UNIVERSITY BANCORP INC /DE/
Form 10QSB
November 14, 2006
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington D.C. 20549

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FORM 10-QSB

(Mark One)

[X] Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended September 30, 2006

OR

[] 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 0-16023

UNIVERSITY BANCORP, INC.
(Exact name of registrant as specified in its charter)

| | |
|---|---|
| Delaware | 38-2929531 |
| (State of incorporation) | (IRS Employer Identification Number) |

| | |
|---|---|
| 2015 Washtenaw, Ann Arbor, Michigan | 48104 |
| (Address of principal executive offices) | (Zip Code) |

Registrant's telephone number, including area code: (734) 741-5858

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

X Yes ___No

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

_ Yes X No

State the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Common Stock, $0.01 par value outstanding at November 14, 2006: 4,248,378 shares

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The information furnished in these interim statements reflects all adjustments and accruals, which are in the opinion of management, necessary for a fair statement of the results for such periods. The results of operations in the interim statements are not necessarily indicative of the results that may be expected for the full year.

Part I. - Financial Information
Item 1.- Unaudited Consolidated Financial Statements

UNIVERSITY BANCORP, INC. AND SUBSIDIARIES
Consolidated Balance Sheets
September 30, 2006 and December 31, 2005

| ASSETS | | (Unaudited) September 30, 2006 | |
|---|---|---|---|
| Cash and due from banks | $ | 8,690,556 | $ |
| Securities available for sale, at market | | 709,553 | |
| Federal Home Loan Bank Stock | | 791,200 | |
| Loans and financings held for sale, at the lower of cost or market | | 2,101,919 | |
| Loans and financings | | 48,061,066 | |
| Allowance for loan and financing losses | | (457,511) | |
| Loans, net | | 47,603,555 | |
| Premises and equipment, net | | 2,738,557 | |
| Mortgage servicing rights, net | | 1,525,282 | |
| Real estate owned, net | | 496,290 | |
| Accounts receivable | | 63,987 | |
| Accrued interest and profit receivable | | 241,370 | |
| Prepaid expenses | | 278,561 | |
| Goodwill | | 103,914 | |
| Other assets | | 497,607 | |
| TOTAL ASSETS | $ | 65,842,351 | $ |

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UNIVERSITY BANCORP, INC. AND SUBSIDIARIES
Consolidated Balance Sheets (continued)
September 30, 2006 and December 31, 2005

| LIABILITIES AND STOCKHOLDERS' EQUITY | (Unaudited) September 30, 2006 |
|---|---|
| Liabilities: | |
| Deposits: | |
| Demand - non interest bearing | $ 4,688,782 |
| Demand - interest bearing and profit sharing | 40,042,329 |
| Savings | 277,973 |
| Time | 12,006,387 |
| Total Deposits | 57,015,471 |
| Accounts payable | 694,988 |
| Accrued interest and profit sharing payable | 72,961 |
| Other liabilities | 154,542 |
| Total Liabilities | 57,937,962 |
| Minority Interest | 2,603,975 |
| Stockholders' equity: | |
| Preferred stock, $0.001 par value; $1,000 liquidation value; Authorized - 500,000 shares; Issued - 37,672 shares in 2006 and 27,791 shares in 2005 | 28 |
| Common stock, $0.01 par value; Authorized - 5,000,000 shares; Issued - 4,363,562 shares in 2006 and 4,263,062 shares in 2005 | 43,636 |
| Additional paid-in-capital | 6,508,601 |
| Accumulated deficit | (887,032) |
| Treasury stock - 115,184 shares in 2006 and 2005 | (340,530) |
| Accumulated other comprehensive loss, unrealized losses on securities available for sale, net | (24,299) |
| Total Stockholders' Equity | 5,300,414 |
| TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY | $ 65,842,351 |

See accompanying notes to consolidated financial statements (unaudited).

