

Huron Community Financial Services, Inc.

Consolidated Financial Report
December 31, 2008

Huron Community Financial Services, Inc.

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To the Board of Directors and Stockholders
Huron Community Financial Services, Inc.

We have audited the accompanying consolidated balance sheet of Huron Community Financial Services, Inc. (the "Corporation") as of December 31, 2008 and 2007 and the related consolidated statements of income, stockholders' equity, and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Huron Community Financial Services, Inc. at December 31, 2008 and 2007 and the consolidated results of its operations, changes in stockholders' equity, and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 1, as of January 1, 2008, the Corporation adopted the provisions of EITF 06-4, *Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements*.

Plante & Moran, PLLC

March 10, 2009

Huron Community Financial Services, Inc.

Consolidated Balance Sheet (000s omitted, except per share data)

	December 31, 2008	December 31, 2007
Assets		
Cash and due from banks	\$ 5,159	\$ 3,400
Federal funds sold	129	3,198
Total cash and cash equivalents	5,288	6,598
Investment securities - Available for sale (Note 2)	10,083	12,828
Investment securities - Held to maturity (Note 2)	6,555	5,157
Other securities (Note 2)	1,554	1,494
Loans - Net of allowance for loan losses (Note 3)	151,098	145,688
Premises and equipment (Note 5)	3,541	3,773
Intangible assets	749	978
Accrued interest receivable	670	817
Other assets	6,919	4,399
Total assets	\$ 186,457	\$ 181,732
Liabilities and Stockholders' Equity		
Liabilities		
Deposits:		
Noninterest-bearing	\$ 20,916	\$ 19,936
Interest-bearing (Note 6)	121,551	119,393
Total deposits	142,467	139,329
Short-term borrowings (Note 7)	5,385	6,240
Borrowings (Note 8)	17,000	13,000
Accrued and other liabilities	1,313	1,555
Total liabilities	166,165	160,124
Stockholders' Equity		
Common stock - \$1 par value:		
Authorized - 1,050,000 shares		
Issued and outstanding - 568,891 shares and 587,185 shares in 2008 and 2007, respectively	569	587
Additional paid-in capital	17,540	15,306
Undivided profits	2,147	5,698
Accumulated other comprehensive income	36	17
Total stockholders' equity	20,292	21,608
Total liabilities and stockholders' equity	\$ 186,457	\$ 181,732

Huron Community Financial Services, Inc.

Consolidated Statement of Income (000s omitted, except per share data)

	Year Ended	
	December 31, 2008	December 31, 2007
Interest Income		
Loans - Including fees	\$ 10,169	\$ 11,528
Investment securities	805	955
Federal funds sold	117	232
Total interest income	11,091	12,715
Interest Expense		
Deposits	3,023	4,229
Interest on FHLB advances	812	679
Interest on short-term borrowings	83	111
Total interest expense	3,918	5,019
Net Interest Income	7,173	7,696
Provision for Loan Losses (Note 3)	408	150
Net Interest Income After Provision for Loan Losses	6,765	7,546
Other Operating Income		
Service charges - Deposits	618	572
Impairment loss on investment securities	(863)	-
Loan servicing income - Net	292	254
Other	218	243
Total other operating income	265	1,069
Other Operating Expenses		
Salaries and employee benefits	2,943	3,049
Amortization of intangible assets	229	229
Occupancy expense	482	430
Service fees	227	204
Depreciation expense	360	371
Other	1,372	1,229
Total other operating expenses	5,613	5,512
Income - Before income taxes	1,417	3,103
Provision for Income Taxes (Note 9)	324	821
Net Income	<u>\$ 1,093</u>	<u>\$ 2,282</u>
Earnings per Share		
Basic earnings per common share	\$ 1.85	\$ 3.85
Diluted earnings per common share	1.78	3.68

Huron Community Financial Services, Inc.

Consolidated Statement of Stockholders' Equity (000s omitted, except per share data)

	Common Stock	Additional Paid-in Capital	Undivided Profits	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity
Balance - January 1, 2007	\$ 586	\$ 13,424	\$ 6,878	\$ (12)	\$ 20,876
Comprehensive income:					
Net income	-	-	2,282	-	2,282
Change in net unrealized loss on securities available for sale - Net of tax benefit of \$15	-	-	-	29	29
Total comprehensive income					2,311
Sale of common stock	44	1,754	-	-	1,798
Purchases of common stock	(43)	-	(2,282)	-	(2,325)
Tax effect of stock options exercised	-	113	-	-	113
Stock-based compensation	-	15	-	-	15
Dividends declared \$2.00 per common share	-	-	(1,180)	-	(1,180)
Balance - December 31, 2007	587	15,306	5,698	17	21,608
Change in accounting for split-dollar arrangement	-	-	(136)	-	(136)
Comprehensive income:					
Net income	-	-	1,093	-	1,093
Change in net unrealized loss on securities available for sale - Net of tax benefit of \$10	-	-	-	19	19
Total comprehensive income					1,112
Sale of common stock	45	2,117	-	-	2,162
Purchases of common stock	(63)	-	(3,096)	-	(3,159)
Tax effect of stock options exercised	-	106	-	-	106
Stock-based compensation	-	11	-	-	11
Dividends declared \$2.40 per common share	-	-	(1,412)	-	(1,412)
Balance - December 31, 2008	\$ 569	\$ 17,540	\$ 2,147	\$ 36	\$ 20,292

Huron Community Financial Services, Inc.

