First Federal of Northern Michigan Bancorp, Inc.
Form 10-K
March 31, 2009

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

þ **Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
**For the Fiscal Year Ended December 31, 2008**

**OR**

o **Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
**For the transition period from _____ to _____**

**Commission File Number: 000-31957**

**FIRST FEDERAL OF NORTHERN MICHIGAN BANCORP, INC.**
(Exact name of registrant as specified in its charter)

| **Maryland** | **32-0135202** |
|---|---|
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification Number) |
| **100 S. Second Avenue, Alpena, Michigan** | **49707** |
| (Address of Principal Executive Offices) | Zip Code |

**(989) 356-9041**
(Registrant s telephone number)

**Securities Registered Pursuant to Section 12(b) of the Act:**

| **Common Stock, par value $.01 per share** | **The Nasdaq Stock Market LLC** |
|---|---|
| (Title of Class) | (Name of Exchange of 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 o. NO þ.

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 o. NO þ.

Indicate by check mark whether the registrant (1) filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the past twelve 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 þ. NO o.

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. þ.

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. (Check one):

Large accelerated filer o Accelerated filer o Smaller reporting company þ

Non-accelerated filer o

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined by Rule 12b-2 of the Exchange Act). YES o. NO þ.

The aggregate market value of the voting stock held by non-affiliates of the registrant, computed by reference to the last sale price on June 30, 2008 ($5.99 per share) was $15.3 million.

As of March 27, 2009, there were issued and outstanding 2,884,249 shares of the registrant s common stock.

**DOCUMENTS INCORPORATED BY REFERENCE**

1. Proxy Statement for the 2009 Annual Meeting of Stockholders (Parts I and III).
2. Annual Report to Shareholders for the Year Ended December 31, 2008 (Part II).

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# PART I

## ITEM 1. BUSINESS

### Forward-Looking Statements

This Annual Report contains certain forward-looking statements which may be identified by the use of words such as believe, expect, anticipate, should, planned, estimated and potential. Examples of forward-looking state include, but are not limited to, estimates with respect to our financial condition, results of operations and business that are subject to various factors which could cause actual results to differ materially from these estimates and most other statements that are not historical in nature. These factors include, but are not limited to, general and local economic conditions, changes in interest rates, deposit flows, demand for mortgage, commercial and other loans, real estate values, competition, changes in accounting principles, policies, or guidelines, changes in legislation or regulation, and other economic, competitive, governmental, regulatory, and technological factors affecting our operations, pricing products and services.

As used in this Form 10-K, unless we specify otherwise, we, us, our and similar terms refer to First Federal of Northern Michigan, the wholly owned savings bank subsidiary of First Federal of Northern Michigan Bancorp, Inc. as indicated by the context.

### First Federal of Northern Michigan Bancorp, Inc.

First Federal of Northern Michigan Bancorp, Inc. is a Maryland corporation that owns all of the outstanding shares of common stock of First Federal of Northern Michigan. At December 31, 2008, First Federal of Northern Michigan Bancorp, Inc. had consolidated assets of $247.7 million, deposits of $165.8 million and stockholders equity of $29.4 million. As of December 31, 2008, First Federal of Northern Michigan Bancorp, Inc. had 2,884,249 shares of common stock issued and outstanding. First Federal of Northern Michigan Bancorp, Inc. s executive offices are located at 100 South Second Avenue, Alpena, Michigan 49707. Its phone number at that address is (989) 356-9041.

### First Federal of Northern Michigan

First Federal of Northern Michigan is a full-service, community-oriented savings bank that provides financial services to individuals, families and businesses from eight full-service facilities located in Alpena, Cheboygan, Emmett, Iosco, Otsego, Montmorency and Oscoda Counties, Michigan. First Federal of Northern Michigan was chartered in 1957, and reorganized into the mutual holding company structure in 1994. In 2000, First Federal of Northern Michigan became the wholly owned subsidiary of Alpena Bancshares, Inc., our predecessor company, and in April 2005 we completed our second step mutual-to-stock conversion and formed our current ownership structure.

First Federal of Northern Michigan s business consists primarily of accepting deposits from the general public and investing those deposits, together with funds generated from operations and borrowings, in one- to four-family residential mortgage loans, commercial real estate loans, commercial business loans, consumer loans and in investment securities and mortgage-backed securities.

First Federal of Northern Michigan s executive offices are located at 100 South Second Avenue, Alpena, Michigan 49707. Its phone number at that address is (989) 356-9041.

### Market Area and Competition

First Federal of Northern Michigan conducts operations through its main office in Alpena, Michigan, which is located in the northeastern lower peninsula of Michigan, and through its seven other branch offices in Michigan. The population of Alpena (city and township), from which the majority of our deposits is drawn, has decreased 6.7% since 2000, and currently is approximately 20,000. The population of our primary market area, which includes Alpena County and seven surrounding counties, is approximately 184,000, and increased by less than 1.0% from 2000 to 2007. The population of our primary market area decreased by approximately 2,700 or 1.4% from 2006 to 2007. Per capita income in our market area was $28,551 in 2006, which was 22.2% less than the national level, and 15.5% less than the state of Michigan as a whole, reflecting the largely rural nature of our market area and the absence of more densely populated urban and suburban areas. Growth in per capita income in our market area is projected to increase only modestly over the next five years. The unemployment rate in our primary market area was 12.0% at December 31, 2008, compared to 7.2% nationally and 10.2% for the state of Michigan.

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Alpena is the largest city located in the northeastern lower peninsula of Michigan. This area has long been associated with agricultural, wood and concrete industries. Tourism has also been a major industry in our primary market area. All of these industries tend to be seasonal and are strongly affected by state and national economic conditions.

Major employers in our primary market area include various public schools and governmental agencies, Alpena Regional Medical Center, Besser Company (a manufacturer of concrete products equipment), Lafarge Corporation (a limestone mining and cement producer), Panel Processing (a peg board manufacturer), Treetops Sylvan Resort (an operator of resort properties), Garland Resort (an operator of resort properties and golf courses), Otsego Memorial Hospital, Community Memorial Hospital, Decorative Panels International (a hardboard manufacturer), OMNI Metalcraft Corp. (a diversified manufacturer), and various other small companies.

As of December 31, 2008, First Federal of Northern Michigan was the only thrift institution headquartered in our market area. We encounter strong competition both in attracting deposits and in originating real estate and other loans. Our most direct competition for deposits has historically come from commercial banks, other savings institutions, and credit unions in our market area. Competition for loans comes from such financial institutions as well as mortgage banking companies. We expect continued strong competition in the foreseeable future, including the super-regional banks currently in our markets, from internet banks, and from credit unions in many of our markets. We compete for savings deposits by offering depositors a high level of personal service and a wide range of competitively priced financial products. In recent years, additional strong competition for deposits has come from securities brokers. We compete for real estate loans primarily on the basis of the interest rates and fees we charge and through advertising. Strong competition for deposits and loans may limit our ability to grow and may adversely affect our profitability in the future.

**Lending Activities**

***General.*** The largest part of our loan portfolio is mortgage loans secured by one- to four-family residential real estate. In recent years, we have sold into the secondary mortgage market most of the fixed-rate conventional one- to four-family mortgage loans that we originate that have terms of 15 years or more. We retain the servicing on a majority of the mortgage loans that we sell. To a lesser extent, we also originate commercial loans, commercial real estate loans and consumer loans. At December 31, 2008, we had total loans of $198.2 million, of which $91.3 million, or 46.1%, were one- to four-family residential real estate mortgage loans, $43.8 million, or 22.0%, were commercial real estate loans, and $30.2 million, or 15.2%, were commercial loans. Other loans consisted primarily of home equity loans, which totaled $22.3 million, or 11.3% of total loans, construction loans which totaled $7.0 million or 3.6% of total loans, and other consumer loans which totaled $3.6 million, or 1.8% of total loans.

***One- to Four-Family Residential Real Estate Lending.*** Our primary lending activity consists of originating one- to four-family owner-occupied residential mortgage loans, virtually all of which are collateralized by properties located in our market area. We also originate one- to four-family loans that pay interest only during the initial construction period (which generally does not exceed twelve months) and then pay interest and principal for the remainder of the loan term. We generally sell into the secondary mortgage market most of our one- to four-family fixed-rate mortgage loans with terms of 15 years or more and retain the loan servicing on a majority of these mortgage loans. One- to four-family residential mortgage loans are underwritten and originated according to policies and guidelines established by the secondary mortgage market agencies and approved by our Board of Directors. We utilize existing liquidity, deposits, loan repayments, and Federal Home Loan Bank advances to fund new loan originations.

We currently offer fixed rate one- to four-family residential mortgage loans with terms ranging from 15 to 30 years. One- to four-family residential mortgage loans often remain outstanding for significantly shorter periods than their contractual terms because borrowers may refinance or prepay loans at their option. The average length of time that our one- to four-family residential mortgage loans remain outstanding varies significantly depending upon trends in market interest rates and other factors. In recent years, the average maturity of our mortgage loans has decreased significantly because of the declining trend in market interest rates and the unprecedented volume of refinancing activity resulting from such interest rate decreases. Accordingly, estimates of the average length of one- to four-family loans that remain outstanding cannot be made with any degree of certainty.

Originations of fixed rate mortgage loans are regularly monitored and are affected significantly by the level of market interest rates, our interest rate gap position, and loan products offered by our competitors. Our fixed rate mortgage loans amortize on a monthly basis with principal and interest due each month. To make our loan portfolio less interest rate sensitive, fixed-rate loans originated with terms of 15 years or greater are generally underwritten to secondary mortgage market standards and sold. Adjustable rate mortgage loans are generally underwritten to secondary mortgage market standards, but are retained in our loan portfolio.

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We have in the past originated some fixed-rate loans that are generally amortized over 15 years but that have balloon payments that are due upon the maturity of the loan in five years. As a general rule, we no longer originate this type of mortgage loans. Upon maturity, existing balloon mortgage loans are either underwritten as fixed-rate loans and sold in the secondary mortgage market or rewritten as adjustable rate mortgages at current market rates. While the majority of our balloon mortgage loans amortize over 15 years, some amortize over 10 or 30 years, and a limited number amortize over five years.

Our one- to four-family residential mortgage loans customarily include due-on-sale clauses, which are provisions giving us the right to declare a loan immediately due and payable in the event, among other things, that the borrower sells or otherwise disposes of the underlying real property serving as security for the loan. Due-on-sale clauses are an important means of adjusting the rates on our fixed-rate mortgage loan portfolio, and we have generally exercised our rights under these clauses.

Regulations limit the amount that a savings institution may lend relative to the appraised value of the real estate securing the loan, as determined by an appraisal at the time of loan origination. Such regulations permit a maximum loan-to-value ratio of 100% for residential property and 90% for all other real estate loans. Our lending policies limit the maximum loan-to-value ratio on fixed-rate loans without private mortgage insurance to 90% of the lesser of the appraised value or the purchase price of the property serving as collateral for the loan.

We make one- to four-family real estate loans with typical loan-to-value ratios of up to 90%. However, for one- to four-family real estate loans with loan-to-value ratios of between 80% and 90%, we may require the total loan amount to be covered by private mortgage insurance. In 2005 we began making 80/20 loans and interest-only loans subject to Board-approved dollar limits to limit risk exposure. In late 2007 these products were eliminated. We require fire and casualty insurance, flood insurance when applicable, as well as title insurance, on all properties securing real estate loans made by us.

***Commercial Real Estate Lending.*** We also originate commercial real estate loans. At December 31, 2008, we had a total of 180 loans secured primarily by commercial real estate properties, unimproved vacant land and, to a limited extent, multifamily properties. Our commercial real estate loans are secured by income-producing properties such as office buildings, retail buildings, restaurants and car washes. Substantially all of our commercial real estate loans are secured by properties located in our primary market area. We have originated commercial construction loans that are originated as permanent loans but are interest-only during the initial construction period, which generally does not exceed nine months. At December 31, 2008, our commercial real estate loans totaled $49.8 million, or 25.1% of our total loans, and had an average principal balance of approximately $243,000. The terms of each loan are negotiated on a case-by-case basis, although such loans typically amortize over 15 years and have a three- or five-year balloon feature. An origination fee of 0.5% to 1.0% is generally charged on commercial real estate loans. We generally make commercial real estate loans up to 75% of the appraised value of the property securing the loan. At December 31, 2008, our largest commercial real estate relationship consisted of two loans having a total principal balance of $5.5 million, of which $1.4 million has been charged off. These loans were secured by two commercial buildings and all corporate assets of the borrower. At December 31, 2008, these loans were in non-accrual status due to insufficient cash flows to meet future payment obligations.

Commercial real estate loans generally carry higher interest rates and have shorter terms than those on one- to four-family residential mortgage loans. However, loans secured by commercial real estate generally involve a greater degree of credit risk than one- to four-family residential mortgage loans and carry larger loan balances. This increased credit risk is a result of several factors, including the concentration of principal in a limited number of loans and borrowers, the effects of general economic conditions on income producing properties, and the increased difficulty of evaluating and monitoring these types of loans. Furthermore, the repayment of loans secured by commercial real estate is typically dependent upon the successful operation of the business or the related real estate property. If the cash flow from the business operation is reduced, the borrower s ability to repay the loan may be impaired. This may be particularly true in the early years of the business operation when the risk of failure is greatest. Some of our commercial real estate loans have been made to borrowers whose business operations are untested, which increases our risk.

***Consumer and Other Loans.*** We originate a variety of consumer and other loans, including loans secured by savings accounts, new and used automobiles, mobile homes, boats, recreational vehicles, and other personal property. As of December 31, 2008, consumer and other loans totaled $25.9 million, or 13.1% of our total loan portfolio. At such date, $597,000, or 0.2% of our consumer loans, were unsecured. As of December 31, 2008, home equity loans totaled $8.7 million, or 4.4% of our total loan portfolio, and automobile loans totaled $2.4 million, or 1.2% of our total loan portfolio. We originate automobile loans directly to our customers and have no outstanding agreements with automobile dealerships to generate indirect loans.

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Our procedures for underwriting consumer loans include an assessment of an applicant s credit history and the ability to meet existing obligations and payments on the proposed loan. Although an applicant s creditworthiness is a primary consideration, the underwriting process also includes a comparison of the value of the collateral security, if any, to the proposed loan amount.

Consumer loans generally entail greater risk than residential mortgage loans, particularly in the case of consumer loans that are unsecured or secured by assets that tend to depreciate rapidly, such as automobiles, mobile homes, boats and recreational vehicles. In addition, the repayment of consumer loans depends on the borrower s continued financial stability, as repayment is more likely to be adversely affected by job loss, divorce, illness or personal bankruptcy than a single family mortgage loan.

***Commercial Loans.*** At December 31, 2008, we had $30.2 million in commercial loans which amounted to 15.2% of total loans. We make commercial business loans primarily in our market area to a variety of professionals, sole proprietorships and small businesses. Commercial lending products include term loans and revolving lines of credit. The maximum amount of a commercial business loan is our loans-to-one-borrower limit, which was $4.6 million at December 31, 2008. Such loans are generally used for longer-term working capital purposes such as purchasing equipment or furniture. Commercial loans are made with either adjustable or fixed rates of interest. Variable rates are generally based on the prime rate, as published in *The Wall Street Journal,* plus a margin. Fixed rate commercial loans are set at a margin above the Federal Home Loan Bank comparable advance rate.

