbase Document		X
101.LAB+	XBRL Extension Labels Linkbase Document		X

<u>Exhibit</u>	<u>Description</u>	<u>Incorporated Herein by Reference To</u>	<u>Filed Herewith</u>
101.PRE+	XBRL Taxonomy Extension Presentation Linkbase Document		X
101.DEF+	XBRL Taxonomy Extension Definition Linkbase Document		X

- \* Designates management or compensatory agreements, plans or arrangements required to be filed as exhibits pursuant to Item 15(b) of Form 10-K.
- \*\* Mutual Savings Bank is now known as "Bank Mutual."
- + In accordance with SEC rules, this interactive data file is deemed "furnished" and not "filed" for purposes of Sections 11 or 12 of the Securities Act of 1933 and Section 18 of the Securities and Exchange Act of 1934, and otherwise is not subject to liability under those sections or acts.

## Corporate Information

### Executive Officers

Michael T. Crowley, Jr.	Chairman and Chief Executive Officer
David A. Baumgarten	President
Michael W. Dosland	Senior Vice President, Chief Financial Officer
James P. Carter	Vice President, Secretary
Richard L. Schroeder	Vice President, Controller
P. Terry Anderegg	Senior Vice President, Retail Banking (of the Bank)
Gregory A. Larson	Senior Vice President, Director of Commercial Banking (of the Bank)
Christopher L. Mayne	Senior Vice President, Chief Credit Officer (of the Bank)

### Bank Mutual Corporation Directors

David A. Baumgarten  
David C. Boerke  
Richard A. Brown  
Thomas H. Buestrin  
Michael T. Crowley, Jr.  
Mark C. Herr  
Thomas J. Lopina, Sr.  
William J. Mielke  
Robert B. Olson  
J. Gus Swoboda

### Corporate Offices

Bank Mutual Corporation  
4949 West Brown Deer Road  
Milwaukee, WI 53223  
414-354-1500  
www.bankmutualcorp.com

### Transfer Agent

Inquiries regarding change of address, transfer of stock, lost certificates, and dividend reinvestment should be directed to:  
Registrar and Transfer Company  
10 Commerce Drive  
Cranford, NJ 07016  
800-368-5948

### Independent Auditors

Deloitte & Touche LLP  
555 East Wells Street  
Milwaukee, WI 53202

### General Counsel

Quarles & Brady LLP  
411 East Wisconsin Avenue  
Milwaukee, WI 53202

### Annual Meeting

The 2013 Annual Meeting of Shareholders will be held on May 6, 2013, at 10:00 a.m. at the Four Points Sheraton Milwaukee North Hotel, 8900 North Kildeer Court, Milwaukee, Wisconsin.

### Stock Listing

Bank Mutual Corporation common stock is traded on the NASDAQ Global Select Market under the symbol BKMU.