Consolidated Statement of Cash Flows (000s omitted)

	Year Ended	
	December 31, 2008	December 31, 2007
Cash Flows from Operating Activities		
Net income	\$ 1,093	\$ 2,282
Adjustments to reconcile net income to net cash from operating activities:		
Depreciation and amortization	589	600
Impairment loss on investment securities	863	-
Provision for loan losses	408	150
Amortization and accretion on securities	116	(67)
Stock-based compensation	11	15
Net change in:		
Accrued interest receivable and late fees	147	94
Other assets	(2,530)	(537)
Accrued expenses and other liabilities	(378)	(36)
Net cash provided by operating activities	319	2,501
Cash Flows from Investing Activities		
Activity in available-for-sale securities:		
Maturities, prepayments, and calls	18,925	7,267
Purchases	(17,179)	(3,494)
Activity in held-to-maturity securities:		
Maturities, prepayments, and calls	1,478	1,015
Purchases	(2,887)	(1,029)
Net (increase) decrease in loans	(5,818)	1,207
Capital expenditures	(128)	(250)
Net cash (used in) provided by investing activities	(5,609)	4,716
Cash Flows from Financing Activities		
Net increase (decrease) in deposits	3,138	(3,453)
Net change in short-term borrowings	(855)	848
Proceeds from FHLB advances	5,000	7,000
Payments on FHLB advances	(1,000)	(9,500)
Proceeds from sale of common stock	2,162	1,798
Purchases of common stock	(3,159)	(2,325)
Tax effect of stock options exercised	106	113
Cash dividends paid on common stock	(1,412)	(1,180)
Net cash provided by (used in) financing activities	3,980	(6,699)
Net (Decrease) Increase in Cash and Cash Equivalents	(1,310)	518
Cash and Cash Equivalents - Beginning of year	6,598	6,080
Cash and Cash Equivalents - End of year	\$ 5,288	\$ 6,598
Supplemental Cash Flow Information - Cash paid for		
Interest	\$ 4,033	\$ 5,034
Income taxes	490	1,025

Huron Community Financial Services, Inc.

Notes to Consolidated Financial Statements December 31, 2008 and 2007

Note 1 - Nature of Business and Significant Accounting Policies

Basis of Presentation and Consolidation - The consolidated financial statements include the accounts of Huron Community Financial Services, Inc. (the "Corporation") and its wholly owned subsidiary, Huron Community Bank (the "Bank"). The Bank also owns 100 percent of HCB Investments, Inc., which provides insurance products to customers. All significant intercompany transactions and balances have been eliminated. The 000s have been omitted in tabular columns.

Change in Accounting Principle - On January 1, 2008, the Corporation adopted the provisions of EITF 06-4, *Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements*. EITF 06-4 requires the recognition of a liability and related compensation costs for endorsement split-dollar life insurance arrangements that provide a benefit to an employee that extends to postretirement periods. The Corporation has recognized the effects of applying EITF 06-4 as a change in accounting principle through a cumulative-effect adjustment to retained earnings as of January 1, 2008. Retained earnings decreased and other liabilities increased by \$136,000 on January 1, 2008 as a result of the adoption of EITF 06-4. Subsequent changes to the liability recognized by the Corporation are recorded as compensation expense in the consolidated statement of income.

Use of Estimates - In preparing consolidated financial statements in conformity with accounting principles generally accepted in the United States of America, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the consolidated balance sheet and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses, the valuation of investment securities, mortgage servicing rights, impairment of intangible assets, and goodwill.

Nature of Operations - The Bank operates in Iosco, Arenac, and southern Alcona counties in the state of Michigan. The Bank's revenue results primarily from providing real estate and commercial loans and, to a lesser extent, consumer loans. Its primary deposit products are savings and term certificate accounts.

Significant Group Concentrations of Credit Risk - Most of the Corporation's activities are with customers located within the counties of Iosco, Arenac, and Alcona in Michigan. Note 2 discusses the types of securities in which the Corporation invests. Note 3 discusses the types of lending in which the Corporation engages. The Corporation does not have any significant concentrations to any one industry or customer.

Huron Community Financial Services, Inc.

Notes to Consolidated Financial Statements December 31, 2008 and 2007

Note 1 - Nature of Business and Significant Accounting Policies (Continued)

Cash and Cash Equivalents - Cash and cash equivalents include cash on hand, amounts due from banks, and federal funds sold. Federal funds sold are generally sold for one-day periods.

Securities - Debt securities that management has the positive intent and ability to hold to maturity are classified as "held to maturity" and recorded at amortized cost. Securities not classified as held to maturity or trading, including equity securities with readily determinable fair values, are classified as "available for sale" and are recorded at fair value, with unrealized gains and losses excluded from earnings and reported in other comprehensive income. Restricted investment securities include Federal Reserve and Federal Home Loan Bank stock and are carried at cost.