UNIVERSITY BANCORP, INC. AND SUBSIDIARIES
Consolidated Statements of Operations
For the Periods Ended September 30, 2006 and 2005
(Unaudited)

| | For the Three-Month Period Ended 2006 | 2005 |
|---|---|---|
| Interest and financing income: | | |

| | | | |
|---|---|---|---|
| Interest and fees on loans and financing income | $ 826,648 | $ 801,930 | $ |
| Interest on securities: | | | |
| U.S. Government agencies | 2,673 | 3,710 | |
| Other securities | 6,688 | 9,904 | |
| Interest on federal funds and other | 86,474 | 13,810 | |
| Total interest income and financing income | 922,483 | 829,354 | |
| Interest and profit sharing expense: | | | |
| Interest and profit sharing on deposits: | | | |
| Demand deposits | 164,436 | 121,446 | |
| Savings deposits | 713 | 1,110 | |
| Time deposits | 147,590 | 126,333 | |
| Short term borrowings | - | 28,789 | |
| Long term borrowings | - | - | |
| Total interest and profit sharing expense | 312,739 | 277,678 | |
| Net interest and financing income | 609,744 | 551,676 | |
| Provision for loan losses | 57,411 | - | |
| Net interest and financing income after provision for loan losses | 552,333 | 551,676 | |
| Other income: | | | |
| Loan servicing and sub-servicing fees | 619,158 | 441,360 | |
| Initial loan set up and other fees | 422,779 | 391,105 | |
| Gain(loss) on sale of mortgage loans | (1,474) | 92,345 | |
| Insurance and investment fee income | 43,151 | 50,062 | |
| Deposit service charges and fees | 21,762 | 27,951 | |
| Other | 92,057 | 51,193 | |
| Total other income | 1,197,433 | 1,054,016 | |

-Continued-

UNIVERSITY BANCORP, INC. AND SUBSIDIARIES
Consolidated Statements of Operations
For the Periods Ended September 30, 2006 and 2005
(Unaudited)

| | For the Three-Month Period Ended 2006 | 2005 | |
|---|---|---|---|
| Other expenses: | | | |
| Salaries and benefits | $ 851,672 | $ 736,177 | $ |

| | | | | |
|---|---|---|---|---|
| Occupancy, net | | 128,688 | | 140,816 |
| Data processing and equipment expense | | 160,042 | | 144,240 |
| Legal and audit expense | | 81,133 | | 95,639 |
| Consulting fees | | 44,259 | | 53,281 |
| Mortgage banking expense | | 61,176 | | 90,953 |
| Servicing rights amortization | | 193,610 | | (35,007) |
| Advertising | | 51,886 | | 49,148 |
| Memberships and training | | 21,235 | | 32,290 |
| Travel and entertainment | | 35,336 | | 39,337 |
| Supplies and postage | | 75,796 | | 51,020 |
| Insurance | | 35,816 | | 44,605 |
| Other operating expenses | | 142,088 | | 155,233 |
| Total other expenses | | 1,882,737 | | 1,597,732 |
| Income (loss) before income taxes | | (132,971) | | 7,960 |
| Income tax expense | | - | | - |
| Net Income (loss) | $ | (132,971) | $ | 7,960 |
| Preferred stock dividends | | 8,585 | | 6,081 |
| Net income (loss) available to common shareholders | $ | (141,556) | $ | 1,879 |
| Basic earnings/(loss) per common share | $ | (0.03) | $ | 0.00 |
| Diluted earnings/(loss) per common share | $ | (0.03) | $ | 0.00 |
| Weighted average shares outstanding - Basic | | 4,248,378 | | 4,148,878 |
| Weighted average shares outstanding - Diluted | | 4,248,378 | | 4,184,430 |

See accompanying notes to consolidated financial statements (unaudited).