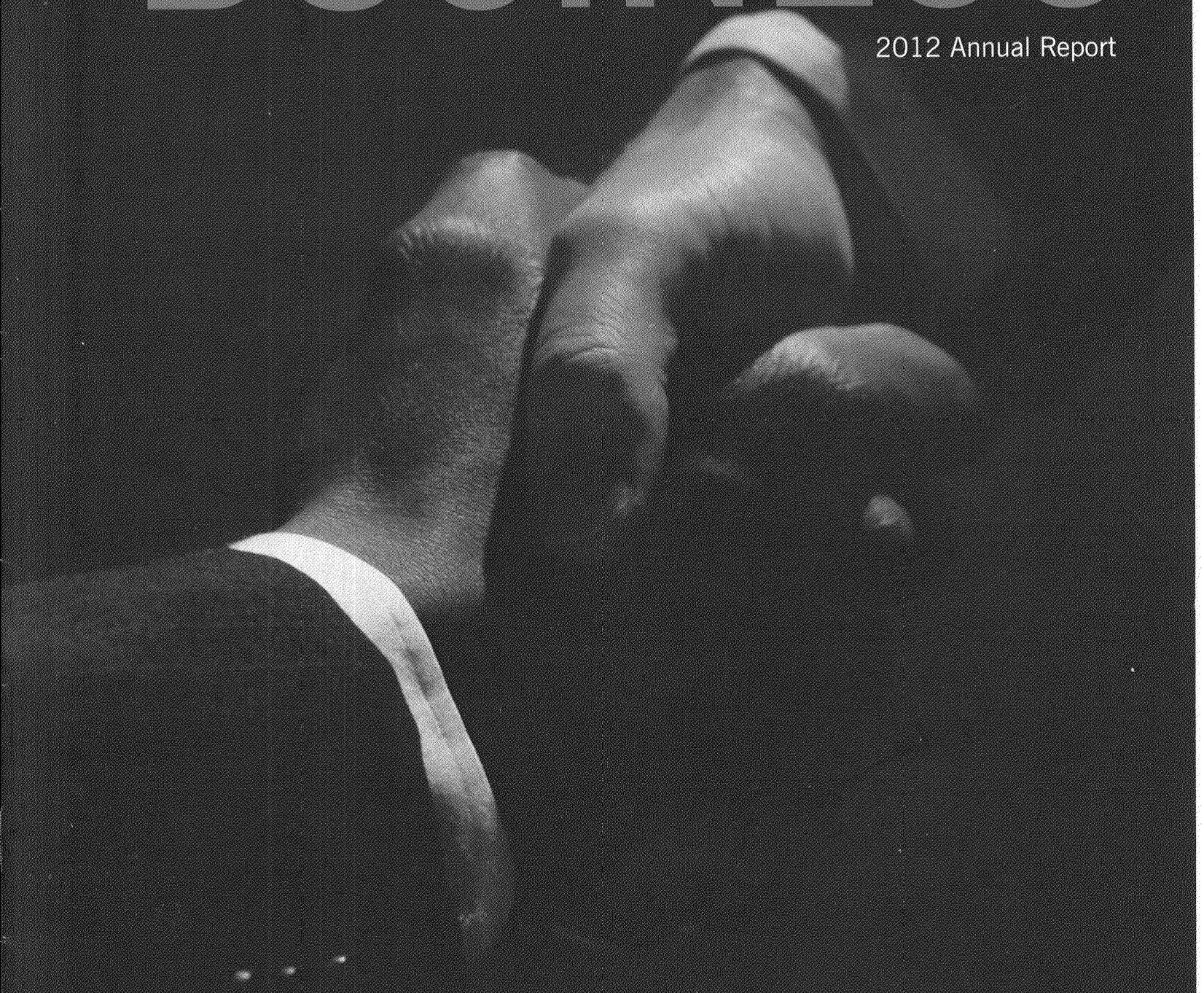
### Investor Relations

Shareholders, analysts, the news media and others desiring general information about the Company or its subsidiaries may contact Michael T. Crowley, Jr., Chairman and Chief Executive Officer, or Michael W. Dosland, Chief Financial Officer, at the corporate offices.

*A copy (without exhibits) of our Annual Report on Form 10-K for the year ended December 31, 2012, as filed with the Securities and Exchange Commission is available to shareholders on our Web site (www.bankmutualcorp.com) or at no charge upon written request to our corporate offices. The Annual Report on Form 10-K is included herewith and includes complete financial statements and other financial information about Bank Mutual Corporation. We urge shareholders and others to read the Form 10-K.*

# WE MEAN BUSINESS

2012 Annual Report



**BankMutual**  
The bank you can really use.

TO OUR SHAREHOLDERS:

# WE MEAN WHAT WE SAY.

A year ago we had the privilege of sharing a vision for a stronger, healthier Bank Mutual. We told our customers, employees, and investors that the tough decisions we had made and the course we had set would lead to positive results, both in terms of the performance of the company and in the banking experiences of our customers.

And while we may not have a crystal ball, a year later we're pleased to report that we delivered on that vision.

But this is merely the beginning. We're energized by the early returns on our hard work, and remain dedicated to serving the needs of our retail and commercial customers. As one of the largest Wisconsin-based banks, our commitment to serving our communities remains strong.

The following pages highlight key successes we achieved in 2012. Our teams continue to excel in earning the business of new retail and commercial banking customers, while offering sound financial solutions to our current customer base.

With asset quality now a competitive advantage, our attention in 2013 will be even more focused on the strategies necessary to increase our revenue and control our expenses.

We'll look to continue to capitalize on the opportunities of an ever-changing banking landscape. Our position as a local financial partner resonates with customers and prospects, as they search for strength in a sea of uncertainty.