Purchase premiums and discounts are recognized in interest income using the interest method over the terms of the securities. Declines in the fair value of held-to-maturity and available-for-sale securities below their cost that are deemed to be other than temporary are reflected in earnings as realized losses. In estimating other-than-temporary impairment losses, management considers (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, and (3) the intent and ability of the Corporation to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value. Gains and losses on the sale of securities are recorded on the trade date and are determined using the specific identification method.

Loans - The Corporation grants mortgage, commercial, and consumer loans to customers. A substantial portion of the loan portfolio is represented by mortgage loans throughout Michigan. The ability of the Corporation's debtors to honor their contracts is dependent upon the real estate and general economic conditions in this area.

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or pay-off are reported at their outstanding unpaid principal balances adjusted for charge-offs, the allowance for loan losses, and any deferred fees or costs on originated loans. Interest income is accrued on the unpaid principal balance. Loan origination fees, net of certain direct origination costs, are deferred and recognized as an adjustment of the related loan yield using the interest method.

The accrual of interest on loans is discontinued at the time the loan is 90 days delinquent unless the credit is well-secured and in process of collection. In all cases, loans are placed on nonaccrual or charged off at an earlier date if collection of principal or interest is considered doubtful.

Huron Community Financial Services, Inc.

Notes to Consolidated Financial Statements December 31, 2008 and 2007

Note 1 - Nature of Business and Significant Accounting Policies (Continued)

All interest accrued but not collected for loans that are placed on nonaccrual or charged off is reversed against interest income. The interest on these loans is accounted for on the cash basis or cost-recovery method, until qualifying for return to accrual. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Allowance for Loan Losses - The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

The allowance for loan losses is evaluated on a regular basis by management and is based upon management's periodic review of the collectibility of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral, and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

The allowance consists of specific, general, and unallocated components. The specific component relates to loans that are classified as either doubtful, substandard, or special mention. For such loans that are also classified as impaired, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan. The general component covers nonclassified loans and is based on historical loss experience adjusted for qualitative factors. An unallocated component is maintained to cover uncertainties that could affect management's estimate of probable losses. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general losses in the portfolio.

Huron Community Financial Services, Inc.

Notes to Consolidated Financial Statements December 31, 2008 and 2007

Note 1 - Nature of Business and Significant Accounting Policies (Continued)

A loan is considered impaired when, based on current information and events, it is probable that the Corporation will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan-by-loan basis for commercial and construction loans by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price, or the fair value of the collateral if the loan is collateral dependent.

Large groups of homogeneous loans are collectively evaluated for impairment. Accordingly, the Corporation does not separately identify individual consumer and residential loans for impairment disclosures.

Off-balance-sheet Instruments - In the ordinary course of business, the Corporation has entered into commitments under commercial letters of credit and standby letters of credit. The Corporation is considered a guarantor when it issues a letter of credit. Accordingly, the Corporation recognizes, at the inception of a guarantee, a liability for the fair value of the obligation undertaken.

Banking Premises and Equipment - Land is carried at cost. Buildings and equipment are carried at cost, less accumulated depreciation computed on the straight-line method over the estimated useful lives of the assets.

Comprehensive Income - Accounting principles generally require that recognized revenue, expenses, gains, and losses be included in net income. Although certain changes in assets and liabilities, such as unrealized gains and losses on available-for-sale securities, are reported as a separate component of the equity section of the consolidated balance sheet, such items, along with net income, are components of comprehensive income.

Huron Community Financial Services, Inc.

Notes to Consolidated Financial Statements December 31, 2008 and 2007

Note 1 - Nature of Business and Significant Accounting Policies (Continued)

The components of other comprehensive income and related tax effects are as follows (000s omitted):

	2008	2007
Unrealized holding (losses) gains on available-for-sale securities	\$ (834)	\$ 44
Reclassification adjustment for losses realized in income	863	-
Net unrealized gains	29	44
Tax effect	(10)	(15)
Other comprehensive income	\$ 19	\$ 29

Servicing - Servicing assets are recognized as separate assets when rights are acquired through purchase or through sale of financial assets. Capitalized servicing rights are reported in other assets and are amortized into noninterest income in proportion to, and over the period of, the estimated future net servicing income of the underlying financial assets. Servicing assets are evaluated for impairment based on the fair value of the rights as compared to amortized cost. Impairment is determined by stratifying rights by predominant characteristics, such as interest rates and terms. Fair value is determined by using prices for similar assets with similar characteristics, when available, or based on discounted cash flows using market-based assumptions. Impairment is recognized through a valuation allowance for an individual stratum, to the extent that fair value is less than the capitalized amount for the stratum.

Intangible Assets - In connection with certain branch acquisitions, the excess of purchase price over the fair value of net assets acquired has been allocated to core deposit intangibles, which are being amortized over 10 years to 15 years. The amount recorded as core deposit intangibles totaled \$344,000 and \$573,000 as of December 31, 2008 and 2007, respectively. The carrying amount is net of amortization of \$2,941,000 and \$2,712,000 as of December 31, 2008 and 2007, respectively. The expected amortization is \$229,000 for 2009 and \$115,000 for 2010. In connection with the purchase of the bank, the excess of purchase price over fair value of net assets acquired has been allocated to goodwill. In accordance with Statement of Financial Accounting Standards No. 142 (FAS 142), *Goodwill and Other Intangibles*, which was adopted in January 1, 2002, goodwill is not amortized. The amount recorded as goodwill totaled \$405,000 as of December 31, 2008 and 2007.