When making commercial loans, we consider the financial statements of the borrower, our lending history with the borrower, the debt service capabilities of the borrower, the projected cash flows of the business and the value of the collateral. Commercial loans are generally secured by a variety of collateral, primarily accounts receivable, inventory and equipment, and are supported by personal guarantees. Depending on the collateral used to secure the loans, commercial loans are typically made in amounts of up to 75% of the value of the collateral securing the loan.

Commercial loans generally have greater credit risk than residential mortgage loans. Unlike residential mortgage loans, which generally are made on the basis of the borrower s ability to make repayment from his or her employment or other income, and which are secured by real property whose value tends to be more easily ascertainable, commercial loans generally are made on the basis of the borrower s ability to repay the loan from the cash flow of the borrower s business. As a result, the availability of funds for the repayment of commercial loans may depend substantially on the success of the business itself. If the cash flow from the business operation is reduced, the borrower s ability to repay the loan may be impaired. This may be particularly true in the early years of the business operation when the risk of failure is greatest. Some of our commercial loans have been made to borrowers whose business operations are untested, which increases our risk. Moreover, any collateral securing the loans may depreciate over time, may be difficult to appraise and may fluctuate in value. We seek to minimize these risks through our underwriting standards. At December 31, 2008, our largest commercial loan was a $2.4 million commercial construction participation loan for the construction of a manufacturing plant and purchase of related equipment. At December 31, 2008 the outstanding balance was $2.1 million and the loan was performing according to its repayment terms.

***Construction Loans.*** We originate construction loans to local home builders in our market area, generally with whom we have an established relationship, and to individuals engaged in the construction of their residence. We also originate loans for the construction of commercial buildings. Our construction loans totaled 7.0 million, or 3.6% of our total loan portfolio, at December 31, 2008.

Our construction loans to home builders are repaid on an interest-only basis for the term of the loan (which is generally six to 12 months), with interest calculated on the amount disbursed to the builders based upon a percentage of completion of construction. These loans typically have a maximum loan-to-value ratio of 80%, based on the appraised value. Interest rates are fixed during the construction phase of the loan. Loans to builders are made on either a pre-sold or, to a lesser extent, on a speculative (unsold) basis. Most of our construction loans to individuals who intend to occupy the completed dwelling are originated via a one-step closing process, whereby the construction phase and end-financing are handled with one loan closing. Prior to funding a construction loan, we require an appraisal of the property from a qualified appraiser approved by us, and all appraisals are reviewed by us.

Construction lending exposes us to greater credit risk than permanent mortgage financing because of the inherent difficulty in estimating both a property s value at completion of the project and the estimated cost of the project. If the estimate of construction costs is inaccurate, we may be required to advance funds beyond the amount originally committed to permit completion of the project. If the estimate of value upon completion is inaccurate, the value of the

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property may be insufficient to assure full repayment. Projects also may be jeopardized by disagreements between borrowers and builders and by the failure of builders to pay subcontractors. Loans to builders to construct homes for which no purchaser has been identified carry more risk because the repayment of the loan depends on the builder s ability to sell the property prior to the time that the construction loan is due. We have attempted to minimize these risks by, among other things, limiting our construction lending primarily to residential properties in our market area and generally requiring personal guarantees from the principals of corporate borrowers.

***Loan Portfolio Composition.*** The following table sets forth the composition of our loan portfolio by type of loan at the dates indicated.

| | At December 31, | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | 2008 | | 2007 | | 2006 | | 2005 | | 2004 | |
| | Amount | Percent | Amount | Percent | Amount | Percent | Amount | Percent | Amount | Percent |
| | (Dollars in thousands) | | | | | | | | | |
| Real estate loans: | | | | | | | | | | |
| Residential mortgage | $ 91,339 | 46.1% | $ 97,266 | 47.3% | $ 99,490 | 46.9% | $ 100,042 | 49.3% | $ 102,600 | 52.1% |
| Commercial mortgage | 43,774 | 22.0% | 44,634 | 21.7% | 45,274 | 21.4% | 40,270 | 19.8% | 29,690 | 15.1% |
| Construction | 7,038 | 3.6% | 8,292 | 4.0% | 9,406 | 4.4% | 10,030 | 4.9% | 8,906 | 4.5% |
| Home Equity/Junior Liens | 22,303 | 11.3% | 24,095 | 11.7% | 24,868 | 11.7% | 21,238 | 10.5% | 19,927 | 10.1% |
| Non real estate loans | | | | | | | | | | |
| Commercial | 30,173 | 15.2% | 26,783 | 13.0% | 28,209 | 13.3% | 26,658 | 13.1% | 30,174 | 15.3% |
| Consumer and other loans | 3,564 | 1.8% | 4,555 | 2.3% | 4,688 | 2.3% | 4,669 | 2.4% | 5,617 | 2.9% |
| Total Loans | $ 198,191 | 100.0% | $ 205,625 | 100.0% | $ 211,935 | 100.0% | $ 202,907 | 100.0% | $ 196,914 | 100.0% |
| Other items: | | | | | | | | | | |
| Deferred loan origination costs | 13 | | 13 | | 20 | | 28 | | 37 | |
| Deferred loan origination fees | (287) | | (292) | | (358) | | (336) | | (349) | |
| Allowance for loan losses | (5,647) | | (4,013) | | (2,079) | | (1,416) | | (1,214) | |
| Total loans, net | $ 192,270 | | $ 201,333 | | $ 209,518 | | $ 201,183 | | $ 195,388 | |

***Loan Portfolio Maturities and Yield.*** The following table summarizes the scheduled repayments of our loan portfolio at December 31, 2008. Demand loans, loans having no stated repayment or maturity, and overdraft loans are reported as being due in one year or less.

| | Residential Mortgage | | Commercial Mortgage | | Construction | | HomeEquity/Junior Liens | |
|---|---|---|---|---|---|---|---|---|
| | Amount | Weighted Average Rate | Amount | Weighted Average Rate | Amount | Weighted Average Rate | Amount | Weighted Average Rate |
| | (Dollars in thousands) | | | | | | | |
| Due During the Years Ending December 31, | | | | | | | | |
| 2009 | $ 3,558 | 5.13% | $ 6,038 | 6.01% | $ 6,524 | 5.33% | $ 95 | 6.32% |
| 2010 | 1,158 | 7.05% | 9,240 | 6.81% | | 0.00% | 245 | 7.05% |
| 2011 | 457 | 7.73% | 9,358 | 6.98% | 514 | 3.93% | 1,989 | 5.14% |
| 2012 to 2013 | 2,792 | 6.50% | 16,228 | 7.13% | | 0.00% | 2,441 | 5.95% |
| 2014 to 2018 | 9,030 | 6.12% | 1,935 | 7.21% | | 0.00% | 5,819 | 6.60% |
| 2019 to 2023 | 8,577 | 6.59% | 94 | 6.00% | | 0.00% | 8,993 | 5.27% |
| 2023 and beyond | 65,767 | 6.40% | 881 | 7.25% | | 0.00% | 2,721 | 4.62% |
| Total | $ 91,339 | 6.36% | $ 43,774 | 6.81% | $ 7,038 | 5.25% | $ 22,303 | 5.75% |

| | Commercial | | Consumer and Other | | Total | |
|---|---|---|---|---|---|---|
| | Amount | Weighted Average Rate | Amount | Weighted Average Rate | Amount | Weighted Average Rate |
| Due During the Years Ending December 31, | | | | | | |
| 2009 | $ 15,371 | 4.41% | $ 465 | 8.66% | $ 32,051 | 5.64% |
| 2010 | 4,176 | 4.31% | 301 | 8.72% | 15,120 | 6.34% |
| 2011 | 4,057 | 6.11% | 458 | 8.23% | 16,833 | 6.57% |
| 2012 to 2013 | 2,446 | 6.85% | 655 | 7.60% | 24,562 | 6.63% |
| 2014 to 2018 | 2,595 | 6.31% | 1,303 | 8.70% | 20,682 | 6.62% |
| 2019 to 2023 | | 0.00% | 382 | 8.12% | 18,046 | 5.63% |
| 2023 and beyond | 1,528 | 5.16% | | 0.00% | 70,897 | 6.14% |
| Total | $ 30,173 | 4.75% | $ 3,564 | 8.58% | $ 198,191 | 6.37% |

***Fixed- and Adjustable-Rate Loans.*** The following table sets forth the scheduled repayments of fixed- and adjustable-rate loans at December 31, 2008 that are contractually due after December 31, 2009.

| | Due After December 31, 2009 | | |
|---|---|---|---|
| | Fixed | Adjustable | Total |
| | (In thousands) | | |
| Residential mortgage | $ 41,362 | $ 46,419 | $ 87,781 |
| Commercial mortgage | 35,674 | 2,062 | $ 37,736 |

| | | | |
|---|---|---|---|
| Construction | 514 | | $ 514 |
| Home Equity/Junior Liens | 13,494 | 8,714 | $ 22,208 |
| Commercial | 7,371 | 7,431 | $ 14,802 |
| Consumer and other | 2,668 | 431 | $ 3,099 |
| Total loans | $ 101,083 | $ 65,057 | $ 166,140 |

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***Loan Originations, Purchases, Sales and Servicing.*** While we originate both fixed-rate and adjustable-rate loans, our ability to generate each type of loan depends upon borrower demand, market interest rates, borrower preference for fixed- versus adjustable-rate loans, and the interest rates offered on each type of loan by other lenders in our market area. These lenders include competing banks, savings banks, credit unions, internet lenders, mortgage banking companies and life insurance companies that may also actively compete for local commercial real estate loans. Loan originations are derived from a number of sources, including real estate agent referrals, existing customers, borrowers, builders, attorneys, our directors and walk-in customers. Upon receiving a loan application, we obtain a credit report and employment verification to verify specific information relating to the applicant s employment, income, and credit standing. In the case of a real estate loan, we obtain a determination of value of the real estate intended to collateralize the proposed loan. Our residential mortgage lending limits vary by residential mortgage officer but range from $150,000 to $250,000. While certain Senior Bank Officers have residential lending limits up to $400,000 the Officer Loan Committee generally approves residential loans from $250,000 to $400,000 while requests from $400,000 to $500,000 will receive approval from Senior Loan Committee. Residential loan requests over $500,000 must be approved by the Board of Directors. Secured consumer lending limits by officer range from $25,000 to $150,000. For secured commercial loans, the limits range from $75,000 to $400,000.

A commercial commitment letter specifies the terms and conditions of the proposed loan including the amount of the loan, interest rate, amortization term, a brief description of the required collateral, and required insurance coverage. Commitments are typically issued for 15-day periods. The borrower must provide proof of fire and casualty insurance on the property serving as collateral, which must be maintained during the full term of the loan. A title insurance policy is required on all real estate loans. At December 31, 2008, we had outstanding loan commitments of $32.1 million, including unfunded commitments under lines of credit and commercial and standby letters of credit.

Our loan origination and sales activity may be adversely affected by a rising interest rate environment that typically results in decreased loan demand, while declining interest rates may stimulate increased loan demand. Accordingly, the volume of loan originations, the mix of fixed- and adjustable-rate loans, and the profitability of this activity can vary from period to period. One- to four-family residential mortgage loans are generally underwritten to investor guidelines, and closed on standard investor documents. We currently sell to Freddie Mac and Taylor, Bean & Whitaker. If such loans are sold, the sales are conducted using standard investor purchase contracts and master commitments as applicable. The majority of one- to four-family mortgage loans that we have sold to investors have been sold on a non-recourse basis, whereby foreclosure losses are generally the responsibility of the purchaser and not First Federal of Northern Michigan.

We are a qualified loan servicer for Freddie Mac. Our policy has historically been to retain the servicing rights for all conforming loans sold, and to continue to collect payments on the loans, maintain tax escrows and applicable fire and flood insurance coverage, and supervise foreclosure proceedings if necessary. We retain a portion of the interest paid by the borrower on the loans as consideration for our servicing activities. We have recently begun to sell loans to Taylor, Bean & Whitaker on a servicing-released basis to be able to offer additional product choices to our customers.

We require appraisals of real property securing loans. Appraisals are performed by independent appraisers, who are approved by our Board of Directors annually. We require fire and extended coverage insurance in amounts adequate to protect our principal balance. Where appropriate, flood insurance is also required. Private mortgage insurance is required for most residential mortgage loans with loan-to-value ratios greater than 80%.

***Loan Origination Fees and Costs.*** In addition to interest earned on loans, we generally receive fees in connection with loan originations. Such loan origination fees, net of costs to originate, are deferred and amortized using an interest method over the contractual life of the loan. Fees deferred are recognized into income immediately upon prepayment or subsequent sale of the related loan. At December 31, 2008, we had $274,000 of net deferred loan origination fees. Such fees vary with the volume and type of loans and commitments made and purchased, principal repayments, and competitive conditions in the mortgage markets, which in turn respond to the demand and availability of money. In addition to loan origination fees, we also generate other income through the sales and servicing of mortgage loans, late charges on loans, and fees and charges related to deposit accounts. We recognized fees and service charges of $942,000, $911,000 and $1,044,000 for the years ended December 31, 2008, 2007 and 2006, respectively.

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To the extent that originated loans are sold with servicing retained, we capitalize a mortgage servicing asset at the time of the sale in accordance with applicable accounting standards (Statement of Financial Accounting Standards No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities ). The capitalized amount is amortized thereafter (over the period of estimated net servicing income) as a reduction of servicing fee income. The unamortized amount is fully charged to income when loans are prepaid. Originated mortgage servicing rights with an amortized cost of $430,000 were included in other assets at December 31, 2008.

***Origination, Purchase and Sale of Loans***. The table below shows our loan originations, purchases, sales, and repayments of loans for the periods indicated. In 2008, we purchased $5.2 million in commercial real estate loan participations.

| | Years Ended December 31, | | |
|---|---|---|---|
| | **2008** | **2007** | **2006** |
| | | (In Thousands) | |
| Loans receivable at beginning of period | $ 205,625 | $ 211,935 | $ 202,907 |
| Originations: | | | |
| Real estate: | | | |
| Residential 1-4 family | 30,187 | 31,496 | 33,371 |
| Commercial and Multi-family | 24,191 | 21,644 | 23,760 |
| Consumer | 6,543 | 9,035 | 15,992 |
| Total originations | 60,921 | 62,175 | 73,123 |
| Loan purchases | 5,177 | 11,125 | 4,625 |
| Loan sales | (11,641) | (16,287) | (14,632) |
| Transfer of mortgage loans to foreclosed real estate | (8,251) | (1,719) | (703) |
| Repayments | (53,640) | (61,604) | (53,385) |
| Total loans receivable at end of period | $ 198,191 | $ 205,625 | $ 211,935 |

**Delinquent Loans, Other Real Estate Owned and Classified Assets**

***Collection Procedures.*** Our general collection procedures provide that when a mortgage, consumer or commercial loan becomes 10 days past due, a computer-generated late charge notice is sent to the borrower requesting payment. If delinquency continues, a second delinquent notice is mailed when the loan continues past due for 30 days. If a loan becomes 60 days past due, the loan becomes subject to possible legal action. We will generally send a due and payable letter upon a loan becoming 60 days delinquent. This letter grants the mortgagor 30 days to bring the account paid to date prior to the start of any legal action. If not paid, foreclosure proceedings are initiated after this 30-day period. To the extent required by regulations of the Department of Housing and Urban Development ( HUD ), generally within 30 days of delinquency, a Section 160 HUD notice is given to the borrower which provides access to consumer counseling services. General collection procedures may vary with particular circumstances on a loan by loan basis. Also, collection procedures for Freddie Mac serviced loans follow the Freddie Mac guidelines which are different from our general procedures.