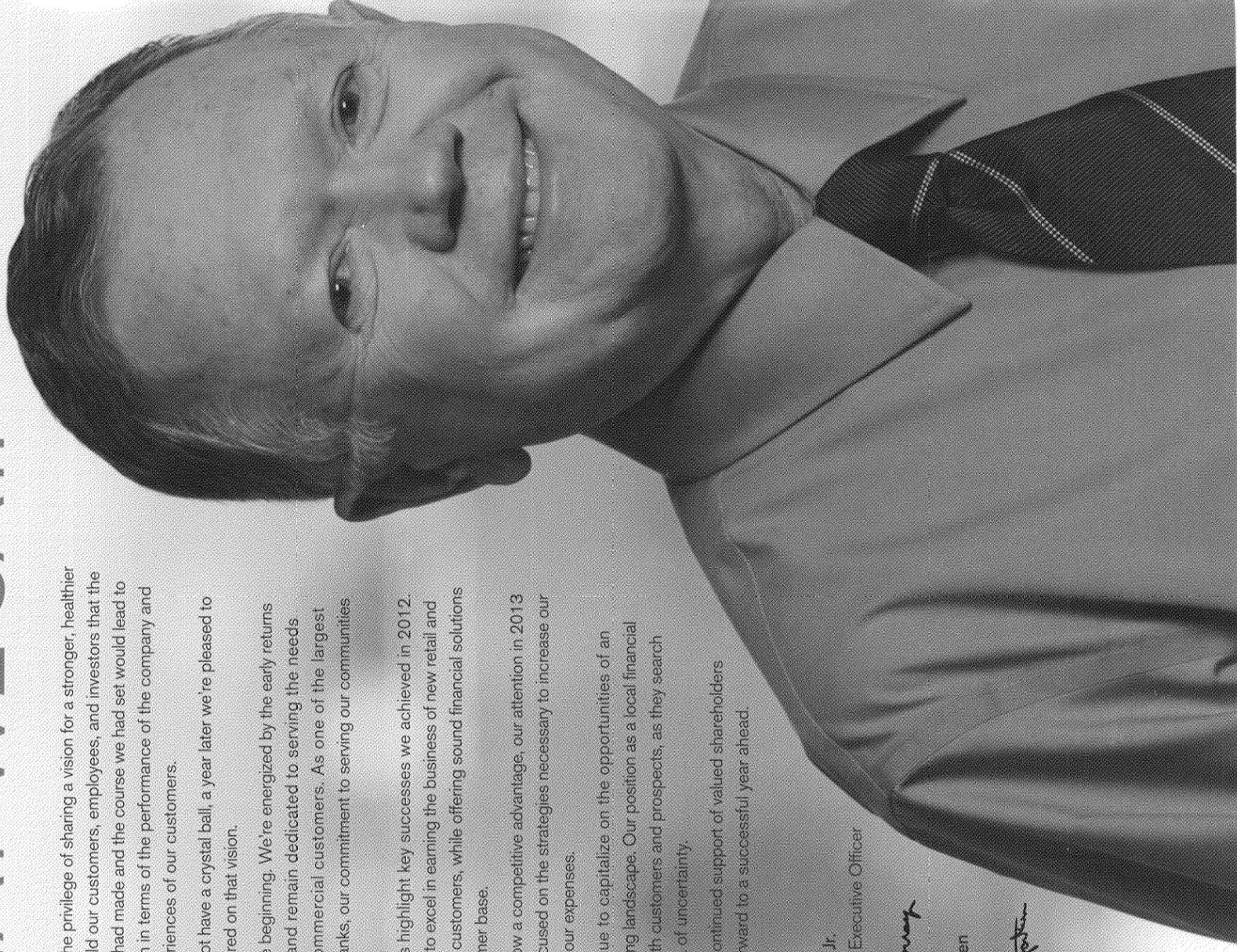
We appreciate the continued support of valued shareholders like you, and look forward to a successful year ahead.