UNIVERSITY BANCORP, INC. AND SUBSIDIARIES
Consolidated Statements of Comprehensive Income
For the Periods Ended September 30, 2006 and 2005
(Unaudited)

| | For the Three-Month Period Ended | |
|---|---|---|
| | 2006 | 2005 |
| Net income(loss) | $(132,971) | $7, |

| | | |
|---|---|---|
| Other comprehensive income(loss): | | |
| Unrealized gains(losses) on securities available for sale | 16,997 | (4,1 |
| Less: reclassification adjustment for accumulated gains(losses) included in net gains(losses) | - | |
| Other comprehensive income(loss), before tax effect | 16,997 | (4,1 |
| Income tax expense | - | |
| Other comprehensive income(loss), net of tax | 16,997 | (4,1 |
| Comprehensive income(loss) | $(115,974) | $3, |

See accompanying notes to consolidated financial statements (unaudited).

UNIVERSITY BANCORP, INC. AND SUBSIDIARIES
Consolidated Statements of Cash Flows
For the Nine-Month Periods Ended September 30, 2006 and 2005
(Unaudited)

| | 2 |
|---|---|
| Operating activities: | |
| Net income (loss) | $ |
| Adjustments to reconcile net income (loss) to net cash provided by operating activities: | |
| Depreciation | |
| Amortization | |
| Provision for loan losses | |
| Net gain on mortgage loan sales | |
| Net accretion on investment securities | |
| Gain on the sale of fixed assets | |
| Gain on the sale of other real estate owned | |
| Originations of mortgage loans | |
| Proceeds from mortgage loan sales | |
| Non-employee stock awards | |
| Change in: | |
| Real estate owned | |
| Other assets | |
| Other liabilities | |
| Net cash provided by operating activities | |
| Investing activities: | |

| | |
|---|---|
| Proceeds from maturities and pay downs of securities available for sale | |
| Redemption of FHLB Stock | |
| Loans granted, net of repayments | |
| Proceeds from sale of other real estate | |
| Premises and equipment expenditures | |
| | --------- |
| Net cash used in investing activities | |
| | --------- |

-Continued-

UNIVERSITY BANCORP, INC. AND SUBSIDIARIES
Consolidated Statements of Cash Flows
For the Nine-Month Periods Ended September 30, 2006 and 2005
(Unaudited)

| | |
|---|---|
| | --------- |
| Financing activities: | |
| Net increase in deposits | |
| Net decrease in short-term borrowings | |
| Principal payments on long-term borrowings | |
| Issuance of preferred stock | |
| Issuance of common stock | |
| Dividends on preferred stock | |
| | --------- |
| Net cash provided by financing activities | |
| | --------- |
| Net change in cash and cash equivalents Cash and cash equivalents: | |
| Beginning of period | |
| | --------- |
| End of period | $ |
| | ========= |
| Supplemental disclosure of cash flow information: | |
| Cash paid for interest | $ |
| Supplemental disclosure of non-cash transactions: | |
| Mortgage loans converted to other real estate owned | $ |

See accompanying notes to consolidated financial statements (unaudited).

UNIVERSITY BANCORP, INC. AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

(1) General

See Note 1 of the Financial Statements incorporated by reference in the Company's 2005 Annual Report on Form 10-K for a summary of the Company's significant accounting policies.

The unaudited financial statements included herein were prepared from the books of the Company in accordance with generally accepted accounting principles and reflect all adjustments which are, in the opinion of management, of a normal recurring nature and necessary to provide a fair statement of the results of operations and financial position for the interim periods. Such financial statements generally conform to the presentation reflected in the Company's 2005 Annual Report on Form 10-K. The current interim periods reported herein are included in the fiscal year subject to independent audit at the end of the year.