***Loans Past Due and Non-Performing Assets.*** Loans are reviewed on a regular basis and are placed on non-accrual status when, in the opinion of management, the collection of additional interest is doubtful or when extraordinary efforts are required to collect the debt. Interest accrued and unpaid at the time a loan is placed on non-accrual status is charged against interest income.

Real estate acquired by us as a result of foreclosure or by deed in lieu of foreclosure is deemed real estate owned ( REO ) until such time as it is sold. In general, we consider collateral for a loan to be in-substance foreclosed if: (i) the borrower has little or no equity in the collateral; (ii) proceeds for repayment of the loan can be expected to come only from the operation or sale of the collateral; and (iii) the borrower has either formally or effectively abandoned control of the collateral, or retained control of the collateral but is unlikely to be able to rebuild equity in the collateral or otherwise repay the loan in the foreseeable future. Cash flow attributable to in-substance foreclosures is used to reduce the carrying value of the collateral.

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When collateral, other than real estate, securing commercial and consumer loans is acquired as a result of delinquency or other reasons, it is classified as Other Repossessed Assets ( ORA ) and recorded at the lower of cost or fair market value until it is disposed of.

When collateral is acquired or otherwise deemed REO/ORA, it is recorded at the lower of the unpaid principal balance of the related loan or its estimated net realizable value. This write down is recorded against the allowance for loan losses. Periodic future valuations are performed by management, and any subsequent decline in fair value is charged to operations. At December 31, 2008, we held $1.6 million in properties that were classified REO and $70,000 in assets classified as ORA.

***Delinquent Loans.*** The following table sets forth certain information with respect to our loan portfolio delinquencies at the dates indicated.

| | Loan Delinquent For | | | | | |
|---|---|---|---|---|---|---|
| | 60-89 Days | | 90 Days and Over | | Total | |
| | Number | Amount | Number | Amount | Number | Amount |
| | ( Dollars In Thousands) | | | | | |
| At December 31, 2008 | | | | | | |
| Residential Mortgages | 26 | 2,513 | 2 | 128 | 28 | 2,641 |
| Commercial Mortgages | 5 | 736 | | | 5 | 736 |
| Construction | | | | | | |
| Commercial | | | 1 | 72 | 1 | 72 |
| Consumer | 26 | 155 | 8 | 17 | 34 | 172 |
| Total | 57 | $ 3,404 | 11 | $ 217 | 68 | 3,621 |
| At December 31, 2007 | | | | | | |
| Residential Mortgages | 24 | 1,315 | 6 | 532 | 30 | 1,847 |
| Commercial Mortgages | 1 | 797 | | | 1 | 797 |
| Construction | | | | | | |
| Commercial | | | 1 | 100 | 1 | 100 |
| Consumer | 19 | 181 | 10 | 45 | 29 | 226 |
| Total | 44 | $ 2,293 | 17 | $ 677 | 61 | 2,969 |
| At December 31, 2006 | | | | | | |
| Residential Mortgages | 22 | 1,218 | 9 | 645 | 31 | 1,863 |
| Commercial Mortgages | 1 | 636 | 2 | 221 | 3 | 857 |
| Construction | 1 | 74 | | | 1 | 74 |
| Commercial | 6 | 317 | 10 | 540 | 16 | 857 |
| Consumer | 17 | 105 | 9 | 84 | 26 | 189 |
| Total | 47 | $ 2,350 | 30 | $ 1,490 | 77 | 3,839 |
| At December 31, 2005 | | | | | | |
| Residential Mortgages | 24 | 1,375 | 19 | 1,684 | 43 | 3,059 |
| Commercial Mortgages | | | 4 | 670 | 4 | 670 |
| Construction | 1 | 341 | | | 1 | 341 |
| Commercial | 8 | 506 | 2 | 115 | 10 | 621 |
| Consumer | 23 | 197 | 13 | 185 | 36 | 382 |

| | | | | | | |
|---|---|---|---|---|---|---|
| Total | 56 | $ 2,419 | 38 | $ 2,654 | 94 | 5,073 |
| | | | | | | |
| At December 31, 2004 | | | | | | |
| Residential Mortgages | 6 | $ 1,045 | 16 | $ 960 | 22 | $ 2,005 |
| Commercial Mortgages | | | | | | |
| Construction | | | | | | |
| Commercial | 2 | 195 | 1 | 105 | 3 | 300 |
| Consumer | 5 | 179 | 16 | 175 | 21 | 354 |
| | | | | | | |
| Total | 13 | $ 1,419 | 33 | $ 1,240 | 46 | $ 2,659 |

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***Nonperforming Assets.*** The following table sets forth the amounts and categories of our non-performing assets at the dates indicated.

| | At December 31, | | | | |
|---|---|---|---|---|---|
| | **2008** | **2007** | **2006** | **2005** | **2004** |
| | (Dollars in thousands) | | | | |
| Non-Accrual Loans delinquent 90 days or more: | | | | | |
| Residential Mortgage | 1,876 | 697 | 670 | 308 | 21 |
| Commercial Mortgage | 4,002 | 3,825 | 1,395 | 1,006 | 442 |
| Construction | 3,469 | 3,475 | | | |
| Commercial | 2,515 | 433 | 364 | | |
| Consumer and other | 90 | 29 | 61 | 39 | 15 |
| Total non-accrual loans delinquent 90 days or more | $ 11,952 | $ 8,459 | $ 2,490 | $ 1,353 | $ 478 |
| Accrual loans delinquent 90 days or more: | | | | | |
| Residential Mortgage | 128 | 532 | 645 | 1,684 | 960 |
| Commercial Mortgage | 72 | | 221 | 670 | |
| Construction | | | | | |
| Commercial | | 100 | 540 | 115 | 105 |
| Consumer and other | 17 | 45 | 84 | 185 | 175 |
| Total accrual loans delinquent 90 days or more | $ 217 | $ 677 | $ 1,490 | $ 2,654 | $ 1,240 |
| Total nonperforming loans (1) | $ 12,169 | $ 9,136 | $ 3,980 | $ 4,007 | $ 1,718 |
| Real Estate Owned and Other Repossessed Assets: | | | | | |
| Residential Mortgage | 686 | 872 | 437 | 427 | 9 |
| Commercial Mortgage | 882 | 406 | | | |
| Construction | | | | | |
| Commercial | | | | | |
| Consumer and other | 70 | 2 | 38 | 8 | 20 |
| Total real estate owned and other repossesed assets (2) | $ 1,638 | $ 1,280 | $ 475 | $ 435 | $ 29 |
| Total nonperforming assets | $ 13,807 | $ 10,416 | $ 4,455 | $ 4,442 | $ 1,747 |

| | | | | | |
|---|---|---|---|---|---|
| Total nonperforming loans to net loans receivable | 6.14% | 4.54% | 1.90% | 1.97% | 0.87% |
| Total nonperforming assets to total assets | 5.57% | 4.15% | 1.59% | 1.57% | 0.66% |

***Classification of Assets.*** Our policies, consistent with regulatory guidelines, provide for the classification of loans and other assets such as debt and equity securities and real estate held for sale considered by the Office of Thrift Supervision to be of lesser quality as substandard, doubtful, or loss assets. An asset is considered substandard if it i inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any.

Substandard assets include those characterized by the distinct possibility that the savings institution will sustain some loss if the deficiencies are not corrected. Assets classified as doubtful have all of the weaknesses inherent in those classified substandard, with the added characteristic that the weaknesses present make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable. Assets classified as loss are those considered uncollectible and of such little value that their continuance as assets without

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the establishment of a specific loss reserve is not warranted. Assets that do not expose the savings institution to risk sufficient to warrant classification in one of the aforementioned categories, but which possess some weaknesses, are required to be designated special mention by management. Loans designated as special mention are generally loans that, while current in required payments, have exhibited some potential weaknesses that, if not corrected, could increase the level of risk in the future.

When we classify assets as either substandard or doubtful, we allocate a portion of the related general loss allowances to such assets as deemed prudent by management. The allowance for loan losses represents amounts that have been established to recognize losses inherent in the loan portfolio that are both probable and reasonably estimable at the date of the financial statements. When we classify problem assets as loss, we charge-off such amount. Our determination as to the classification of our assets and the amount of our loss allowances are subject to review by our regulatory agencies, which can order the establishment of additional loss allowances. Management regularly reviews our asset portfolio to determine whether any assets require classification in accordance with applicable regulations. On the basis of management s review of our assets at December 31, 2008, classified assets consisted of substandard assets of $17.7 million. There were no assets classified as doubtful or loss at December 31, 2008.

We classify our assets pursuant to criteria similar to the classification structure provided in the OTS regulations. The following table sets forth the aggregate amount of our internally classified assets at the dates indicated.

| | At December 31, | | |
|---|---|---|---|
| | 2008 | 2007 | 2006 |
| | (In Thousands) | | |
| Substandard assets | $ 19,409 | $ 14,362 | $ 14,027 |
| Doubtful assets | | | 244 |
| Loss assets | | | |
| Total classified assets | $ 19,409 | $ 14,362 | $ 14,271 |

Our investment in land and real estate at December 31, 2008 was classified as substandard by the Office of Thrift Supervision due to slower than expected sales of building lots and condominium units. This project (Wyndham Garden Estates) is an upscale condominium community comprised of 25 single-family building lots and 18 planned condominium units located in Alpena, Michigan. At December 31, 2008, all but five of the residential lots had been developed and sold and all condominium units were sold. Although sales of the remaining lots have been slow, Management believes this is a still a viable project in a desirable location. At December 31, 2008, our investment in these properties was approximately $73,000, which is net of an allowance of $128,000 to record the investment at the lower of cost or fair value, less cost to sell. For reporting purposes, this investment is considered impaired under the definition of SFAS 144, *Accounting for Impairment or Disposal of Long-Lived Assets*.

***Allowance for Loan Losses.*** We provide for loan losses based on the allowance method. Accordingly, all loan losses are charged to the related allowance and all recoveries are credited to it. Additions to the allowance for loan losses are provided by charges to income based on various factors which, in management s judgment, deserve current recognition in estimating probable losses. Management regularly reviews the loan portfolio and makes provisions for loan losses in order to maintain the allowance for loan losses in accordance with accounting principles generally accepted in the United States of America. The allowance for loan losses consists of amounts specifically allocated to non-performing loans and other criticized or classified loans (if any) as well as general allowances determined for each major loan category. Commercial loans and loans secured by commercial real estate are evaluated individually for impairment. Other smaller-balance, homogeneous loan types, including loans secured by one- to four-family residential real estate and consumer installment loans, are evaluated for impairment on a collective basis. After we establish a provision for loans that are known to be non-performing, criticized or classified, we calculate percentage loss factors to apply to the remaining categories within the loan portfolio to estimate probable losses inherent in these categories of the portfolio. When the loan portfolio increases, therefore, the percentage calculation results in a higher dollar amount of estimated probable losses than would be the case without the increase, and when the loan portfolio

decreases, the percentage calculation results in a lower dollar amount of estimated probable losses than would be the case without the decrease. These percentage loss factors are determined by management based on our historical loss experience and credit concentrations for the applicable loan category, which may be adjusted to reflect our evaluation of levels of, and trends in, delinquent and non-accrual loans, trends in volume and terms of loans, and local economic trends and conditions.

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We consider commercial and commercial real estate loans and construction loans to be riskier than one- to four-family residential mortgage loans. Commercial and commercial real estate loans have greater credit risks compared to one- to four-family residential mortgage loans, as they typically involve large loan balances concentrated with single borrowers or groups of related borrowers. In addition, the payment experience on loans secured by income-producing properties typically depends on the successful operation of the related real estate project and thus may be subject to a greater extent to adverse conditions in the real estate market and in the general economy. Construction loans have greater credit risk than permanent mortgage financing because of the inherent difficulty in estimating both a property s value at completion of the project and the estimated cost of the project. If the estimate of construction costs is inaccurate, we may be required to advance funds beyond the amount originally committed to permit completion of the project. If the estimate of value upon completion is inaccurate, the value of the property may be insufficient to assure full repayment. Projects also may be jeopardized by disagreements between borrowers and builders and by the failure of builders to pay subcontractors. Loans to builders to construct homes for which no purchaser has been identified carry more risk because the repayment of the loan depends on the builder s ability to sell the property prior to the time that the construction loan is due. The increased risk characteristics associated with commercial real estate and land loans and construction loans are considered by management in the evaluation of the allowance for loan losses and generally result in a larger loss factor applied to these segments of the loan portfolio in developing an estimate of the required allowance for loan losses. We intend to increase our originations of commercial and commercial real estate loans, and we intend to retain these loans in our portfolio. Because these loans entail significant additional credit risks compared to one- to four-family residential mortgage loans, an increase in our origination (and retention in our portfolio) of these types of loans would, in the absence of other offsetting factors, require us to make additional provisions for loan losses.

The carrying value of loans is periodically evaluated and the allowance is adjusted accordingly. While management uses the best information available to make evaluations, future adjustments to the allowance may be necessary if conditions differ substantially from the information used in making the evaluations. In addition, as an integral part of their examination process, our regulatory agencies periodically review the allowance for loan losses. Such agencies may require us to recognize additions to the allowance based on their judgments of information available to them at the time of their examination.