Huron Community Financial Services, Inc.

Notes to Consolidated Financial Statements December 31, 2008 and 2007

Note 1 - Nature of Business and Significant Accounting Policies (Continued)

Earnings per Common Share - Earnings per common share are computed by dividing net income by the average number of common shares outstanding during the period. The number of weighted average common shares outstanding was 590,406 and 592,403 for the years ended December 31, 2008 and 2007, respectively. The Corporation uses the treasury stock method to compute diluted earnings per share, which assumes that proceeds from the assumed exercise of stock options would be used to purchase common stock at the average market price during the period. The dilutive effect of stock options increased average common shares outstanding by 24,242 and 27,081 shares at December 31, 2008 and 2007, respectively.

Note 2 - Securities

The amortized cost and fair value of securities, with gross unrealized gains and losses, are as follows (000s omitted):

	2008			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Market Value
Available-for-sale securities:				
U.S. government and federal agency	\$ 7,502	\$ 52	\$ -	\$ 7,554
Corporate	1,631	-	-	1,631
State and municipal	895	10	(7)	898
Total available-for- sale securities	<u>\$ 10,028</u>	<u>\$ 62</u>	<u>\$ (7)</u>	<u>\$ 10,083</u>
Held-to-maturity securities - State and municipal	<u>\$ 6,555</u>	<u>\$ 92</u>	<u>\$ (32)</u>	<u>\$ 6,615</u>

Huron Community Financial Services, Inc.

Notes to Consolidated Financial Statements December 31, 2008 and 2007

Note 2 - Securities (Continued)

	2007			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Market Value
Available-for-sale securities:				
U.S. government and federal agency	\$ 8,904	\$ 19	\$ -	\$ 8,923
Corporate	2,999	-	(6)	2,993
Mortgage-backed	3	-	-	3
State and municipal	895	14	-	909
Total available-for- sale securities	<u>\$ 12,801</u>	<u>\$ 33</u>	<u>\$ (6)</u>	<u>\$ 12,828</u>
Held-to-maturity securities - State and municipal	<u>\$ 5,157</u>	<u>\$ 57</u>	<u>\$ (11)</u>	<u>\$ 5,203</u>

At December 31, 2008 and 2007, securities with a carrying value of \$7,553,685 and \$8,923,000, respectively, were pledged to secure borrowings and public deposits and for other purposes required or permitted by law.

The amortized cost and fair value of debt securities by contractual maturity at December 31, 2008 follow (000s omitted):

	Available for Sale		Held to Maturity	
	Amortized Cost	Market Value	Amortized Cost	Market Value
Due in one year or less	\$ 8,633	\$ 8,694	\$ 3,028	\$ 3,025
Due in one through five years	395	389	2,299	2,336
Due after five years through 10 years	-	-	1,183	1,209
Due after 10 years	1,000	1,000	45	45
Total	<u>\$ 10,028</u>	<u>\$ 10,083</u>	<u>\$ 6,555</u>	<u>\$ 6,615</u>

Huron Community Financial Services, Inc.

Notes to Consolidated Financial Statements December 31, 2008 and 2007

Note 2 - Securities (Continued)

Information pertaining to securities with gross unrealized losses at December 31, 2008 and 2007, aggregated by investment category and length of time that individual securities have been in a continuous loss position, is as follows (000s omitted):

	2008			
	Less Than 12 Months		Over 12 Months	
	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value
Available-for-sale securities -				
State and municipal	\$ 7	\$ 389	\$ -	\$ -
Held-to-maturity - State and municipal	\$ 13	\$ 923	\$ 19	\$ 161
	2007			
	Less Than 12 Months		Over 12 Months	
	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value
Available-for-sale securities -				
Corporate	\$ -	\$ -	\$ 6	\$ 493
Held-to-maturity securities -				
State and municipal	\$ 1	\$ 45	\$ 10	\$ 550

Unrealized losses on securities have not been recognized into income because the issuers' bonds are of high credit quality, the Corporation has the intent and ability to hold the securities for the foreseeable future, and the decline in fair value is due primarily to increased market interest rates. The fair value is expected to recover as the bonds approach the maturity date.

Other securities, totaling \$1,554,000 and \$1,494,000 at December 31, 2008 and 2007, respectively, consist of restricted Federal Home Loan Bank stock and Federal Reserve Bank stock. These stocks are carried at cost, which approximates market value.

Huron Community Financial Services, Inc.