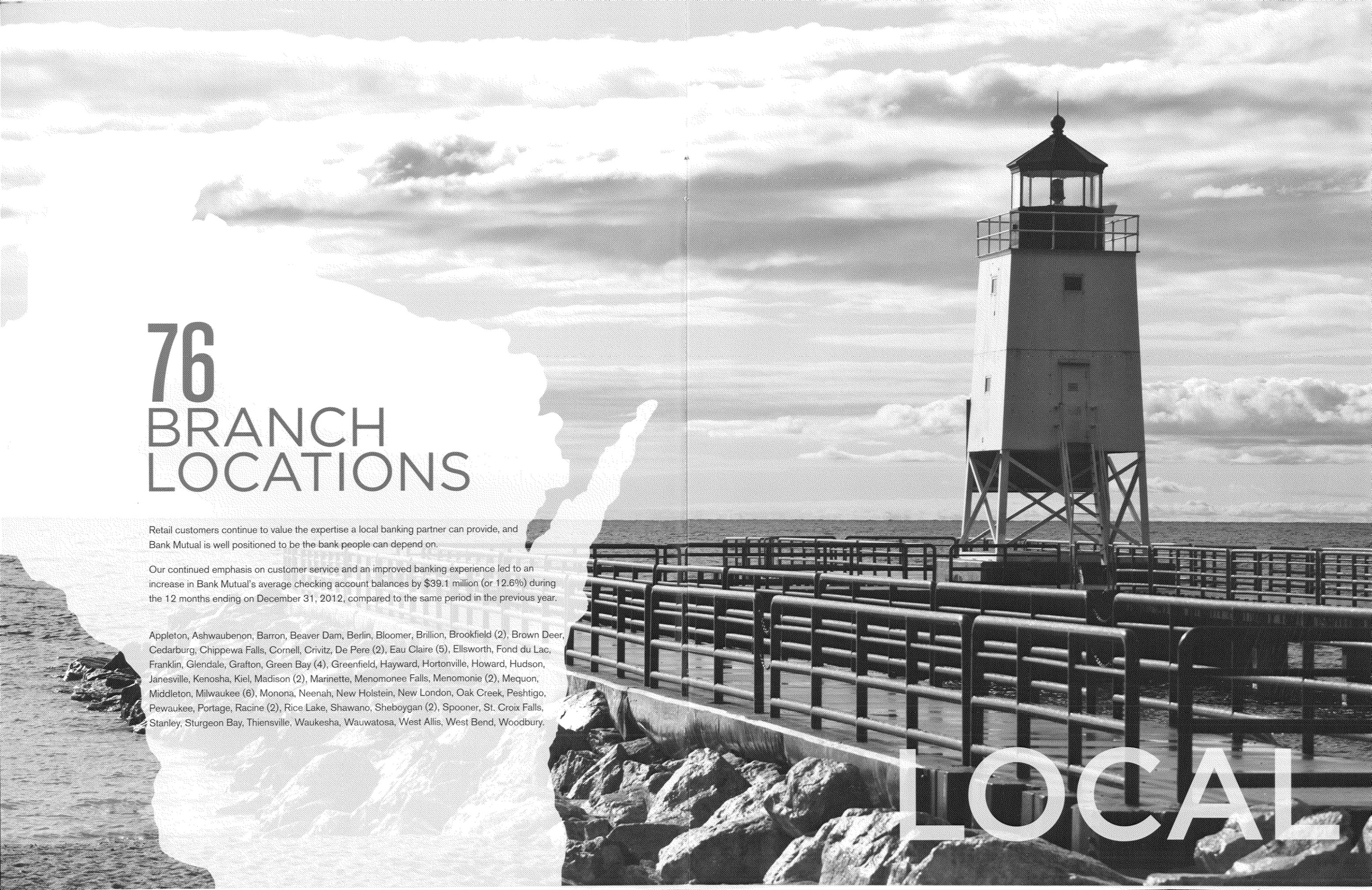
Best regards,

Michael T. Crowley Jr.  
Chairman and Chief Executive Officer



David A. Baumgarten  
President





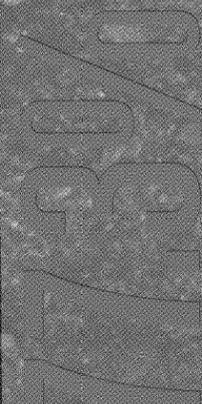
# 76 BRANCH LOCATIONS

Retail customers continue to value the expertise a local banking partner can provide, and Bank Mutual is well positioned to be the bank people can depend on.

Our continued emphasis on customer service and an improved banking experience led to an increase in Bank Mutual's average checking account balances by \$39.1 million (or 12.6%) during the 12 months ending on December 31, 2012, compared to the same period in the previous year.

Appleton, Ashwaubenon, Barron, Beaver Dam, Berlin, Bloomer, Brillion, Brookfield (2), Brown Deer, Cedarburg, Chippewa Falls, Cornell, Crivitz, De Pere (2), Eau Claire (5), Ellsworth, Fond du Lac, Franklin, Glendale, Grafton, Green Bay (4), Greenfield, Hayward, Hortonville, Howard, Hudson, Janesville, Kenosha, Kiel, Madison (2), Marinette, Menomonee Falls, Menomonie (2), Mequon, Middleton, Milwaukee (6), Monona, Neenah, New Holstein, New London, Oak Creek, Peshtigo, Pewaukee, Portage, Racine (2), Rice Lake, Shawano, Sheboygan (2), Spooner, St. Croix Falls, Stanley, Sturgeon Bay, Thiensville, Waukesha, Wauwatosa, West Allis, West Bend, Woodbury.