***Analysis of the Allowance for Loan Losses***. The following table sets forth the activity on our allowance for loan losses for the periods indicated.

| | For the Years Ended December 31, | | | | |
|---|---|---|---|---|---|
| | 2008 | 2007 | 2006 | 2005 | 2004 |
| | (Dollars in thousands) | | | | |
| Allowance at beginning of period | $ 4,013 | $ 2,079 | $ 1,416 | $ 1,214 | $ 1,036 |
| Charge-offs: | | | | | |
| Residential Mortgages | 342 | 225 | 44 | 21 | 12 |
| Commercial Mortgages | 2,023 | 59 | | | |
| Commercial | 331 | 4 | 1 | 57 | |
| Consumer and other | 141 | 190 | 163 | 171 | 179 |
| Total charge offs | 2,837 | 478 | 208 | 249 | 191 |
| Recoveries: | | | | | |
| Residential Mortgages | | 1 | | | 1 |
| Consumer and other | 50 | 34 | 20 | 83 | 45 |
| Total recoveries | 50 | 35 | 20 | 83 | 46 |

| | | | | | |
|---|---|---|---|---|---|
| Net charge offs (recoveries) | 2,787 | 443 | 188 | 166 | 145 |
| Provision for loan losses | 4,421 | 2,377 | 851 | 368 | 323 |
| Balance at end of year | $ 5,647 | $ 4,013 | $ 2,079 | $ 1,416 | $ 1,214 |
| Ratios: | | | | | |
| Net Charge-offs to average loans outstanding (annualized) | 1.40% | 0.21% | 0.08% | 0.08% | 0.07% |
| Allowance for loan loss to non-performing loans at end of period | 46.41% | 43.93% | 22.76% | 35.34% | 70.67% |
| Allowance for loan losses to total loans at end of period | 2.85% | 1.95% | 0.98% | 0.70% | 0.62% |

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***Allocation of Allowance for Loan Losses.*** The following table sets forth the allowance for loan losses allocated by loan category, the total loan balances by category , and the percent of loans in each category to total loans at the dates indicated. The allowance for loan losses allocated to each category is not necessarily indicative of future losses in any particular category and does not restrict the use of the allowance to absorb losses in other categories.

| | At December 31 | | | | | |
|---|---|---|---|---|---|---|
| | 2008 | | 2007 | | 2006 | |
| | Allowance for Loan Losses | Percent of Loans in Each Category to Total Loans | Allowance for Loan Losses | Percent of Loans in Each Category to Total Loans | Allowance for Loan Losses | Percent of Loans in Each Category to Total Loans |
| Real Estate Loans: | | | | | | |
| One to four family residental | $ 1,185 | 46.1% | $ 793 | 47.3% | $ 175 | 46.9% |
| Commercial | $ 1,666 | 22.0% | $ 1,374 | 21.7% | $ 846 | 21.4% |
| Construction | $ 12 | 3.6% | $ 32 | 4.0% | $ 17 | 4.4% |
| Home Equity & Junior Liens | $ 215 | 11.3% | $ 171 | 11.7% | $ 429 | 11.7% |
| Non Real Estate Loans: | | | | | | |
| Commercial business loans | $ 2,515 | 15.2% | $ 1,579 | 13.0% | $ 527 | 13.3% |
| Consumer | $ 54 | 1.8% | $ 64 | 2.3% | $ 85 | 2.3% |
| Total | $ 5,647 | 100.0% | $ 4,013 | 100.0% | $ 2,079 | 100.0% |

| | At December 31 | | | |
|---|---|---|---|---|
| | 2005 | | 2004 | |
| | Allowance for Loan Losses | Percent of Loans in Each Category to Total Loans | Allowance for Loan Losses | Percent of Loans in Each Category to Total Loans |
| Real Estate Loans: | | | | |
| One to four family residental | $ 168 | 49.3% | $ 126 | 52.1% |
| Commercial | $ 457 | 19.8% | $ 300 | 15.1% |
| Construction | $ 17 | 4.9% | $ 11 | 4.5% |
| Home Equity & Junior Liens | $ 383 | 10.5% | $ 361 | 10.1% |
| Non Real Estate Loans: | | | | |

| | | | | |
|---|---|---|---|---|
| Commercial business loans | $ 302 | 13.1% | $ 305 | 15.3% |
| Consumer | $ 89 | 2.4% | $ 111 | 2.9% |
| Total | $ 1,416 | 100.0% | $ 1,214 | 100.0% |

**Mortgage Banking Activities**

Our mortgage banking activities involve the origination and subsequent sale into the secondary mortgage market of one- to four-family residential mortgage loans. When loans are sold into the secondary market, we generally retain the rights to service those loans thereby maintaining our customer relationships. We intend to use these customer relationships to cross-sell additional products and services. Loans that we sell are originated using the same personnel and the same underwriting policies as loans that we maintain in our portfolio. The decision whether to sell a loan is dependent upon the type of loan product and the term of the loan. In recent years, we have sold most of our fixed-rate one- to four-family residential loans with maturities of 15 years or greater, and have retained servicing on all of these loans until late 2006 when we began selling some mortgage loans servicing-released to be able to offer additional products to our customers.

Mortgage servicing involves the administration and collection of home loan payments. When we acquire mortgage servicing rights through the origination of mortgage loans and the subsequent sale of those loans with servicing rights retained, we allocate a portion of the total cost of the mortgage loans to the mortgage servicing rights based on their relative fair value. As of December 31, 2008, we were servicing loans sold to third parties totaling $127.9 million, and the mortgage servicing rights associated with such loans had a book value, at such date, of $430,000. Generally, the value of mortgage servicing rights increases as interest rates rise and decreases as interest rates fall, because the estimated life and estimated income from the underlying loans increase with rising interest rates and decrease with falling interest rates.

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**Insurance Brokerage Activities**

In March 2003, we acquired InsuranCenter of Alpena ( ICA ), a licensed insurance agency, to increase and diversify our sources of non-interest income. ICA sells life, property, casualty and health insurance products and, to a lesser extent, non-insured investment products. All of these products are sold on an agency basis only.

All of the revenue from our insurance segment is derived through sales commissions calculated as a percentage of the premium paid for the insurance product or the dollar value of the investment product. Generally, commission rates vary in amount depending on the type of insurance or investment product sold, as well as the volume and profitability to the underwriter of the business placed with it by ICA during specific periods. Sales commissions on insurance products generally are collected from the underwriter of the insurance and not from the insureds. Sales commissions on investment products generally are collected from the individual investor.

In April 2008, ICA sold to the Grotenhuis Group (a managing agent for Blue Cross/Blue Shield of Michigan) the rights to service insurance contracts and collect commissions on the contracts written through the local Chambers of Commerce. This sale resulted in a nominal gain to us, but reduced health insurance revenues. The sale also reduced non-interest expenses and amortization of intangibles.

On February 27, 2009, we sold the majority of the assets of ICA. We retained the residual income stream associated with the April 2008 sale of its wholesale Blue Cross/Blue Shield override business to the Grotenhuis Group. The financial position and results of operations of ICA are presented separately in our consolidated financial statements as discontinued operations.

See -Subsidiary Activity for a further discussion of ICA.

**Real Estate Development Activities**

On a limited basis, we have purchased real estate for development through our subsidiary Financial Services & Mortgage Corporation. See Subsidiary Activity for a discussion of our real estate development subsidiary, Financial Services & Mortgage Corporation. The last such purchase was a 37 acre lot which we purchased in 1994 for $130,000. As of December 31, 2008, we had sold 37 of the 43 lots comprising this property and two of the smaller lots had been combined into one lot, so that at December 31, 2008 five lots remained unsold. Our investment in land and real estate is held for sale and separately stated in the statement of financial condition, net of any allowance for impairment. Management is actively marketing the property by using local real estate agents to facilitate the sale of these properties. For reporting purposes, this investment is considered impaired under the definition in SFAS 144, Accounting for Impairment or Disposal of Long-Lived Assets. Accordingly, the investment is recorded at the lower of its cost or fair value less cost to sell, which may include realtor commissions, legal and title transfer fees, and closing costs that must be incurred before legal title can be transferred.

Annually, management uses recent sales of comparable property to determine estimated future cash flows. The estimated future cash flows are used as the fair value. The fair value, less cost to sell, is compared to the net carrying amount. If the fair value, less cost to sell, exceeds the recorded amount, a loss is recognized. Losses recognized for the initial and subsequent write-down to fair value, less cost to sell, are recognized in the gain (loss) on the sale of real estate line in the statement of income. A gain is recognized for any subsequent increase in fair value, less cost to sell, but not in excess of the cumulative loss previously recognized. A gain or loss not previously recognized that results from the sale of the property is recognized at the date of sale.

At December 31, 2008, our investment in these properties was approximately $73,000, which was net of an allowance of $128,000. At December 31, 2008, management prepared an analysis based on the February 26, 2008 selling price of a lot. Based on the analysis and recent lot sale, an additional impairment of $16,000 was identified.

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**Investment Activities**

Our investment securities portfolio comprises U.S. Government, state agency and municipal obligations, mortgage-backed securities, Federal Home Loan Bank stock, and other investments. At December 31, 2008, we had no investments in unrated securities. At December 31, 2008, $18.6 million, or 63.7% of our investment portfolio was scheduled to mature in less than five years, and $10.6 million, or 36.3%, was scheduled to mature in over five years. At December 31, 2008, $4.6 million, or 15.8% of our investment portfolio was scheduled to mature in less than one year.

At December 31, 2008, we held U.S. Government and state agency obligations and municipal obligations classified as available-for-sale, with a fair market value of $5.8 million. While these securities generally provide lower yields than other investments such as mortgage-backed securities, our current investment strategy is to maintain investments in such instruments to the extent appropriate for liquidity purposes, as collateral for borrowings, and for prepayment protection.

We invest in mortgage-backed securities in order to: generate positive interest rate spreads with minimal administrative expense; lower credit risk as a result of the guarantees provided by Freddie Mac, Fannie Mae and Ginnie Mae; supplement local loan originations; reduce interest rate risk exposure; and increase liquidity. Our mortgage-backed securities portfolio consists of pass-through certificates. At December 31, 2008, mortgage-backed securities totaled $14.1 million, or 41.6% of total investments. At December 31, 2008, 45.3% of our mortgage-backed securities were secured by balloon loans. All of our pass-through certificates are insured or guaranteed by Freddie Mac, Ginnie Mae or Fannie Mae. Our policy is to hold mortgage-backed securities as available for sale.

We have interests in pools of single-family mortgages in which the principal and interest payments are passed from the mortgage originators, through intermediaries (generally government-sponsored agencies) that pool and repackage loans and sell the participation interest in the form of securities, to investors. These government-sponsored agencies include Freddie Mac, Ginnie Mae, or Fannie Mae. The underlying pool of mortgages can be comprised of either fixed-rate mortgage loans or adjustable-rate mortgage loans. The interest rate risk characteristics of the underlying pool of mortgages, *i.e.*, fixed-rate or adjustable rate, are shared by the investors in that pool.

Our investment policy also permits investment in corporate debt obligations. Although corporate bonds may offer higher yields than U.S. Treasury or agency securities of comparable duration, corporate bonds also have a higher risk of default due to possible adverse changes in the creditworthiness of the issuer.

We are required under federal regulations to maintain a minimum amount of liquid assets that may be invested in specified short term securities and certain other investments. We generally have maintained a portfolio of liquid assets that exceeds regulatory requirements. Liquidity levels may be increased or decreased depending upon the yields on investment alternatives and upon management s judgment as to the attractiveness of the yields then available in relation to other opportunities and its expectation of the level of yield that will be available in the future, as well as management s projections as to the short term demand for funds to be used in our loan origination and other activities.

SFAS No. 115 requires that, at the time of purchase, we designate a security as held to maturity, available for sale, or trading, depending on our ability and intent. Securities available for sale are reported at fair value. As of December 31, 2008, all of our investment securities were designated as available for sale except for $4.0 million in municipal bond investments designated as held to maturity.

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***Investment Securities Portfolio.*** The following table sets forth the composition of our investment securities portfolio at the dates indicated.

| | At December 31, | | | | | |
|---|---|---|---|---|---|---|
| | 2008 | | 2007 | | 2006 | |
| | Amortized Cost | Fair Value | Amortized Cost | Fair Value | Amortized Cost | Fair Value |
| | (In Thousands) | | | | | |
| Debt Securities: | | | | | | |
| U.S. Government and agency obligations | $ 5,680 | $ 5,768 | $ 18,477 | $ 18,514 | $ 36,271 | $ 35,902 |
| State agency and municipal obligations | 7,942 | 7,924 | 3,600 | 3,623 | 3,771 | 3,789 |
| Corporate bonds and other obligations | 1,500 | 1,504 | | | | |
| Mortgage-backed securities: | | | | | | |
| Pass-through securities: | | | | | | |
| Fannie Mae | 9,468 | 9,733 | | | 576 | 539 |
| Freddie Mac | 4,419 | 4,516 | 1,076 | 1,054 | 3,007 | 2,888 |
| Ginnie Mae | 164 | 167 | 197 | 197 | 1,622 | 1,594 |
| Total debt securities | 29,173 | 29,612 | 23,350 | 23,388 | 45,247 | 44,712 |
| Marketable equity securities | | | | | | |
| Common stock | 3 | 2 | 3 | 87 | 3 | 171 |
| Total equity securities | 3 | 2 | 3 | 87 | 3 | 171 |
| Total investment securities | $ 29,176 | $ 29,614 | $ 23,353 | $ 23,476 | $ 45,250 | $ 44,883 |

*Portfolio Maturities and Yields.* The composition and maturities of the investment securities portfolio at December 31, 2008 are summarized in the following table. Maturities are based on the final contractual payment dates, and do not reflect the impact of prepayments or early redemptions that may occur. State and municipal securities yields have not been adjusted to a tax-equivalent basis.

| | At December 31, 2008 | | | | | |
|---|---|---|---|---|---|---|
| | One Year or Less | More than One Year Through Five years | More than Five Years Through Ten Years | More than Ten Years | Total Securities | |
| | Weighted | Weighted | Weighted | Weighted | | Weighted |

| | Amortized Cost | Average Yield | Amortized Cost | Average Yield | Amortized Cost | Average Yield | Amortized Cost | Average Yield | Amortized Cost | Fair Value | Average Yield |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | (Dollars in Thousands) | | | | | | | | | | |
| **Debt Securities:** | | | | | | | | | | | |
| U.S. Government and agency securities | $ 3,999 | 4.06% | $ 1,681 | 4.10% | $ | 0.00% | $ | 0.00% | $ 5,680 | $ 5,768 | 4.07% |
| State agency and municipal obligations | 85 | 3.69% | 4,108 | 4.17% | 1,828 | 4.05% | 1,921 | 4.70% | 7,942 | 7,924 | 4.27% |
| Corporate bonds and other obligations | 499 | 6.38% | 1,001 | 5.72% | | 0.00% | | 0.00% | 1,500 | 1,504 | 5.94% |
| Mortgage-backed securities | | | | | | | | | | | |
| Fannie Mae | | 0.00% | 3,801 | 4.00% | 876 | 4.50% | 4,792 | 5.29% | 9,468 | 9,733 | 4.70% |
| Freddie Mac | | 0.00% | 3,449 | 4.16% | 16 | 4.62% | 954 | 5.00% | 4,419 | 4,516 | 4.35% |
| Ginnie Mae | | 0.00% | | 0.00% | 164 | 5.26% | | 0.00% | 164 | 167 | 5.26% |
| Total debt securities | 4,583 | | 14,040 | | 2,884 | | 7,667 | | 29,173 | 29,612 | |
| **Marketable equity securities:** | | | | | | | | | | | |
| Common Stock | | 0.00% | | 0.00% | | 0.00% | 3 | 0.00% | 3 | 2 | 0.00% |
| Total investment securities | $ 4,583 | | $ 14,040 | | $ 2,884 | | $ 7,670 | | $ 29,176 | $ 29,614 | |

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**Sources of Funds**

***General.*** Deposits are the major source of our funds for lending and other investment purposes. We generate deposits from our eight full-service offices in Alpena, Mio, Cheboygan, Oscoda, Lewiston, Alanson and Gaylord. In addition to deposits, we derive funds from borrowings, proceeds from the settlement of loan sales, the amortization and prepayment of loans and mortgage-backed securities, the maturity of investment securities, and operations. Scheduled loan principal repayments are a relatively stable source of funds, while deposit inflows and outflows and loan prepayments are influenced significantly by general interest rates and market conditions. Borrowings are used on a short-term basis to compensate for reductions in the availability of funds from other sources or on a longer term basis for general business purposes. We currently are managing liquidity levels and loan funding primarily through secondary mortgage market sales and Federal Home Loan Bank advances.