Basic earnings per share represents income available to common stockholders divided by the weighted average number of common shares outstanding during the period. Diluted earnings per share reflects additional common shares that would have been outstanding if dilutive potential common shares had been issued, as well as any adjustment to income that would result from the assumed issuance. Potential common shares that may be issued by the Corporation relate solely to outstanding stock options, and are determined using the treasury stock method. Earnings per common share have been computed based on the following:

| | For the Three-Month Period Ended September 30, | |
|---|---|---|
| | 2006 | 2005 |
| Net Income (loss) | $(132,971) | $7 |
| Less: Preferred stock dividends | 8,585 | 6 |
| Net income(loss) applicable to common stock | $(141,556) | $1 |
| Weighted average number of common shares outstanding | 4,248,378 | 4,148 |
| Effect of dilutive options | - | 35 |
| Average number of common shares outstanding used to calculate diluted earnings per common share | 4,248,378 | 4,184 |

(2) Investment Securities

The Bank's available-for-sale securities portfolio at September 30, 2006 had a net unrealized loss of approximately $24,299 as compared with a net unrealized loss of approximately $34,721 at December 31, 2005.

Securities available for sale at September 30, 2006:

| | Amortized Cost | Unrealized Gains | Losses | Fair Value |
|---|---|---|---|---|
| U.S. agency mortgage-backed securities | $733,852 | $ - | $(24,299) | $709,553 |
| | ======= | ======= | ======== | ======= |

Securities available for sale at December 31, 2005:

| | Amortized Cost | Unrealized Gains | Losses | Fair Value |
|---|---|---|---|---|
| U.S. agency mortgage-backed securities | $868,483 | $ - | $(34,721) | $833,762 |
| | ======= | ===== | ======== | ======= |

(3) Stock options

The Company has adopted SFAS No. 123(R), "Share-Based Payment", which is a revision of SFAS No. 123, "Accounting for Stock Based Compensation", and supersedes APB Opinion No. 25, "Accounting for Stock Issued to Employees", and was issued in December 2004. The revisions require that the compensation cost relating to share-based payment transactions be recognized in the financial statements. That cost will be measured based on the fair value of the equity or liability instruments issued. For the nine-months ended September 30, 2006, the Company recorded $19,644 of compensation expense related to stock options.

Prior to the 2006 year, the Company adopted the disclosure-only provisions of SFAS No. 123. Accordingly, if the Company had elected to recognize compensation cost based on the fair value of the options at grant date, the Company's earnings and earnings per share from continuing operations, assuming dilution, for the nine-month period ended September 30, 2005 would have been the pro forma amounts indicated below:

| | Nine-months ended September 30, 2005 |
|---|---|
| Net Income (Loss) applicable to Common Stock: | |
| As reported: | $102,572 |
| Compensation expense | 2,989 |
| Pro forma | $99,583 |
| Net earnings per share: | |
| As reported: | |
| Basic | $0.02 |
| Diluted | $0.02 |
| Pro forma: | |
| Basic | $0.02 |
| Diluted | $0.02 |

(4) Issuance of Stock

In April, 2006, the Company agreed to modify a relationship with a company that assisted in the development of the Islamic Banking subsidiary and products.

Under the original agreement, University Islamic Financial Corporation was to pay a share of revenue earned from all future mortgage alternative products sold in the secondary market. University Islamic Financial Corporation agreed to pay this company $100,000 in cash and the Company paid 100,500 shares of University Bancorp, Inc. common stock and fully vested stock options totaling 48,563 with a strike price starting at $2.50 and increasing to $3.50 through June 30, 2015

to eliminate this provision in the agreement, as well as to acquire the firm providing trustee services for some of the Islamic financings. By modifying the agreement, management believes University Islamic Financial will materially reduce future expenses related to the agreement. The value of the shares expensed in the second quarter totaled $241,822.

(5) Income Taxes

Income tax expense was $0 for the nine-months ended September 30, 2006 and 2005. The effective tax rate was 0% for both nine-month periods ended September 30, 2006 and 2005 due to existence of loss carry forwards resulting from prior years' net operating losses. At September 30, 2006, the Company had a $120,000 deferred tax asset. This asset represents a loss carry forward that is expected to be realized. At December 31, 2005, the Company had a tax deferred asset of $100,000 based on expected realization of loss carry forwards.