Notes to Consolidated Financial Statements December 31, 2008 and 2007

Note 3 - Loans

A summary of the balances of loans follows (000s omitted):

	2008	2007
Mortgage loans on real estate - Residential 1-4 family	\$ 58,935	\$ 63,039
Commercial and commercial real estate	81,224	71,117
Consumer installment loans	13,088	13,768
Total loans	153,247	147,924
Less allowances for loan losses	2,149	2,236
Net loans	\$ 151,098	\$ 145,688
Allowance for loan losses as a percent of loans	1.40%	1.51%

An analysis of the allowance for loan losses follows (000s omitted):

	2008	2007
Balance - Beginning of year	\$ 2,236	\$ 2,388
Provision charged to operations	408	150
Loans charged off	(506)	(308)
Loan recoveries	11	6
Balance - End of year	\$ 2,149	\$ 2,236

The following is a summary of information pertaining to impaired loans (000s omitted):

	2008	2007
Impaired loans without a valuation allowance	\$ 692	\$ -
Impaired loans with a valuation allowance	1,166	3,014
Total impaired loans	\$ 1,858	\$ 3,014
Valuation allowance related to impaired loans	\$ 270	\$ 455
Total nonaccrual loans	2,766	1,469
Loans 90 days delinquent and still accruing	1,840	513

The following is a summary of information pertaining to impaired loans (000s omitted):

	2008	2007
Average investment in impaired loans	\$ 2,463	\$ 3,001
Interest income recognized on impaired loans	-	-
Interest income recognized on a cash basis on impaired loans	-	-

No additional funds are committed to be advanced in connection with impaired loans.

Huron Community Financial Services, Inc.

Notes to Consolidated Financial Statements December 31, 2008 and 2007

Note 3 - Loans (Continued)

The Corporation has had, and expects to have in the future, transactions with the Corporation's executive officers, directors, and their affiliates. Such transactions were made in the ordinary course of business and included extensions of credit, all of which were made on substantially the same terms, including interest rates and collateral, as those prevailing at the same time for comparable transactions with other customers, and did not, in management's opinion, involve more than a normal risk of collectibility or present other unfavorable features. The aggregate amount of such loans attributable to persons who were related parties approximated \$5,923,787 at the beginning of 2008 and \$5,182,000 at the end of 2008. During 2008, new loans to related parties aggregated \$1,031,849 and repayments totaled \$89,315.

Note 4 - Loan Servicing

Loans serviced for others are not included in the accompanying consolidated balance sheet. The unpaid principal balances of mortgage and other loans serviced for others were \$67,502,568 and \$66,421,000 at December 31, 2008 and 2007, respectively.

The balance of capitalized servicing rights, net of valuation allowance, included in other assets at December 31, 2008 and 2007 was \$337,000 and \$382,000, respectively. The fair value of the capitalized servicing rights approximates the carrying value. The key economic assumptions used in determining the fair value of the mortgage servicing rights include an annual constant prepayment speed (CPR) of 12.27 percent and 13.26 percent for December 31, 2008 and 2007, respectively, and a discount rate of 8.0 percent and 9.0 percent for December 31, 2008 and 2007, respectively.

The following summarizes mortgage servicing rights capitalized and amortized, along with the aggregate activity in related valuation allowances (000s omitted):

	2008	2007
Mortgage servicing rights capitalized	\$ 123	\$ 89
Mortgage servicing rights amortized	193	143
Valuation allowances:		
Balance at beginning of year	25	25
Balance at end of year	-	25

Huron Community Financial Services, Inc.

Notes to Consolidated Financial Statements December 31, 2008 and 2007

Note 5 - Bank Premises and Equipment

A summary of the cost and accumulated depreciation of premises and equipment follows (000s omitted):

	2008	2007
Buildings and improvements	\$ 4,205	\$ 4,157
Furniture and fixtures	2,542	2,506
Vault and equipment	300	300
Automobiles	106	135
Land	711	667
Total premises and equipment	7,864	7,765
Accumulated depreciation	(4,323)	(3,992)
Net premises and equipment	\$ 3,541	\$ 3,773

Depreciation expense for the years ended December 31, 2008 and 2007 amounted to \$360,000 and \$371,000, respectively.

Note 6 - Deposits

The following is a summary of the distribution of interest-bearing deposits at December 31 (000s omitted):

	2008	2007
NOW accounts	\$ 46,100	\$ 45,361
Savings	12,756	12,154
Money market demand	995	623
Time:		
Under \$100,000	46,069	44,846
\$100,000 and over	15,631	16,409
Total interest-bearing deposits	\$ 121,551	\$ 119,393

Huron Community Financial Services, Inc.

Notes to Consolidated Financial Statements December 31, 2008 and 2007

Note 6 - Deposits (Continued)

At December 31, 2008, the scheduled maturities of time deposits are as follows (000s omitted):

2009	\$	40,881
2010		11,110
2011		7,421
2012		<u>2,288</u>
Total	\$	<u>61,700</u>

Note 7 - Short-term Borrowings

Short-term borrowings include securities sold under agreements to repurchase, which are classified as secured borrowings and generally mature within one to four days from the transaction date. Securities sold under agreements to repurchase are reflected at the amount of cash received in connection with the transaction. The Corporation may be required to provide additional collateral based on the fair value of the underlying securities.

Note 8 - FHLB Advances

The Bank has advances from Federal Home Loan Bank. Interest rates range from 2.96 percent to 4.95 percent. Interest is payable monthly. The advances are collateralized by approximately \$29,500,000 and \$34,437,000 of mortgage loans as of December 31, 2008 and 2007, respectively, under a blanket collateral agreement.

The advances are subject to prepayment penalties and the provisions and conditions of the credit policy of Federal Home Loan Bank. Future obligations of the advances are as follows at December 31, 2008 (000s omitted):

2009	\$	5,000
2010		9,000
2011		2,000
2012		-
2013		<u>1,000</u>
Total	\$	<u>17,000</u>

Huron Community Financial Services, Inc.