***Deposits.*** We generate deposits primarily from our market area by offering a broad selection of deposit instruments including NOW accounts, regular savings, money market deposits, term certificate accounts and individual retirement accounts. Deposit account terms vary according to the minimum balance required, the period of time during which the funds must remain on deposit, and the interest rate, among other factors. The rate of interest which we must pay is not established by regulatory authority. The asset/liability committee regularly evaluates our internal cost of funds, surveys rates offered by competing institutions, reviews the cash flow requirements for lending and liquidity, and executes rate changes when deemed appropriate. We have sought to decrease the risk associated with changes in interest rates by offering competitive rates on some deposit accounts and by pricing certificates of deposit to provide customers with incentives to choose certificates of deposit with longer maturities. We also attract non-interest bearing commercial deposit accounts from our commercial borrowers and offer a competitive sweep product that is not insured by the FDIC. In recent periods, we generally have not obtained funds through brokers or through a solicitation of funds outside our market area. At December 31, 2008 we had no brokered deposits. We offer a limited amount of certificates of deposit in excess of $100,000 which may have negotiated rates. Future liquidity needs are expected to be satisfied through the use of Federal Home Loan Bank borrowings as necessary. Management does not generally plan on paying above-market rates on deposit products, although from time-to-time we may do so as liquidity needs dictate.

The following table sets forth the distribution of total deposit accounts, by account type, at the dates indicated.

| | At December 31, | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | 2008 | | | 2007 | | | 2006 | | |
| | Amount | Percent of Total | Weighted Average Interest Rate | Amount | Percent of Total | Weighted Average Interest Rate | Amount | Percent of Total | Weighted Average Interest Rate |
| | (Dollars in thousands) | | | | | | | | |
| Non-interest-bearing | $ 10,410 | 6.28% | NA | $ 10,186 | 6.45% | NA | $ 10,029 | 5.88% | NA |
| NOW accounts | 14,652 | 8.84% | 0.33% | 15,135 | 9.59% | 0.32% | 15,526 | 9.10% | 0.31% |
| Passbook | 14,857 | 8.96% | 0.15% | 15,964 | 10.11% | 0.30% | 18,990 | 11.13% | 0.30% |
| Money market accounts | 19,394 | 11.70% | 2.66% | 11,116 | 7.04% | 2.61% | 12,450 | 7.30% | 2.64% |
| Time deposits that mature: | | | | | | | | | |
| Less than 12 months | 68,753 | 41.47% | 3.72% | 77,275 | 48.96% | 4.37% | 86,106 | 50.47% | 4.52% |
| Within 12-36 months | 34,429 | 20.77% | 3.95% | 24,944 | 15.80% | 4.68% | 19,670 | 11.53% | 4.08% |
| Beyond 36 months | 3,283 | 1.98% | 3.78% | 3,213 | 2.04% | 4.22% | 7,125 | 4.18% | 5.31% |
| Jumbo | | 0.00% | 0.00% | | 0.00% | 0.00% | 700 | 0.41% | 4.04% |

| | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| Total deposits | $ 165,778 | 100.00% | 2.79% | $ 157,833 | 100.00% | 3.19% | $ 170,596 | 100.00% | 3.27% |

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***Time Deposit Rates.*** The following table sets forth time deposits classified by rates as of the dates indicated (see Note 8 to our consolidated financial statements contained within Exhibit 13) for a more detailed breakdown by rate range):

| Rate | At December 31, 2008 | 2007 | 2006 |
|---|---|---|---|
| | | (In Thousands) | |
| Less than 2% | $ 8,577 | $ | $ 757 |
| 2.00 percent to 2.99 percent | 11,776 | 11,346 | 4,487 |
| 3.00 percent to 3.99 percent | 42,403 | 11,977 | 25,847 |
| 4.00 percent to 4.99 percent | 38,278 | 70,900 | 52,502 |
| 5.00 percent to 6.99 percent | 4,036 | 9,857 | 28,503 |
| 7.00 percent to 8.99 percent | 1,395 | 1,352 | 1,505 |
| | $ 106,465 | $ 105,432 | $ 122,590 |

***Time Deposit Maturities***. The following table sets forth the amount and maturities of time deposits at December 31, 2008.

| Rate | Less Than One Year | 1 Less than 2 Years | 2 Less than 3 Years | 3 Less than 5 Years | 5 years and Greater | Total |
|---|---|---|---|---|---|---|
| Less than 2% | $ 6,182 | $ 2,387 | $ 8 | $ | $ | $ 8,577 |
| 2.00 percent to 2.99 percent | 7,005 | 4,537 | 141 | 31 | 62 | 11,776 |
| 3.00 percent to 3.99 percent | 27,904 | 7,782 | 4,745 | 1,497 | 475 | 42,403 |
| 4.00 percent to 4.99 percent | 26,134 | 8,629 | 2,296 | 1,069 | 150 | 38,278 |
| 5.00 percent to 6.99 percent | 1,529 | 2,021 | 486 | | | 4,036 |
| 7.00 percent to 8.99 percent | | 1,395 | | | | 1,395 |
| | $ 68,754 | $ 26,751 | $ 7,676 | $ 2,597 | $ 687 | $ 106,465 |

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As of December 31, 2008, the aggregate amount of outstanding certificates of deposit in amounts greater than or equal to $100,000 was $35.6 million. The following table sets forth the maturity of those certificates as of December 31, 2008.

| Maturity Period | Certificates of Deposit in excess of $100,000 |
|---|---|
| | (In thousands) |
| Three months or less | $ 11,111 |
| Three through six months | 6,155 |
| Six through twelve months | 7,888 |
| Over twelve months | 10,495 |
| Total | $ 35,649 |

***Borrowings.*** Our borrowings consist primarily of advances from the Federal Home Loan Bank of Indianapolis. At December 31, 2008, we had access to additional Federal Home Loan Bank advances of up to $49.3 million. The following table sets forth information concerning balances and interest rates on our Federal Home Loan Bank advances and other borrowings at the dates and for the periods indicated.

| | Years Ended December 31, | | |
|---|---|---|---|
| | 2008 | 2007 | 2006 |
| | (Dollars in Thousands) | | |
| Balance at end of period | $40,969 | $52,684 | $66,042 |
| Average balance during period | $47,075 | $54,425 | $62,159 |
| Maximum outstanding at any month end | $48,900 | $66,850 | $66,650 |
| Weighted average interest rate at end of period | 4.22% | 4.68% | 5.09% |
| Average interest rate during period | 4.27% | 4.78% | 4.99% |

**Subsidiary Activity**

First Federal of Northern Michigan Bancorp, Inc. s only direct subsidiary is First Federal of Northern Michigan.

First Federal of Northern Michigan has two wholly owned subsidiaries as of December 31, 2008. First Federal of Northern Michigan and these subsidiaries have been consolidated in the financial statements and all inter-company balances and transactions have been eliminated in consolidation.

One subsidiary, Financial Services & Mortgage Corporation, leases, sells, develops and maintains real estate properties. For reporting purposes, Financial Services & Mortgage Corporation is included in our banking segment. As of December 31, 2008, First Federal of Northern Michigan s investment in Financial Services & Mortgage Corporation was $293,000. The primary asset of the subsidiary is an investment in land and real estate. See Real Estate Development Activities. At December 31, 2008, Financial Services & Mortgage Corporation owned five developed building sites which were being offered for sale. Financial Services & Mortgage Corporation is not currently a party to any agreement that is material to First Federal of Northern Michigan Bancorp, Inc. on a consolidated basis.

First Federal of Northern Michigan s second subsidiary, ICA, is a licensed insurance agency engaged in the business of property, casualty and health insurance sales. First Federal of Northern Michigan acquired ICA in June 2003 for $2.87 million. ICA s revenues are derived from the sale of life insurance, property and casualty insurance and health insurance.

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In April 2008, ICA sold to the Grotenhuis Group (a managing agent for Blue Cross/Blue Shield of Michigan) the rights to service insurance contracts and collect commissions on the contracts written through the local Chambers of Commerce. This sale resulted in a nominal gain to us, but reduced health insurance revenues. The sale also reduced non-interest expenses and amortization of intangibles.

On February 27, 2009, we sold the majority of the assets of ICA. We retained the residual income stream associated with the April 2008 sale of its wholesale Blue Cross/Blue Shield override business to the Grotenhuis Group. The financial position and results of operations of ICA are presented separately in our consolidated financial statements as discontinued operations.

**Personnel**

As of December 31, 2008, First Federal of Northern Michigan had 77 full-time and 19 part-time employees. None of the Bank s employees is represented by a collective bargaining group. The Bank believes its relationship with its employees to be good. ICA had 11 full-time and 5 part-time employees as of the same date. First Federal of Northern Michigan Bancorp, Inc. and FSMC have no separate employees.

## SUPERVISION AND REGULATION

**General**

As a federally chartered savings bank, First Federal of Northern Michigan is regulated and supervised by the Office of Thrift Supervision and the Federal Deposit Insurance Corporation. This regulation and supervision establishes a comprehensive framework of activities in which we may engage, and is intended primarily for the protection of the Federal Deposit Insurance Corporation s deposit insurance funds and depositors. Under this system of federal regulation, financial institutions are periodically examined to ensure that they satisfy applicable standards with respect to their capital adequacy, assets, management, earnings, liquidity and sensitivity to market interest rates. After completing an examination, the federal agency critiques the financial institution s operations and assigns its rating (known as an institution s CAMELS). Under federal law, an institution may not disclose its CAMELS rating to the public. First Federal of Northern Michigan also is a member of, and owns stock in, the Federal Home Loan Bank of Indianapolis, which is one of the twelve regional banks in the Federal Home Loan Bank System. First Federal of Northern Michigan also is regulated, to a lesser extent, by the Board of Governors of the Federal Reserve System, governing reserves to be maintained against deposits and other matters. The Office of Thrift Supervision examines First Federal of Northern Michigan and prepares reports for consideration by our board of directors on any operating deficiencies. First Federal of Northern Michigan s relationship with our depositors and borrowers also is regulated to a great extent by both federal and state laws, especially in matters concerning the ownership of deposit accounts and the form and content of our loan documents.

There can be no assurance that changes to existing laws, rules and regulations, or any other new laws, rules or regulations, will not be adopted in the future, which could make compliance more difficult or expensive or otherwise adversely affect our business, financial condition or prospects. Any change in these laws or regulations, or in regulatory policy, whether by the Federal Deposit Insurance Corporation, the Office of Thrift Supervision or Congress, could have a material adverse impact on our business, financial condition or operations.

Certain of the regulatory requirements that are applicable to First Federal of Northern Michigan and First Federal of Northern Michigan Bancorp, Inc. are described below. This description of statutes and regulations is not intended to be a complete explanation of such statutes and regulations and their effects on First Federal of Northern Michigan and First Federal of Northern Michigan Bancorp. Inc. and is qualified in its entirety by reference to the actual statutes and regulations.

**Federal Banking Regulation**

***Business Activities.*** A federal savings bank derives its lending and investment powers from the Home Owners Loan Act, and the regulations of the Office of Thrift Supervision. Under these laws and regulations, First Federal of Northern Michigan may invest in mortgage loans secured by residential and commercial real estate, commercial business and consumer loans, certain types of debt securities and certain other loans and assets. First Federal of Northern Michigan also may establish subsidiaries that may engage in activities not otherwise permissible for First Federal of Northern Michigan directly, including real estate investment, securities brokerage and insurance agency services.

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***Capital Requirements.*** Office of Thrift Supervision (OTS) regulations require savings banks to meet three minimum capital standards: a 1.5% tangible capital ratio, a 4% leverage ratio (3% for institutions receiving the highest CAMELS rating) and an 8% risk-based capital ratio. The prompt corrective action standards discussed below, in effect, establish a minimum 2% tangible capital standard.

The risk-based capital standard for savings banks requires the maintenance of Tier 1 (core) and total capital (which is defined as core capital and supplementary capital) to risk-weighted assets of at least 4% and 8%, respectively. In determining the amount of risk-weighted assets, all assets, including certain off-balance sheet assets, are multiplied by a risk-weight factor of 0% to 100%, assigned by the Office of Thrift Supervision capital regulation based on the risks inherent in the type of asset. Core capital is defined as common stockholders equity (including retained earnings), certain noncumulative perpetual preferred stock and related surplus and minority interests in equity accounts of consolidated subsidiaries, less intangibles other than certain mortgage servicing rights and credit card relationships. The components of supplementary capital currently include cumulative preferred stock, long-term perpetual preferred stock, mandatory convertible securities, subordinated debt and intermediate preferred stock, allowance for loan and lease losses up to a maximum of 1.25% of risk-weighted assets, and up to 45% of net unrealized gains on available-for-sale equity securities with readily determinable fair market values. Overall, the amount of supplementary capital included as part of total capital cannot exceed 100% of core capital.

At December 31, 2008, First Federal of Northern Michigan s capital exceeded all applicable requirements. The following table sets forth the Bank s capital position at December 31, 2008 and 2007, as compared to the minimum capital requirements.

| | At December 31, | | | |
|---|---|---|---|---|
| | 2008 | | 2007 | |
| | Amount | Percent of Assets | Amount | Percent of Assets |
| | (Dollars in Thousands) | | | |
| Equity capital | $ 28,320 | 11.43% | $ 31,154 | 12.42% |
| Tangible Capital Requirement: | | | | |
| Tangible capital level | 24,887 | 10.31% | 27,295 | 11.05% |
| Requirement | 3,628 | 1.50% | 3,705 | 1.50% |
| Excess | 21,260 | 8.81% | 23,590 | 9.55% |
| Core Capital Requirement: | | | | |
| Core capital level | 24,887 | 10.31% | 27,295 | 11.05% |
| Requirement | 9,674 | 4.00% | 9,880 | 4.00% |
| Excess | 15,213 | 6.31% | 17,415 | 7.05% |
| Risk-based Capital Requirement: | | | | |
| Risk-based capital level | 27,079 | 15.75% | 29,607 | 16.27% |
| Requirement | 13,840 | 8.00% | 14,558 | 8.00% |
| Excess | 13,239 | 7.75% | 15,049 | 8.27% |

***Loans to One Borrower.*** A federal savings bank generally may not make a loan or extend credit to a single or related group of borrowers in excess of 15% of unimpaired capital and surplus on an unsecured basis. An additional amount may be loaned, equal to 10% of unimpaired capital and surplus, if the loan is secured by readily marketable collateral, which generally does not include real estate. At December 31, 2008 First Federal of Northern Michigan was determined by the OTS to be in violation of the loans-to-one-borrower limitation with respect to one commercial loan

relationship which totaled $5.8 million. Otherwise First Federal of Northern Michigan was in compliance with the loans-to-one borrower limitation.

***Qualified Thrift Lender Test.*** As a federal savings bank, First Federal of Northern Michigan is subject to a qualified thrift lender, or QTL, test. Under the QTL test, First Federal of Northern Michigan must maintain at least 65% of its portfolio assets in qualified thrift investments in at least nine months of the most recent 12-month period. Portfolio assets generally means total assets of a savings institution, less the sum of specified liquid assets up to 20% of total assets, goodwill and other intangible assets, and the value of property used in the conduct of the institution s business.