# LOCAL



## MORE COMMERCIAL AND MULTI-FAMILY LOANS ORIGINATED

The commercial banking team we began to assemble in 2011 capitalized on our dedication to lending to mid-market businesses with tremendous results.

During the past two years, we've augmented our senior management team by hiring experienced leaders and added a number of commercial relationship managers and support personnel experienced in servicing and selling to the mid-tier commercial banking market. By continuing to enhance our team across our markets, Bank Mutual has reaffirmed our pledge to support local businesses with superior lending solutions and sound financial advice.

Moreover, additions to our commercial deposit products and services generated increased fee revenue in 2012, particularly related to treasury management services. In fact, the treasury management team achieved a 74% increase in fee income from the previous year.

Originations of commercial and multi-family loans in 2012 grew by \$146.6 million compared to the same period in 2011.

# DEDICATED



# DRIVEN



# \$6.8 MILLION

NET INCOME

On a full-year basis, Bank Mutual reported net income of \$6.8 million or \$0.15 per diluted share in 2012 and announced an increase in its dividend in the fourth quarter.

## FEWER PROBLEM ASSETS

9.30% 5.70% 1.80% 5.50% 4.00% 1.60%

NON-PERFORMING LOANS TO LOANS

NON-PERFORMING ASSETS TO ASSETS

■ DECEMBER 31, 2010

■ DECEMBER 31, 2011

■ DECEMBER 31, 2012

## REGULATORY CAPITAL RATIOS

5.0% 10.30% 10% 18.00%

TIER 1 CAPITAL

TOTAL RISK-BASED CAPITAL

■ MINIMUM RATIO TO BE WELL CAPITALIZED

■ ACTUAL RATIO AT 12/31/12



## **MICHAEL T. CROWLEY JR. TO RETIRE**

After more than 45 years of dedicated service as an executive officer of Bank Mutual, Michael T. Crowley Jr. will be retiring as our Chief Executive Officer later this year. We are pleased that Mike will be continuing on our Board and remaining as our Chairman. We look forward to continuing to work with Mike in those roles.

All of us at Bank Mutual want to take this opportunity to publicly appreciate Mike for his strong leadership and hard work, and for his many efforts over the years to grow Bank Mutual from a mutual saving and loan with assets of \$150 million into the fourth largest financial institution holding company headquartered in the state of Wisconsin that it is today. Thank you, Mike!

## **EXECUTIVE OFFICERS**

### **MICHAEL T. CROWLEY JR.**

Chairman & Chief Executive Officer

### **DAVID A. BAUMGARTEN**

President

### **MICHAEL W. DOSLAND**

Senior Vice President, Chief Financial Officer

### **JAMES P. CARTER**

Vice President, Secretary & General Counsel

### **RICHARD L. SCHROEDER**

Vice President, Controller

### **P. TERRY ANDEREGG**

Senior Vice President, Retail Banking (of the Bank)

### **GREGORY A. LARSON**

Senior Vice President, Commercial Banking (of the Bank)

### **CHRISTOPHER L. MAYNE**

Senior Vice President, Chief Credit Officer (of the Bank)

## **CORPORATION DIRECTORS**

**DAVID A. BAUMGARTEN, DAVID C. BOERKE, RICHARD A. BROWN, THOMAS H. BUESTRIN, MICHAEL T. CROWLEY JR., MARK C. HERR, THOMAS J. LOPINA SR., WILLIAM J. MIELKE, ROBERT B. OLSON, J. GUS SWOBODA**

## **ANNUAL MEETING**

The 2013 Annual Meeting of Shareholders will be held on May 6, 2013 at 10:00 a.m. at the Four Points Sheraton Milwaukee North Hotel, 8900 North Kildeer Court, Milwaukee, Wisconsin.

## **STOCK LISTING**

Bank Mutual Corporation common stock is traded on the NASDAQ Global Select Market under the symbol BKMU.

## **INVESTOR RELATIONS**

Shareholders, analysts, the news media and others desiring general information about the Company or its subsidiaries may contact Michael T. Crowley Jr., Chairman and Chief Executive Officer, or Michael W. Dosland, Chief Financial Officer, at the Corporate Headquarters.