Notes to Consolidated Financial Statements December 31, 2008 and 2007

Note 9 - Income Taxes

The components of the net deferred tax assets, included in other assets, are as follows (000s omitted):

	<u>2008</u>	<u>2007</u>
Deferred tax assets:		
Allowance for loan losses	\$ 643	\$ 688
Accrued employee benefits	181	156
Total deferred tax assets	<u>824</u>	<u>844</u>
Deferred tax liabilities:		
Depreciation	123	115
Net unrealized gain on securities available for sale	19	9
Investment in subsidiary	117	130
Prepaid assets	20	23
Other	18	30
Total deferred tax liabilities	<u>297</u>	<u>307</u>
Net deferred tax assets	<u>\$ 527</u>	<u>\$ 537</u>

Allocation of income taxes between current and deferred portions is as follows (000s omitted):

	<u>2008</u>	<u>2007</u>
Current	\$ 324	\$ 821
Deferred	-	-

The reasons for the differences between the income tax expense at the federal statutory income tax rate and the recorded income tax expense are summarized as follows (000s omitted):

	<u>2008</u>	<u>2007</u>
Income before income taxes	\$ 1,417	\$ 3,103
Income tax expense at federal statutory rate of 34 percent	\$ 482	\$ 1,055
Increases resulting from nondeductible expenses	7	6
Decreases resulting from nontaxable income	(165)	(240)
Net income tax expense	<u>\$ 324</u>	<u>\$ 821</u>

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Notes to Consolidated Financial Statements December 31, 2008 and 2007

Note 10 - Benefit Plan

The Corporation has a 401(k) plan whereby a certain percentage of employees' contributions can be matched with discretionary contributions by the Corporation. Contributions to the plan for the years ended December 31, 2008 and 2007 were \$78,000 and \$73,000, respectively.

Note 11 - Fair Value of Financial Instruments

The fair value of a financial instrument is the current amount that would be exchanged between willing parties, other than in a forced liquidation. Fair value is best determined based upon quoted market prices. However, in many instances, there are no quoted market prices for the Corporation's various financial instruments. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. Accordingly, the fair value estimates may not be realized in an immediate settlement of the instrument. SFAS 107 excludes certain financial instruments and all nonfinancial instruments from its disclosure requirements. Accordingly, the aggregate fair value amounts presented may not necessarily represent the underlying fair value of the Corporation.

The following methods and assumptions were used by the Corporation in estimating fair value disclosures for financial instruments:

Cash and Cash Equivalents - The carrying amounts of cash and cash equivalents approximate fair values.

Securities - Fair values of securities are based on quoted market prices. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities. The carrying value of Federal Home Loan Bank and Federal Reserve Bank stock approximates fair value based on the redemption provisions of the issuers.

Loans Receivable - For variable rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying values. Fair values for other loans are estimated using discounted cash flow analyses, using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality. Fair values of nonperforming loans are estimated using discounted cash flow analyses or underlying collateral values, where applicable.

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Notes to Consolidated Financial Statements December 31, 2008 and 2007

Note 11 - Fair Value of Financial Instruments (Continued)

Deposit Liabilities - The fair values disclosed for demand deposits are, by definition, equal to the amount payable on demand at the reporting date (i.e., their carrying amounts). The carrying amounts of variable rate, fixed-term money market accounts and certificates of deposit approximate their fair values at the reporting date. Fair values for fixed rate certificates of deposit are estimated using a discounted cash flow calculation that applies interest rates currently being offered on certificates to a schedule of aggregated expected monthly maturities on time deposits.

Short-term Borrowings - The carrying amounts of federal funds purchased, borrowings under repurchase agreements, and other short-term borrowings maturing within 90 days approximate their fair values. Fair values of other short-term borrowings are estimated using discounted cash flow analyses based on the Corporation's current incremental borrowing rates for similar types of borrowing arrangements.

Other Borrowings - The fair values of the Corporation's other borrowings are estimated using discounted cash flow analyses based on the Corporation's current incremental borrowing rates for similar types of borrowing arrangements.

Accrued Interest - The carrying amounts of accrued interest approximate fair value.

Other Financial Instruments - The fair value of other financial instruments, including loan commitments and unfunded letters of credit, based on discounted cash flow analyses, is not material.

The estimated fair values and related carrying or notional amounts of the Corporation's financial instruments are as follows (000s omitted):

	2008		2007	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Financial assets:				
Cash and cash equivalents	\$ 5,288	\$ 5,288	\$ 6,598	\$ 6,598
Securities	18,192	18,252	19,479	19,525
Loans	151,098	150,968	145,688	147,369
Accrued interest receivable	670	670	817	817
Financial liabilities:				
Demand deposits	20,916	20,916	19,936	19,936
Interest-bearing deposits	121,551	120,784	119,393	117,119
FHLB advances	17,000	17,636	13,000	13,250
Short-term borrowings	5,385	5,219	6,240	6,240
Accrued interest payable	255	255	370	370

Huron Community Financial Services, Inc.

Notes to Consolidated Financial Statements December 31, 2008 and 2007

Note 12 - Off-balance-sheet Activities

Credit-related Financial Instruments - The Corporation is a party to credit-related financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit, standby letters of credit, and commercial letters of credit. Such commitments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the consolidated balance sheet.