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Qualified thrift investments include various types of loans made for residential and housing purposes, investments related to such purposes, including certain mortgage-backed and related securities, and loans for personal, family, household and certain other purposes up to a limit of 20% of portfolio assets. Qualified thrift investments also include 100% of an institution s credit card loans, education loans and small business loans. First Federal of Northern Michigan also may satisfy the QTL test by qualifying as a domestic building and loan association as defined in the Internal Revenue Code of 1986.

A savings bank that fails the QTL test must either convert to a bank charter or operate under specified restrictions. At December 31, 2008, First Federal of Northern Michigan maintained approximately 91.8% of its portfolio assets in qualified thrift investments, and therefore satisfied the QTL test.

***Capital Distributions.*** Office of Thrift Supervision regulations govern capital distributions by a federal savings bank, which include cash dividends, stock repurchases and other transactions charged to the institution s capital account. A savings bank must file an application for approval of a capital distribution if:

the total capital distributions for the applicable calendar year exceed the sum of the savings bank s net income for that year to date plus the savings bank s retained net income for the preceding two years;

the savings bank would not be at least adequately capitalized following the distribution;

the distribution would violate any applicable statute, regulation, agreement or Office of Thrift Supervision-imposed condition; or

the savings bank is not eligible for expedited treatment of its filings.

Even if an application is not otherwise required, every savings bank that is a subsidiary of a holding company must still file a notice with the Office of Thrift Supervision at least 30 days before the board of directors declares a dividend or approves a capital distribution.

The Office of Thrift Supervision may disapprove a notice or application if:

the savings bank would be undercapitalized following the distribution;

the proposed capital distribution raises safety and soundness concerns; or

the capital distribution would violate a prohibition contained in any statute, regulation or agreement.

In addition, the Federal Deposit Insurance Act provides that an insured depository institution shall not make any capital distribution if after making such distribution the institution would be undercapitalized.

***Liquidity.*** A federal savings bank is required to maintain a sufficient amount of liquid assets to ensure its safe and sound operation

***Community Reinvestment Act and Fair Lending Laws.*** All savings banks have a responsibility under the Community Reinvestment Act and related regulations of the Office of Thrift Supervision to help meet the credit needs of their communities, including low- and moderate-income neighborhoods. In connection with its examination of a federal savings bank, the Office of Thrift Supervision is required to assess the savings bank s record of compliance with the Community Reinvestment Act. In addition, the Equal Credit Opportunity Act and the Fair Housing Act prohibit lenders from discriminating in their lending practices on the basis of characteristics specified in those statutes. A savings bank s failure to comply with the provisions of the Community Reinvestment Act could, at a minimum, result in regulatory restrictions on its activities. The failure to comply with the Equal Credit Opportunity Act and the Fair Housing Act could result in enforcement actions by the Office of Thrift Supervision, as well as other federal regulatory agencies and the Department of Justice. First Federal of Northern Michigan received an Outstanding Community Reinvestment Act rating in its most recent federal examination.

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***Transactions with Related Parties.*** A federal savings bank s authority to engage in transactions with its affiliates is limited by Office of Thrift Supervision regulations and Regulation W of the Federal Reserve Board, which implements Sections 23A and 23B of the Federal Reserve Act. The term affiliates for these purposes generally means any company that controls or is under common control with an institution. First Federal of Northern Michigan Bancorp, Inc. and its non-savings institution subsidiaries will be affiliates of First Federal of Northern Michigan. In general, transactions with affiliates must be on terms that are as favorable to the savings bank as comparable transactions with non-affiliates. In addition, certain types of these transactions are restricted to an aggregate percentage of the savings bank s capital. Collateral in specified amounts must usually be provided by affiliates in order to receive loans from the savings bank. In addition, Office of Thrift Supervision regulations prohibit a savings bank from lending to any of its affiliates that are engaged in activities that are not permissible for bank holding companies and from purchasing the securities of any affiliate, other than a subsidiary.

First Federal of Northern Michigan s authority to extend credit to its directors, executive officers and 10% stockholders, as well as to entities controlled by such persons, is currently governed by the requirements of Sections 22(g) and 22(h) of the Federal Reserve Act and Regulation O of the Federal Reserve Board. Among other things, these provisions require that extensions of credit to insiders (i) be made on terms that are substantially the same as, and follow credit underwriting procedures that are not less stringent than, those prevailing for comparable transactions with unaffiliated persons and that do not involve more than the normal risk of repayment or present other unfavorable features, and (ii) not exceed certain limitations on the amount of credit extended to such persons, individually and in the aggregate, which limits are based, in part, on the amount of First Federal of Northern Michigan s capital. In addition, extensions of credit in excess of certain limits must be approved by First Federal of Northern Michigan s board of directors.

***Enforcement.*** The Office of Thrift Supervision has primary enforcement responsibility over federal savings banks and has the authority to bring enforcement action against all institution-affiliated parties, including stockholders, attorneys, appraisers and accountants who knowingly or recklessly participate in wrongful action likely to have an adverse effect on an institution. Formal enforcement action may range from the issuance of a capital directive or cease and desist order to removal of officers and/or directors of the savings bank, receivership, conservatorship or the termination of deposit insurance. Civil penalties cover a wide range of violations and actions, and range up to $25,000 per day, unless a finding of reckless disregard is made, in which case penalties may be as high as $1 million per day. The Federal Deposit Insurance Corporation also has the authority to recommend to the Director of the Office of Thrift Supervision that enforcement action be taken with respect to a particular savings bank. If action is not taken by the Director, the Federal Deposit Insurance Corporation has authority to take action under specified circumstances.

***Standards for Safety and Soundness.*** Federal law requires each federal banking agency to prescribe certain standards for all insured depository institutions. These standards relate to, among other things, internal controls, information systems and audit systems, loan documentation, credit underwriting, interest rate risk exposure, asset growth, compensation, and other operational and managerial standards as the agency deems appropriate. The federal banking agencies adopted Interagency Guidelines Prescribing Standards for Safety and Soundness to implement the safety and soundness standards required under federal law. The guidelines set forth the safety and soundness standards that the federal banking agencies use to identify and address problems at insured depository institutions before capital becomes impaired. The guidelines address internal controls and information systems, internal audit systems, credit underwriting, loan documentation, interest rate risk exposure, asset growth, compensation, fees and benefits. If the appropriate federal banking agency determines that an institution fails to meet any standard prescribed by the guidelines, the agency may require the institution to submit to the agency an acceptable plan to achieve compliance with the standard. If an institution fails to meet these standards, the appropriate federal banking agency may require the institution to submit a compliance plan.

***Prompt Corrective Action Regulations.*** Under the prompt corrective action regulations, the Office of Thrift Supervision is required and authorized to take supervisory actions against undercapitalized savings banks. For this purpose, a savings bank is placed in one of the following five categories based on the savings bank s capital:

well-capitalized (at least 5% leverage capital, 6% tier 1 risk-based capital and 10% total risk-based capital);

adequately capitalized (at least 4% leverage capital, 4% tier 1 risk-based capital and 8% total risk-based capital);

undercapitalized (less than 3% leverage capital, 4% tier 1 risk-based capital or 8% total risk-based capital);

significantly undercapitalized (less than 3% leverage capital, 3% tier 1 risk-based capital or 6% total risk-based capital); or

critically undercapitalized (less than 2% tangible capital).

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Generally, the Office of Thrift Supervision is required to appoint a receiver or conservator for a savings bank that is critically undercapitalized. The regulation also provides that a capital restoration plan must be filed with the Office of Thrift Supervision within 45 days of the date a savings bank receives notice that it is undercapitalized, significantly undercapitalized or critically undercapitalized. In addition, numerous mandatory supervisory actions become immediately applicable to the savings bank, including, but not limited to, restrictions on growth, investment activities, capital distributions and affiliate transactions. The Office of Thrift Supervision may also take any one of a number of discretionary supervisory actions against undercapitalized savings banks, including the issuance of a capital directive and the replacement of senior executive officers and directors.

At December 31, 2008, First Federal of Northern Michigan met the criteria for being considered well-capitalized.

***Insurance of Deposit Accounts.*** First Federal of Northern Michigan is a member of the Deposit Insurance Fund, which is administered by the FDIC. Deposit accounts at First Federal of Northern Michigan are insured by the FDIC, generally up to a maximum of $100,000 for each separately insured depositor and up to a maximum of $250,000 for self-directed retirement accounts. However, the FDIC increased the deposit insurance available on all deposit accounts to $250,000, effective until December 31, 2009. In addition, certain noninterest-bearing transaction accounts maintained with financial institutions participating in the FDIC s Temporary Liquidity Guarantee Program are fully insured regardless of the dollar amount until December 31, 2009. First Federal of Northern Michigan has opted to participate in the FDIC s Temporary Liquidity Guarantee Program. See Temporary Liquidity Guarantee Program.

The FDIC imposes an assessment against all depository institutions for deposit insurance. This assessment is based on the risk category of the institution and, prior to 2009, ranged from five to 43 basis points of the institution s deposits. On February 27, 2009, the FDIC published a final rule raising the current deposit insurance assessment rates to a range from 12 to 45 basis points beginning April 1, 2009. Additionally, the FDIC issued an interim final rule that would impose a special 20 basis points assessment on deposits as of June 30, 2009, which would be payable to the FDIC on September 30, 2009. The cost of this special assessment to First Federal of Northern Michigan, based on deposits as of December 31, 2008, would be approximately $360,000.

Insurance of deposits may be terminated by the FDIC upon a finding that an institution 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. We do not currently know of any practice, condition or violation that might lead to termination of our deposit insurance.

In addition to the FDIC assessments, the Financing Corporation ( FICO ) is authorized to impose and collect, with the approval of the FDIC, assessments for anticipated payments, issuance costs and custodial fees on bonds issued by the FICO in the 1980s to recapitalize the former Federal Savings and Loan Insurance Corporation. The bonds issued by the FICO are due to mature in 2017 through 2019. For the quarter ended December 31, 2008, the annualized FICO assessment was equal to 1.10 basis points for each $100 in domestic deposits maintained at an institution.

***Temporary Liquidity Guarantee Program.*** On October 14, 2008, the FDIC announced a new program - the Temporary Liquidity Guarantee Program. This program has two components. One guarantees newly issued senior unsecured debt of a participating organization, up to certain limits established for each institution, issued between October 14, 2008 and June 30, 2009. The FDIC will pay the unpaid principal and interest on an FDIC -guaranteed debt instrument upon the uncured failure of the participating entity to make a timely payment of principal or interest in accordance with the terms of the instrument. The guarantee will remain in effect until June 30, 2012. In return for the FDIC s guarantee, participating institutions will pay the FDIC a fee based on the amount and maturity of the debt. First Federal of Northern Michigan opted not to participate in this component of the Temporary Liquidity Guarantee Program. [CONFIRM]

The other component of the program provides full federal deposit insurance coverage for non-interest bearing transaction deposit accounts, regardless of dollar amount, until December 31, 2009. An annualized 10 basis point assessment on balances in noninterest-bearing transaction accounts that exceed the existing deposit insurance limit of $250,000 will be assessed on a quarterly basis to insured depository institutions that have not opted out of this component of the Temporary Liquidity Guarantee Program. First Federal of Northern Michigan opted to participate in this component of the Temporary Liquidity Guarantee Program.

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***U.S. Treasury s Troubled Asset Relief Program Capital Purchase Program.*** The Emergency Economic Stabilization Act of 2008 was enacted in October 2008 and provides the U.S. Secretary of the Treasury with broad authority to implement certain actions to help restore stability and liquidity to U.S. markets. One of the provisions resulting from the legislation is the U.S. Treasury s Capital Purchase Program ( CPP ) under the Troubled Asset Relief Program. CPP provides direct equity investment in perpetual preferred stock by the U.S. Treasury in qualified financial institutions. The program is voluntary and requires an institution to comply with a number of restrictions and provisions, including limits on executive compensation, stock redemptions and dividends. The CPP provides for a minimum investment of one percent of total risk-weighted assets and a maximum investment equal to the lesser of three percent of total risk-weighted assets or $25 billion. Participation in the program is not automatic and is subject to approval by the U.S. Treasury. First Federal of Northern Michigan Bancorp, Inc. opted not to participate in the CPP.

***Prohibitions Against Tying Arrangements*.** Federal savings banks are prohibited, subject to some exceptions, from extending credit to or offering any other service, or fixing or varying the consideration for such extension of credit or service, on the condition that the customer obtain some additional service from the savings bank or its affiliates or not obtain services of a competitor of the savings bank.

***Federal Home Loan Bank System.*** First Federal of Northern Michigan is a member of the Federal Home Loan Bank System, which consists of 12 regional Federal Home Loan Banks. The Federal Home Loan Bank System provides a central credit facility primarily for member institutions. As a member of the Federal Home Loan Bank of Indianapolis, First Federal of Northern Michigan is required to acquire and hold shares of capital stock in the Federal Home Loan Bank in an amount equal to at least 1% of the aggregate principal amount of its unpaid residential mortgage loans and similar obligations at the beginning of each year, or 1/20 of its borrowings from the Federal Home Loan Bank, whichever is greater. As of December 31, 2008, First Federal of Northern Michigan was in compliance with this requirement.

**Other Regulations**

Interest and other charges collected or contracted for by First Federal of Northern Michigan are subject to state usury laws and federal laws concerning interest rates. First Federal of Northern Michigan s operations are also subject to federal laws applicable to credit transactions, such as the:

- Truth-In-Lending Act, governing disclosures of credit terms to consumer borrowers;
- Home Mortgage Disclosure Act, requiring financial institutions to provide information to enable the public and public officials to determine whether a financial institution is fulfilling its obligation to help meet the housing needs of the community it serves;
- Equal Credit Opportunity Act, prohibiting discrimination on the basis of race, creed or other prohibited factors in extending credit;
- Fair Credit Reporting Act, governing the use and provision of information to credit reporting agencies;
- Fair Debt Collection Act, governing the manner in which consumer debts may be collected by collection agencies;
- Truth in Savings Act; and
- rules and regulations of the various federal agencies charged with the responsibility of implementing such federal laws.

The operations of First Federal of Northern Michigan also are subject to the:

- Right to Financial Privacy Act, which imposes a duty to maintain confidentiality of consumer financial records and prescribes procedures for complying with administrative subpoenas of financial records;

Electronic Funds Transfer Act and Regulation E promulgated thereunder, which govern automatic deposits to and withdrawals from deposit accounts and customers rights and liabilities arising from the use of automated teller machines and other electronic banking services;

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Check Clearing for the 21st Century Act (also known as Check 21 ), which gives substitute checks, such as digital check images and copies made from that image, the same legal standing as the original paper check;

Title III of The Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (referred to as the USA PATRIOT Act ), which significantly expanded the responsibilities of financial institutions, including savings and loan associations, in preventing the use of the American financial system to fund terrorist activities. Among other provisions, the USA PATRIOT Act and the related regulations of the OTS require savings associations operating in the United States to develop new anti-money laundering compliance programs, due diligence policies and controls to ensure the detection and reporting of money laundering. Such required compliance programs are intended to supplement existing compliance requirements, also applicable to financial institutions, under the Bank Secrecy Act and the Office of Foreign Assets Control regulations; and

The Gramm-Leach-Bliley Act, which places limitations on the sharing of consumer financial information by financial institutions with unaffiliated third parties. Specifically, the Gramm-Leach-Bliley Act requires all financial institutions offering financial products or services to retail customers to provide such customers with the financial institution s privacy policy and provide such customers the opportunity to opt out of the sharing of certain personal financial information with unaffiliated third parties.