## **TRANSFER AGENT**

Inquiries regarding change of address, transfer of stock, lost certificates and dividend reinvestment should be directed to:

Registrar and Transfer Company

10 Commerce Drive | Cranford, NJ 07016 | 800-368-5948

## **Independent Auditors**

Deloitte & Touche LLP  
555 East Wells Street  
Milwaukee, WI 53202

## **Corporate Headquarters**

Bank Mutual Corporation  
4949 West Brown Deer Road  
Milwaukee, WI 53223  
414-354-1500 | bankmutualcorp.com

## **General Counsel**

Quarles & Brady LLP  
411 East Wisconsin Avenue  
Milwaukee, WI 53202

# SELECTED FINANCIAL HIGHLIGHTS

## FINANCIAL CONDITION AT DECEMBER 31

Total Assets	\$2,418,264	\$2,498,484	\$2,591,818	\$3,512,064	\$3,489,689
Loans Receivable, net	\$1,402,246	\$1,319,636	\$1,323,569	\$1,506,056	\$1,829,053
Securities Available-for-Sale, at fair value	\$550,185	\$781,770	\$663,257	\$1,480,952	\$1,270,005
Securities Held-to-Maturity, at amortized cost	\$157,558	-	-	-	-
Deposit Liabilities	\$1,867,899	\$2,021,663	\$2,078,310	\$2,137,508	\$2,128,277
Borrowings	\$210,786	\$153,091	\$149,934	\$906,979	\$907,971
Shareholder's Equity	\$271,853	\$265,771	\$312,953	\$402,477	\$399,611
Shareholder's Equity to Total Assets	11.2%	10.6%	12.1%	11.4%	11.5%

## OPERATING RESULTS - YEARS ENDED DECEMBER 31

Net Interest Income	\$61,381	\$82,589	\$46,293	\$68,030	\$73,365
Provision For Loan Losses	\$4,545	\$6,710	\$49,619	\$12,413	\$1,447
Non-Interest Income	\$29,259	\$23,158	\$40,603	\$31,681	\$17,881
Non-Interest Expense <sup>(1)</sup>	\$76,057	\$124,900	\$159,825	\$68,155	\$63,550
Net Income (Loss)	\$6,754	(\$47,565)	(\$72,640)	\$13,725	\$17,156

## PER SHARE DATA AT DECEMBER 31

Diluted Earnings (Loss) Per Share	\$0.15	(\$1.03)	(\$1.59)	\$0.29	\$0.35
Cash Dividends Paid Per Share	\$0.05	\$0.06	\$0.20	\$0.34	\$0.136
Book Value Per Share	\$5.87	\$5.75	\$6.84	\$8.72	\$8.38
Closing Stock Price	\$4.30	\$3.18	\$4.78	\$6.93	\$11.54

## PERFORMANCE RATIOS - YEARS ENDED DECEMBER 31

Return on Average Assets	0.27%	(1.87)%	(2.12)%	0.39%	0.48%
Return on Average Equity	2.50%	(16.37)%	(18.47)%	3.40%	4.15%
Average Net Interest Margin	2.67%	2.76%	1.47%	2.09%	2.21%
Non-Performing Assets to Total Assets	1.64%	4.00%	5.49%	1.72%	1.08%
Allowance for Loan Losses to Loans Receivable, Net	1.54%	2.12%	3.63%	1.13%	0.67%

2012      2011      2010      2009      2008

<sup>(1)</sup> Non-interest expense in 2011 includes a \$52.6 million goodwill impairment and in 2010 includes an \$89.3 million loss on early repayment of FHLB borrowings.

A copy (without exhibits) of our Annual Report on Form 10-K for the year ended December 31, 2012, as filed with the Securities and Exchange Commission, is available to shareholders on our website (bankmutualcorp.com) or at no charge upon written request to our corporate offices. The Annual Report on Form 10-K is included with the proxy statement for Bank Mutual Corporation's 2013 Annual Meeting of Shareholders and includes complete financial statements and other financial information about Bank Mutual Corporation that is not included in this Summary Annual Report. We urge Shareholders and others to read the Form 10-K.

The discussions in this Summary Annual Report that are not historical statements contain forward-looking statements that involve risk and uncertainties. Statements that are not historical statements include those in the future tense or that use terms such as "believe," "expect" and "anticipate." Our actual future results could differ in important and material ways from those discussed. Many factors could cause or contribute to such differences, including those discussed in Item 1A - "Risk Factors" in our Annual Report on Form 10-K filed with the Securities and Exchange Commission.



**Bank Mutual**

The bank you can really use.