The Corporation's exposure to credit loss is represented by the contractual amount of these commitments. The Corporation follows the same credit policies in making commitments as it does for on-balance-sheet instruments.

At December 31, 2008 and 2007, the following financial instruments were outstanding whose contract amounts represent credit risk (000s omitted):

	Contract Amount	
	2008	2007
Unfunded commitments	\$ 21,184	\$ 20,154

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 may require payment of a fee. The commitments for equity lines of credit may expire without being drawn upon. Therefore, the total commitment amounts do not necessarily represent future cash requirements. The amount of collateral obtained, if it is deemed necessary by the Corporation, is based on management's credit evaluation of the customer.

Unfunded commitments under commercial lines of credit, revolving credit lines, and overdraft protection agreements are commitments for possible future extensions of credit to existing customers. These lines of credit are collateralized and usually do not contain a specified maturity date and may not be drawn upon to the total extent to which the Corporation is committed.

Commercial and standby letters of credit are conditional commitments issued by the Corporation to guarantee the performance of a customer to a third party. Those letters of credit are used primarily to support public and private borrowing arrangements. Essentially all letters of credit issued have expiration dates within one year. The credit risk involved is extending loan facilities to customers. The Corporation generally holds collateral supporting those commitments if deemed necessary.

Huron Community Financial Services, Inc.

Notes to Consolidated Financial Statements December 31, 2008 and 2007

Note 12 - Off-balance-sheet Activities (Continued)

Collateral Requirements - To reduce credit risk related to the use of credit-related financial instruments, the Corporation might deem it necessary to obtain collateral. The amount and nature of the collateral obtained are based on the Corporation's credit evaluation of the customer. Collateral held varies but may include cash, securities, accounts receivable, inventory, property, plant, equipment, and real estate.

If the counterparty does not have the right and ability to redeem the collateral or the Corporation is permitted to sell or repledge the collateral on short notice, the Corporation records the collateral in its consolidated balance sheet at fair value with a corresponding obligation to return it.

Legal Contingencies - Various legal claims also arise from time to time in the normal course of business which, in the opinion of management, will have no material effect on the Corporation's consolidated financial statements.

Note 13 - Restrictions on Dividends, Loans, and Advances

Banking regulations place certain restrictions on dividends paid and loans or advances made by the Bank to the Corporation.

Prior approval of the Bank's federal regulator is required if the total dividends declared by the Bank in a calendar year exceed the sum of the net profits of the Bank for the preceding three years, less any required transfers to surplus. In addition, dividends paid by the Bank would be prohibited if the effect thereof would cause the Bank's capital to be reduced below applicable minimum standards. At December 31, 2008, the Bank's retained earnings available for the payment of dividends, without approval from the regulators, totaled \$1,284,000. Accordingly, \$18,030,514 of the Corporation's investment in the Bank was restricted at December 31, 2008.

Loans or advances made by the Bank to the Corporation are generally limited to 10 percent of the Bank's capital stock and surplus.

Huron Community Financial Services, Inc.

Notes to Consolidated Financial Statements December 31, 2008 and 2007

Note 14 - Minimum Regulatory Capital Requirements

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 possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Bank'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 capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the following table) of total and Tier I capital (as defined in the regulations) to risk-weighted assets (as defined) and of Tier I capital (as defined) to average assets (as defined). Management believes, as of December 31, 2008 and 2007, that the Bank met all capital adequacy requirements to which it is subject.

As of December 31, 2008, the most recent notification from the Bank's primary regulator categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, an institution must maintain minimum total risk-based, Tier I risk-based, and Tier I leverage ratios as set forth in the following tables. There are no conditions or events since the notification that management believes have changed the Bank's category. The Bank's actual capital amounts and ratios as of December 31, 2008 and 2007 are also presented in the table.

(000s omitted)	Actual		For Capital Adequacy Purposes		To be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2008						
Total capital to risk-weighted assets - Bank	\$ 20,626	14.5%	\$ 11,380	8.0%	\$ 14,225	10.0%
Tier I capital to risk-weighted assets - Bank	18,842	13.2	5,710	4.0	8,565	6.0
Tier I capital to average assets - Bank	18,842	10.1	7,462	4.0	9,328	5.0
As of December 31, 2007						
Total capital to risk-weighted assets - Bank	21,940	17.0	10,325	8.0	12,906	10.0
Tier I capital to risk-weighted assets - Bank	20,318	15.7	5,177	4.0	7,765	6.0
Tier I capital to average assets - Bank	20,318	11.1	7,322	4.0	9,152	5.0

Huron Community Financial Services, Inc.

Notes to Consolidated Financial Statements December 31, 2008 and 2007

Note 15 - Stock Option Plan

As of December 31, 2008, the Corporation has two share-based compensation plans which are described below. Options available for grant under the 1996 Nonemployee Director Stock Option Plan, the 1996 Employee Stock Option Plan, and the 1997 Nonemployee Director Discretionary Stock Option Plan have been issued. Some of the options issued under the 1996 and 1997 plans are exercisable by the participants until the end of the contractual terms.