**Federal Reserve System**

Federal Reserve Board regulations require savings banks to maintain non-interest-earning reserves against their transaction accounts, such as negotiable order of withdrawal and regular checking accounts. At December 31, 2008, First Federal of Northern Michigan was in compliance with these reserve requirements. The balances maintained to meet the reserve requirements imposed by the Federal Reserve Board may be used to satisfy liquidity requirements imposed by the Office of Thrift Supervision.

**The USA PATRIOT Act**

The USA PATRIOT Act gives the federal government new powers to address terrorist threats through enhanced domestic security measures, expanded surveillance powers, increased information sharing and broadened anti-money laundering requirements. Certain provisions of the Act impose affirmative obligations on a broad range of financial institutions, including federal savings banks, like First Federal of Northern Michigan. These obligations include enhanced anti-money laundering programs, customer identification programs and regulations relating to private banking accounts or correspondence accounts in the United States for non-United States persons or their representatives (including foreign individuals visiting the United States).

First Federal of Northern Michigan has established policies and procedures to ensure compliance with the USA PATRIOT Act s provisions, and the impact of the USA PATRIOT Act on our operations has not been material.

**Holding Company Regulation**

First Federal of Northern Michigan Bancorp, Inc. is a unitary savings and loan holding company, subject to regulation and supervision by the Office of Thrift Supervision. The Office of Thrift Supervision has enforcement authority over First Federal of Northern Michigan Bancorp, Inc. and its non-savings institution subsidiaries. Among other things, this authority permits the Office of Thrift Supervision to restrict or prohibit activities that are determined to be a risk to First Federal of Northern Michigan.

Under prior law, a unitary savings and loan holding company generally had no regulatory restrictions on the types of business activities in which it could engage, provided that its subsidiary savings association was a qualified thrift lender. The Gramm-Leach-Bliley Act, however, restricts unitary savings and loan holding companies not existing on, or

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applied for before, May 4, 1999, to those activities permissible for financial holding companies or for multiple savings and loan holding companies. First Federal of Northern Michigan Bancorp, Inc. is not a grandfathered unitary savings and loan holding company and, therefore, is limited to the activities permissible for financial holding companies or for multiple savings and loan holding companies. A financial holding company may engage in activities that are financial in nature, including underwriting equity securities and insurance, incidental to financial activities or complementary to a financial activity. A multiple savings and loan holding company is generally limited to activities permissible for bank holding companies under Section 4(c)(8) of the Bank Holding Company Act, subject to the prior approval of the Office of Thrift Supervision, and certain additional activities authorized by Office of Thrift Supervision regulations.

Federal law prohibits a savings and loan holding company, directly or indirectly, or through one or more subsidiaries, from acquiring control of another savings institution or holding company thereof, without prior written approval of the Office of Thrift Supervision. It also prohibits the acquisition or retention of, with specified exceptions, 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 or retaining control of an institution that is not federally insured. In evaluating applications by holding companies to acquire savings institutions, the Office of Thrift Supervision must consider the financial and managerial resources and future prospects of the savings institution involved, the effect of the acquisition on the risk to the insurance fund, the convenience and needs of the community and competitive factors.

**Sarbanes-Oxley Act of 2002**

The Sarbanes-Oxley Act of 2002 was enacted in response to public concerns regarding corporate accountability. The stated goals of the Sarbanes-Oxley Act are to increase corporate responsibility, to provide for enhanced penalties for accounting and auditing improprieties at publicly traded companies, and to protect investors by improving the accuracy and reliability of corporate disclosures pursuant to the securities laws. The Sarbanes-Oxley Act generally applies to all companies that file or are required to file periodic reports with the SEC, under the Securities Exchange Act of 1934.

The Sarbanes-Oxley Act includes very specific additional disclosure requirements and new corporate governance rules requiring the SEC and securities exchanges to adopt extensive additional disclosure, corporate governance and other related rules, and mandates further studies of certain issues by the SEC. The Sarbanes-Oxley Act represents significant federal involvement in matters traditionally left to state regulatory systems, such as the regulation of the accounting profession, and to state corporate law, such as the relationship between a board of directors and management and between a board of directors and its committees.

**Federal Securities Laws**

First Federal of Northern Michigan Bancorp, Inc. s common stock is registered with the Securities and Exchange Commission under the Securities Exchange Act of 1934. First Federal of Northern Michigan Bancorp, Inc. is subject to the information, proxy solicitation, insider trader restrictions and other requirements under the Securities Exchange of 1934.

First Federal of Northern Michigan Bancorp, Inc. common stock held by persons who are affiliates (generally officers, directors and principal stockholders) of First Federal of Northern Michigan Bancorp, Inc. may not be resold without registration or unless sold in accordance with certain resale restrictions. If First Federal of Northern Michigan Bancorp, Inc. meets specified current public information requirements, each affiliate of First Federal of Northern Michigan Bancorp, Inc. is able to sell in the public market, without registration, a limited number of shares in any three-month period.

## TAXATION

**Federal Taxation**

***General.*** First Federal of Northern Michigan Bancorp, Inc. and First Federal of Northern Michigan are subject to federal income taxation in the same general manner as other corporations, with some exceptions discussed below. The following discussion of federal taxation is intended only to summarize material federal income tax matters and is not a comprehensive description of the tax rules applicable to First Federal of Northern Michigan Bancorp, Inc. and First Federal of Northern Michigan.

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***Method of Accounting***. For federal income tax purposes, First Federal of Northern Michigan currently reports its income and expenses on the accrual method of accounting and uses a tax year ending December 31 for filing its consolidated federal income tax returns. The Small Business Protection Act of 1996 eliminated the use of the reserve method of accounting for bad debt reserves by savings institutions, effective for taxable years beginning after 1995.

***Bad Debt Reserves.*** Prior to the Small Business Protection Act of 1996, First Federal of Northern Michigan was permitted to establish a reserve for bad debts for tax purposes and to make annual additions to the reserve. These additions could, within specified formula limits, be deducted in arriving at First Federal of Northern Michigan s taxable income. As a result of the Small Business Protection Act, First Federal of Northern Michigan must use the specific charge off method in computing its bad debt deduction for tax purposes.

***Taxable Distributions and Recapture.*** Prior to the Small Business Protection Act of 1996, bad debt reserves created prior to 1988 were subject to recapture into taxable income if First Federal of Northern Michigan failed to meet certain thrift asset and definitional tests. The Small Business Protection Act of 1996 eliminated these thrift-related recapture rules. However, under current law, pre-1988 reserves remain subject to tax recapture should First Federal of Northern Michigan make certain distributions from its tax bad debt reserve or cease to maintain a bank charter. At December 31, 2008, First Federal of Northern Michigan s total federal pre-1988 reserve was approximately $60,000. This reserve reflects the cumulative effects of federal tax deductions by First Federal of Northern Michigan for which no federal income tax provision has been made.

***Minimum Tax.*** The Internal Revenue Code of 1986, as amended, imposes an alternative minimum tax at a rate of 20% on a base of regular taxable income plus certain tax preferences ( alternative minimum taxable income or AMTI ). The alternative minimum tax is payable to the extent such AMTI is in excess of an exemption amount. Net operating losses can, in general, offset no more than 90% of AMTI. Certain payments of alternative minimum tax may be used as credits against regular tax liabilities in future years. First Federal of Northern Michigan has not been subject to the alternative minimum tax and has no such amounts available as credits for carryover.

***Net Operating Loss Carryovers.*** A financial institution may carry back net operating losses to the preceding two taxable years and forward to the succeeding 20 taxable years. At December 31, 2008, First Federal of Northern Michigan had a net operating loss which it may carry back and/or forward for federal income tax purposes.

***Corporate Dividends.*** We may exclude from our income 100% of dividends received from First Federal of Northern Michigan as a member of the same affiliated group of corporations.

The federal income tax returns of First Federal of Northern Michigan Bancorp, Inc. and its predecessor, Alpena Bancshares, Inc. have not been audited by the Internal Revenue Service in the last five fiscal years.

**State and Local Taxation**

During 1999, the State of Michigan enacted legislation that resulted in elimination of the Michigan single business tax by gradually phasing it out over the next 23 years. On August 9, 2006, the Michigan Legislature approved the repeal of the Michigan SBT for tax years beginning after December 31, 2007. The Michigan SBT has been replaced with the Michigan Business Tax (MBT). Financial Institutions are subject to a component of the MBT, the Financial Institutions Tax, which is based on capital rather than taxable earnings.

Other applicable state taxes include generally applicable sales, use and real property taxes.

As a Maryland business corporation, First Federal of Northern Michigan Bancorp, Inc. is required to file annual returns with the State of Maryland.

## ITEM 1A. RISK FACTORS

An investment in our common stock involves risk. You should carefully consider the risks described below and all other information contained in this annual report on Form 10-K before you decide to buy our common stock. It is possible that risks and uncertainties not listed below may arise or become material in the future and affect our business.

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**The United States Economy Is In Recession. A Prolonged Economic Downturn, Especially One Affecting Our Geographic Market Area, Could Materially Affect our Business and Financial Results.**

The United States economy entered a recession in the fourth quarter of 2007. The economy in our principal market area, Northern Michigan, is similarly in a recession. Throughout the course of 2008 and in the first quarter of 2009, economic conditions continued to worsen, due in large part to the fallout from the collapse of the sub-prime mortgage market. While we did not originate or invest in sub-prime mortgages, our lending business is tied, in large part, to the housing market. Declines in home prices, increases in foreclosures and higher unemployment have adversely affected the credit performance of real estate-related loans, resulting in the write-down of asset values. The continuing housing slump also has resulted in reduced demand for the construction of new housing, further declines in home prices, and increased delinquencies on our construction, residential and commercial mortgage loans. Further, the ongoing concern about the stability of the financial markets in general has caused many lenders to reduce or cease providing funding to borrowers. These conditions may also cause a further reduction in loan demand, and increases in our non-performing assets, net charge-offs and provisions for loan losses.

**Future Changes in Interest Rates Could Reduce Our Profits**

Our ability to make a profit largely depends on our net interest income, which could be negatively affected by changes in interest rates. Net interest income is the difference between:

the interest income we earn on our interest-earning assets, such as loans and securities; and

the interest expense we pay on our interest-bearing liabilities, such as deposits and borrowings.

The rates we earn on our assets and the rates we pay on our liabilities are generally fixed for a contractual period of time. Like many savings institutions, our liabilities generally have shorter contractual maturities than our assets. This imbalance can create significant earnings volatility, because market interest rates change over time. In a period of rising interest rates, the interest income earned on our assets may not increase as rapidly as the interest paid on our liabilities. In a period of declining interest rates, the interest income earned on our assets may decrease more rapidly than the interest paid on our liabilities, as borrowers prepay mortgage loans, and mortgage-backed securities and callable investment securities are called or prepaid thereby requiring us to reinvest those cash flows at lower interest rates. See Management s Discussion and Analysis of Financial Condition and Results of Operations Management of Interest Rate Risk.

In addition, changes in interest rates can affect the average life of loans and mortgage-backed and related securities. A reduction in interest rates results in increased prepayments of loans and mortgage-backed and related securities, as borrowers refinance their debt in order to reduce their borrowing costs. This creates reinvestment risk, which is the risk that we may not be able to reinvest prepayments at rates that are comparable to the rates we earned on the prepaid loans or securities. Additionally, increases in interest rates may decrease loan demand and/or make it more difficult for borrowers to repay adjustable-rate loans.

Changes in interest rates also affect the current fair value of our interest-earning securities portfolio. Generally, the value of securities moves inversely with changes in interest rates. At December 31, 2008, the fair value of our available-for-sale securities portfolio, consisting of agency securities, mortgage-backed securities, corporate debt obligations and municipal obligations, totaled $29.6 million. Unrealized net gains on these available-for-sale securities totaled $511,000 at December 31, 2008 and are reported as a separate component of stockholders equity. Decreases in the fair value of securities available for sale in future periods would have an adverse effect on stockholders equity.

We evaluate interest rate sensitivity using income simulation models that estimate the change in our net interest income over a range of interest rate scenarios. Net income at risk measures the risk of a decline in earnings due to potential short-term and long term changes in interest rates. At December 31, 2008, the latest date for which such information is available, in the event of an immediate 200 basis point increase in interest rates, the model projects that we would experience an 8.0% decrease in net interest income over the following 12 months.

**As a Result of Our Previous Emphasis on Originating Commercial Real Estate and Commercial Business Loans, Our Credit Risk Has and Will Continue to Increase. Continued Weakness or a Deeper Downturn in the Real Estate Market and Local Economy Could Adversely Affect Our Earnings.**

At December 31, 2008, our portfolio of commercial real estate loans totaled $43.8 million, or 22.1% of our total loans, and our portfolio of commercial business loans totaled $30.2 million, or 15.2% of our total loans. These loans have increased as a percentage of our total loan portfolio in recent years and generally have more risk than one- to four-family residential mortgage loans. Because the repayment of commercial real estate and commercial business loans depends on the successful management and operation of the borrower s properties or related businesses, repayment of such loans can

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be affected by adverse conditions in the real estate market or the local economy. Many of our borrowers also have more than one commercial real estate or commercial business loan outstanding with us. Consequently, an adverse development with respect to one loan or one credit relationship can expose us to significantly greater risk of loss compared to an adverse development with respect to a one- to four-family residential mortgage loan. Finally, if we foreclose on a commercial real estate or commercial business loan, our holding period for the collateral, if any, typically is longer than for one- to four-family residential mortgage loans because there are fewer potential purchasers of the collateral. Because we plan to continue to increase our originations of these loans, it may be necessary to increase the level of our allowance for loan losses because of the increased risk characteristics associated with these types of loans. Any such increase to our allowance for loan losses would adversely affect our earnings.

**If Our Allowance for Loan Losses is Not Sufficient to Cover Actual Loan Losses, Our Earnings Could Decrease.**

We make various assumptions and judgments about the collectibility of our loan portfolio, including the creditworthiness of our borrowers and the value of the real estate and other assets serving as collateral for the repayment of many of our loans. In determining the amount of the allowance for loan losses, we review our loans and our loss and delinquency experience, and we evaluate economic conditions. If our assumptions are incorrect, our allowance for loan losses may not be sufficient to cover losses inherent in our loan portfolio, resulting in additions to our allowance. Our allowance for loan losses was 2.85% of total loans and 40.90% of non-performing assets at December 31, 2008, compared to 1.95% of total loans and 38.53% of non-performing assets at December 31, 2007. Material additions to our allowance could materially decrease our net income.