The Corporation's 2005 Nonemployee Director Stock Option Plan and 2005 Employee Stock Option Plan (the "Plans"), which are stockholder approved, permit the grant of stock options for up to 15,000 and 35,000 shares of common stock, respectively. The Corporation believes that such awards better align the interests of its employees with those of its stockholders. Option awards are generally granted with an exercise price equal to the market price of the entity's stock at the date of grant; those option awards generally vest immediately for nonemployees and over three years for employees and have 10-year contractual terms. Certain option awards provide for accelerated vesting if there is a change in control (as defined in the Plans). The compensation cost that has been charged against income for the Plans was approximately \$11,000 and \$15,000 for 2008 and 2007, respectively.

The Corporation uses a Black Scholes formula to estimate the calculated value of its share-based payments. The volatility assumption used in the Black Scholes formula is based on the volatility of the Corporation's stock price and dividend payments throughout the year. The Corporation calculated the historical volatility of that using the monthly closing total stock price for the one year immediately prior.

The weighted average assumptions used in the Black Scholes model are noted in the following table. The Corporation uses historical data to estimate option exercise and employee termination within the valuation model. The risk-free rate for periods within the contractual life of the option is based on the U.S. Treasury yield curve in effect at the time of grant.

	2008	2007
Calculated volatility	15.99 %	10.15 %
Weighted average dividends	4.64 %	3.91 %
Expected term (in years)	8	8
Risk-free rate	2.28 %	4.50 %

Huron Community Financial Services, Inc.

Notes to Consolidated Financial Statements December 31, 2008 and 2007

Note 15 - Stock Option Plan (Continued)

A summary of option activity under the Plans for the years ended December 31, 2008 and 2007 is presented below:

	2008		2007	
	Number of Shares	Weighted Average Exercise Price	Number of Shares	Weighted Average Exercise Price
Options outstanding at beginning of year	77,989	\$ 33.81	84,951	\$ 30.80
Options granted	7,667	47.43	4,250	53.75
Options exercised	(11,150)	25.72	(11,212)	22.96
Options outstanding at end of year	74,506	36.43	77,989	33.81
Exercisable at year end	66,223	35.02	72,439	32.56

The weighted average grant date-calculated value of options granted during the years 2008 and 2007 was \$4 and \$5, respectively.

As of December 31, 2008, there was approximately \$15,000 of total unrecognized compensation cost related to nonvested share-based compensation arrangements granted under the Plans. That cost is expected to be recognized over a weighted average period of 2.5 years.

Note 16 - Fair Value Measurements

The following tables present information about the Corporation's assets measured at fair value on a recurring basis at December 31, 2008, and the valuation techniques used by the Corporation to determine those fair values.

In general, fair values determined by Level 1 inputs use quoted prices in active markets for identical assets or liabilities that the Corporation has the ability to access.

Fair values determined by Level 2 inputs use other inputs that are observable, either directly or indirectly. These Level 2 inputs include quoted prices for similar assets and liabilities in active markets, and other inputs such as interest rates and yield curves that are observable at commonly quoted intervals.

Level 3 inputs are unobservable inputs, including inputs that are available in situations where there is little, if any, market activity for the related asset or liability.

In instances where inputs used to measure fair value fall into different levels in the above fair value hierarchy, fair value measurements in their entirety are categorized based on the lowest level input that is significant to the valuation. The Corporation's assessment of the significance of particular inputs to these fair value measurements requires judgment and considers factors specific to each asset or liability.

Huron Community Financial Services, Inc.

Notes to Consolidated Financial Statements December 31, 2008 and 2007

Note 16 - Fair Value Measurements (Continued)

Assets Measured at Fair Value on a Recurring Basis at December 31, 2008 (dollars in thousands)

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at December 31, 2008
Assets - Investment securities - Available for sale	\$ 631	\$ 9,452	\$ -	\$ 10,083

The Corporation also has assets that under certain conditions are subject to measurement at fair value on a non-recurring basis. These assets include held-to-maturity investments and loans. The Corporation has estimated the fair values of these assets using Level 3 inputs, specifically discounted cash flow projections.

Assets Measured at Fair Value on a Nonrecurring Basis (dollars in thousands)

	Balance at December 31, 2008	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Losses for the Period Ended December 31, 2008
Assets - Impaired loans accounted for under FAS 114	\$ 1,166	\$ -	\$ -	\$ 1,166	\$ 370

Impaired loans accounted for under FAS 114 categorized as Level 3 assets consist of non-homogeneous loans that are considered impaired. The Corporation estimates the fair value of the loans based on the present value of expected future cash flows using management's best estimate of key assumptions. These assumptions include future payment ability, timing of payment streams, and estimated realizable values of available collateral (typically based on outside appraisals).

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Notes to Consolidated Financial Statements December 31, 2008 and 2007

Note 16 - Fair Value Measurements (Continued)

Other assets, including bank-owned life insurance, goodwill, intangible assets, and other assets acquired in business combinations, are also subject to periodic impairment assessments under other accounting principles generally accepted in the United States of America. These assets are not considered financial instruments. Effective February 12, 2008, the FASB issued a staff position, FSP FAS 157-2, which delayed the applicability of FAS 157 to non-financial instruments. Accordingly, these assets have been omitted from the above disclosures.