In addition, bank regulators periodically review our allowance for loan losses and may require us to increase our provision for loan losses or recognize further loan charge-offs. Any increase in our allowance for loan losses or loan charge-offs as required by these regulatory authorities may have a material adverse effect on our financial condition and results of operations.

**Future Legislative or Regulatory Actions Responding to Financial and Market Weakness Could Affect Us Adversely. There Can Be No Assurance that Actions of the U.S. Government, Federal Reserve and Other Governmental and Regulatory Bodies For the Purpose of Stabilizing the Financial Markets Will Achieve the Intended Effect.**

In response to the financial crises affecting the banking system and financial markets, the U.S. Congress has passed legislation and the U.S. Treasury has promulgated programs designed to purchase assets from, provide equity capital to, and guarantee the liquidity of the financial services industry. Specifically, Congress adopted the Emergency Economic Stabilization Act of 2008, under which the U.S. Treasury has the authority to expend up to $700 billion to assist in stabilizing and providing liquidity to the U.S. financial system. On October 14, 2008, the U.S. Treasury announced the Capital Purchase Program, under which it will purchase up to $250 billion of non-voting senior preferred shares of certain qualified financial institutions in an attempt to encourage financial institutions to build capital to increase the flow of financing to businesses and consumers and to support the economy. In addition, Congress temporarily increased FDIC deposit insurance from $100,000 to $250,000 per depositor through December 31, 2009. The FDIC has also announced the creation of the Temporary Liquidity Guarantee Program which is intended to strengthen confidence and encourage liquidity in financial institutions by temporarily guaranteeing newly issued senior unsecured debt of participating organizations and providing full insurance coverage for noninterest-bearing transaction deposit accounts (such as business checking accounts, interest-bearing transaction accounts paying 50 basis points or less and lawyers trust accounts), regardless of dollar amount until December 31, 2009. Finally, in February 2009, the American Recovery and Reinvestment Act of 2009 was enacted, which is intended to expand and establish government spending programs and provide certain tax cuts to stimulate the economy. The U.S. government continues to evaluate and develop various programs and initiatives designed to stabilize the financial and housing markets and stimulate the economy, including the U.S. Treasury s recently announced Financial Stability Plan and the recently announced foreclosure prevention program.

The potential exists for additional federal or state laws and regulations regarding lending and funding practices and liquidity standards, and bank regulatory agencies are expected to be active in responding to concerns and trends identified in examinations, and the issuance of many formal enforcement orders is expected. Actions taken to date, as

well as potential actions, may not have the beneficial effects that are intended, particularly with respect to the extreme levels of volatility and limited credit availability currently being experienced. In addition, new laws, regulations, and other regulatory changes will increase our costs of regulatory compliance and of doing business, and otherwise affect our operations. Our FDIC insurance premiums have increased, and are expected to continue to increase, because market developments have significantly depleted the insurance fund of the FDIC and reduced the ratio of reserves to insured deposits. New laws, regulations, and other regulatory changes, along with negative developments in the financial services industry and the credit markets, may significantly affect the markets in which we do business, the markets for and value of our loans and investments, and our ongoing operations, costs and profitability.

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**Lack of Consumer Confidence in Financial Institutions May Decrease Our Level of Deposits.**

Our level of deposits may be affected by lack of consumer confidence in financial institutions, which has resulted in large numbers of depositors unwilling to maintain deposits that are not insured by the Federal Deposit Insurance Corporation. In some cases, depositors have withdrawn deposits and invested uninsured funds in investments perceived as being more secure, such as securities issued by the U.S. Treasury. These consumer preferences may force us to pay higher interest rates to retain deposits and may constrain liquidity as we seek to meet funding needs caused by reduced deposit levels.

**Strong Competition Within Our Market Area May Limit Our Growth and Profitability.**

We face substantial competition in all phases of our operations from a variety of different competitors. Our future growth and success will depend on our ability to compete effectively in this highly competitive environment. We compete for deposits, loans and other financial services with numerous Michigan-based banks, thrifts, credit unions and other financial institutions as well as other entities which provide financial services. Some of these competitors are not subject to the same regulatory restrictions, have advantages of scale due to their size, or have cost advantages due to their tax status. Our profitability depends upon our continued ability to successfully compete in our market area. The greater resources and deposit and loan products offered by some of our competitors may limit our ability to increase our interest-earning assets.

**Recent Negative Developments in the Financial Services Industry And the Credit Markets May Subject Us to Additional Regulation.**

As a result of the recent financial crisis, the potential exists for the promulgation of new federal or state laws and regulations regarding lending and funding practices and liquidity standards, and bank regulatory agencies are expected to be active in responding to concerns and trends identified in examinations, which are expected to result in the issuance of many formal enforcement orders. Negative developments in the financial services industry and the credit markets, and the impact of new legislation in response to these developments, may negatively affect our operations by restricting our business operations, including our ability to originate or sell loans and pursue business opportunities. Compliance with such regulation also will likely increase our costs.

**Our Future Growth May Require Us to Raise Additional Capital in the Future, But That Capital May Not Be Available When It Is Needed.**

We are required by regulatory authorities to maintain adequate levels of capital to support our operations. We believe that our current capital levels will satisfy our regulatory requirements for the foreseeable future. We may at some point, however, need to raise additional capital to support our continued growth. Our ability to raise additional capital will depend, in part, on conditions in the capital markets at that time, which are outside our control, and on our financial performance. Accordingly, we may be unable to raise additional capital, if and when needed, on terms acceptable to us, or at all. If we cannot raise additional capital when needed, our ability to further expand our operations through internal growth and acquisitions could be materially impaired. In addition, if we decide to raise additional equity capital, your interest in our common stock could be diluted.

**Our Expenses Will Increase as a Result of Increases in FDIC Insurance Premiums.**

The FDIC imposes an assessment against financial institutions for deposit insurance. This assessment is based on the risk category of the institution and currently ranges from 5 to 43 basis points of the institution s deposits. On February 27, 2009, the FDIC issued a final rule that increases the current deposit insurance assessment rates to a range from 12 to 45 basis points beginning April 1, 2009. We expect this increase to add approximately $150,000 to our non-interest expenses in 2009 and beyond. Additionally, the FDIC has issued an interim rule that would impose a special 20 basis points assessment on deposits as of June 30, 2009, which would be paid on September 30, 2009. This special assessment would add approximately $360,000 in non-interest expense in 2009.

**We Recently Suspended our Common Stock Cash Dividend.**

We suspended our quarterly dividend effective for the ended December 31, 2008. We are dependent primarily upon the Bank for our earnings and funds to pay dividends on our common stock. The payment of dividends also is subject to legal and regulatory restrictions. Any reinstatement of dividends in the future will depend, in large part, on the Bank s earnings, capital requirements, financial condition and other factors considered by our Board of Directors.

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**ITEM 1B. UNRESOLVED STAFF COMMENTS**

None

**ITEM 2. PROPERTY**

As of December 31, 2008, First Federal of Northern Michigan owned its main office and all of its branch offices. At December 31, 2008, the aggregate net book value of our premises and equipment was $7.1 million, net of $4.5 million of depreciation. The following is a list of our locations:

**Main Office**

100 South Second Avenue
Alpena, Michigan 49707

**Branch Offices**

300 South Ripley Boulevard
Alpena, Michigan 49707

6232 River Street
Alanson, Michigan 49706

101 South Main Street
Cheboygan, Michigan 49721

1000 South Wisconsin
Gaylord, Michigan 49735

2885 South County Road #489
Lewiston, Michigan 49756

625 North Williams Street (2)
Mancelona, Michigan 49659

308 North Morenci
Mio, Michigan 48647

201 North State Street
Oscoda, Michigan 48750

11874 U.S. 23 South (1)
Ossineke, Michigan 49766

**InsuranCenter of Alpena**

123 S. Second Avenue (3)
Alpena, Michigan 49707

(1) This branch was closed on February, 16, 2007. The property has been listed for sale.

(2) This branch was closed on February 1, 2008. The property sold in March, 2008.

(3) The majority of the assets of ICA were sold on February 27, 2009, however the Company still owns this property.

**ITEM 3. LEGAL PROCEEDINGS**

The Company and the Bank are periodically involved in claims and lawsuits that are incident to their business. At December 31, 2008, neither the Company nor the Bank was involved in any claims or lawsuits material to their respective businesses.

**ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

No matters were submitted during the fourth quarter of the year ended December 31, 2008 to a vote of security holders.

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## PART II

**ITEM 5. MARKET FOR COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND SMALL BUSINESS ISSUER PURCHASES OF EQUITY SECURITIES**

(a) First Federal of Northern Michigan Bancorp, Inc. s common stock is traded on the Nasdaq Global Market under the symbol FFNM.

As of December 31, 2008 there were 2,884,249 shares of First Federal of Northern Michigan Bancorp, Inc. common stock outstanding. At December 31, 2008, First Federal of Northern Michigan Bancorp, Inc. had approximately 600 stockholders of record. The remaining information required by this item is incorporated by reference to Exhibit 13, the Company s Annual Report to Stockholders.

(b) Not Applicable

(c) First Federal of Northern Michigan Bancorp, Inc. did not repurchase any of its equity securities during the quarter ended December 31, 2008.

**ITEM 6. SELECTED FINANCIAL DATA**

Not applicable

**ITEM 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF PERATIONS**

Information contained in the section captioned Management s Discussion and Analysis or Plan of Operation is incorporated by reference to Exhibit 13, the Company s Annual Report to Stockholders.

**ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

Not required for Smaller Reporting Companies.

**ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA**

Information contained in the section captioned Financial Statements is incorporated by reference to Exhibit 13, the Company s Annual Report to Shareholders.

**ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE**

None

**ITEM 9A. CONTROLS AND PROCEDURES**

Not applicable.

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**ITEM 9A(T). CONTROLS AND PROCEDURES**

(a) Evaluation of Disclosure Controls and Procedures

Under the supervision and with the participation of our management, including the Company s Chief Executive Officer and Chief Financial Officer, the Company evaluated the effectiveness of the design and operation of its disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934) as of the end of the period covered by this report. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that, as of the end of the period covered by this report, the Company s disclosure controls and procedures were effective to ensure that information required to be disclosed in the reports the Company files or submits under the Securities Exchange Act of 1934 (1) is recorded, processed, summarized and reported, within the time periods specified by the SEC s rules and forms, and (2) is accumulated and communicated to the Company s management, including its principal executive and principal financial officers, as appropriate, to allow timely decisions regarding required disclosure.

(b) Management s Annual Report on Internal Control over Financial Reporting

Management of First Federal of Northern Michigan Bancorp, Inc. and subsidiaries (the Company ) is responsible for establishing and maintaining adequate internal control over financial reporting. The Company s system of internal control is designed under the supervision of management, including our Chief Executive Officer and Chief Financial Officer, to provide reasonable assurance regarding the reliability of our financial reporting and the preparation of the Company s financial statements for external reporting purposes in accordance with U.S. generally accepted accounting principles ( GAAP ).

Our internal control over financial reporting includes policies and procedures that pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect transactions and dispositions of assets; provide reasonable assurances that transactions are recorded as necessary to permit preparation of financial statements in accordance with GAAP, and that receipts and expenditures are made only in accordance with the authorization of management and the Board of Directors; and 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 our financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Projections on any evaluation of effectiveness 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 policies and procedures may deteriorate.

As of December 31, 2008, management assessed the effectiveness of the Company s internal control over financial reporting based upon the framework established in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based upon its assessment, management believes that the Company s internal control over financial reporting as of December 31, 2008 is effective using these criteria. This annual report does not include an attestation report of the Company s registered public accounting firm regarding internal control over financial reporting. Management s report was not subject to attestation by the Company s registered public accounting firm pursuant to temporary rules of the Securities and Exchange Commission that permit the Company to provide only management s report in this annual report.

(c) Changes in Internal Control over Financial Reporting

There has been no change in the Company s internal control over the financial reporting during the Company s fourth quarter of fiscal year 2008 that has materially affected, or is reasonably likely to materially affect, the Company s internal control over financial reporting.

**ITEM 9B. OTHER INFORMATION**

None.

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## PART III

**ITEM 10. DIRECTORS, EXECUTIVE OFFICERS, AND CORPORATE GOVERNANCE**

Information concerning directors and executive officers is incorporated herein by reference from the Company s Proxy Statement, specifically the section captioned Proposal I Election of Directors.

**ITEM 11. EXECUTIVE COMPENSATION**

Information concerning executive compensation is incorporated herein by reference from the Company s Proxy Statement, specifically the section captioned Proposal I Election of Directors.

**ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS**

Information concerning security ownership of certain owners and management is incorporated herein by reference from the Company s Proxy Statement, specifically the Section captioned Proposal I Election of Directors.

**ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS**

Information concerning relationships and transactions is incorporated herein by reference from the Company s Proxy Statement, specifically the section captioned Transactions with Certain Related Persons .

**ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES**

Information concerning principal accountant fees and services is incorporated herein by reference to the Company s Proxy Statement, specifically the section captioned Proposal II Ratification of Appointment of Auditors.

**ITEM 15. EXHIBITS**

The exhibits filed as a part of this form 10-K are as follows:

3.1 Articles of Incorporation of First Federal of Northern Michigan Bancorp, Inc.*

3.2 Bylaws of First Federal of Northern Michigan Bancorp, Inc.*

4 Form of Common Stock Certificate of First Federal of Northern Michigan Bancorp, Inc.*

10.1 Change in Control Agreements*

10.2 1996 Stock Option Plan*

10.3 1996 Recognition and Retention Plan*

10.4 2006 Stock-Based Incentive Plan**

13 Annual Report to Shareholders

14 Code of Ethics ***

21 Subsidiaries of Registrant

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23 Consent of Plante & Moran PLLC

31.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

31.2 Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

32.1 Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

32.2 Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

* Incorporated by reference to the Registration Statement on Form SB-2 of First Federal of Northern Michigan Bancorp, Inc. (Registration No. 333-121178), originally filed with the Commission on December 10, 2004.

** Incorporate by reference to the Definitive Proxy materials filed on April 10, 2006 (No. 000-31957).

*** Incorporated by reference to the Annual Report on Form 10-K of Alpena Bancshares, Inc. filed with the Commission on March 30, 2004 (Registration No. 000-31957).

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**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.

**FIRST FEDERAL OF NORTHERN MICHIGAN BANCORP, INC.**

By: /s/Michael W. Mahler

Michael W. Mahler
Chief Executive Officer

Date: March 31, 2009

Pursuant to the requirements of the Securities Exchange of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

By: /s/Michael W. Mahler

Michael W. Mahler, Director and
Chief Executive Officer
(Principal Executive Officer)
Date: March 31, 2009

By: /s/Amy E. Essex

Amy E. Essex, Chief Financial Officer, Treasurer and Corporate Secretary
(Principal Financial and Accounting Officer)
Date: March 31, 2009

By: /s/Martin A. Thomson

Martin A. Thomson, Chairman

Date: March 31, 2009

By: /s/Keith Wallace

Keith Wallace, Director

Date: March 31, 2009

By: /s/GaryVanMassenhove

Gary VanMassenhove, Director

Date: March 31, 2009

By: /s/Thomas R. Townsend

Thomas R. Townsend, Director

Date: March 31, 2009

By: /s/James C. Rapin

James C. Rapin, Director

Date: March 31, 2009