(6) Recently Enacted Accounting Pronouncements

Financial Accounting Standards Board's Final Interpretation No. 48,"Accounting for Uncertainty in Income Taxes" ("FIN 48"). This interpretation was issued on July 13, 2006. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in the financial statements in accordance with SFAS No. 109, "Accounting for Income Taxes." This interpretation provides guidance on the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. Further, FIN 48 provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosures and transition. This interpretation is effective for fiscal years beginning after December 15, 2006. The cumulative effects, if any, of applying FIN 48 will be recorded as an adjustment to retained earnings as of the beginning of the period of adoption.

Financial Accounting Standards Board Statement No. 156 - Accounting for Servicing of Financial Assets. This Statement amends FASB Statement No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities, with respect to the accounting for separately recognized servicing assets and servicing liabilities. This standard requires all separately recognized servicing assets and liabilities to be initially measured at fair value and either amortized over the period of estimated servicing income and assessed for impairment each reporting period, or measured at fair value each reporting period with changes in fair value reported in earnings the period in which changes occur. This standard is effective for fiscal years beginning after September 15, 2006.

The Company is in the process of evaluating the expected effect of these pronouncements and is currently unable to determine the impact, if any, that they may have on its results of operations, financial position and cash flows.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

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This report includes "forward-looking statements" as that term is used in the securities laws. All statements regarding our expected financial position, business and strategies are forward-looking statements. In addition, the words "anticipates," "believes," "estimates," "seeks," "expects," "plans," "intends," and similar expressions, as they relate to us or our management, are intended to identify forward-looking statements. The presentation and discussion of the provision and allowance for loan losses and statements concerning future profitability or future growth or increases, are examples of inherently forward looking statements in that they involve judgments and statements of belief as to the outcome of future events. Our ability to predict results or the actual effect of future plans or strategies is inherently uncertain. Factors which could have a material adverse affect on our operations and our future prospects include, but are not limited to, changes in: interest rates, general economic conditions, legislative/regulatory changes, monetary and fiscal policies of the U.S. Government, including policies of the U.S. Treasury and the Federal Reserve Board, the quality or composition of the loan or investment portfolios, demand for loan products, deposit flows, competition, demand for financial services in our market area and accounting principles, policies and guidelines. These risks and uncertainties should be considered in evaluating forward-looking statements and undue reliance should not be placed on such statements. Further information concerning us and our business, including additional factors that could materially affect our financial results, is included in our other filings with the Securities and Exchange Commission.

SUMMARY

Third quarter 2006 compared to third quarter 2005

The net loss for the Company for the third quarter of 2006 was $132,971 versus net income of $7,960 for the same period last year.

Community Banking reported a net loss of $95,000 during the current year's third quarter as opposed to a net loss of $101,000 from the year before. The Bank's subsidiary, Midwest Loan Services reported a net loss of $11,000 for the third quarter of 2006 as compared to net income of $145,000 for the same period in 2005. Income at Midwest was negatively impacted in the third quarter of 2006 by a $150,000 impairment charge against the mortgage servicing rights portfolio. At the end of the quarter, the mortgage rates decreased, thus affecting the value of the portfolio.

Nine-months ended September 30, 2006 compared to nine-months ended September 30, 2005

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The Company's net loss for the nine-months of 2006 was $347,237 versus a net income of $112,063 for the same period last year.

Earnings during 2006 were restrained by start-up expenses at University Islamic Financial Corporation and a settlement agreement with a company that assisted in the development of the Islamic subsidiary and products. Community Banking reported a loss of $261,000 during the nine-months ended September 30, 2006 compared to a net loss of $58,000 during the same period in 2005. Within the Corporate Office a large contract modification expense increased the year to date loss in 2006 to $324,000 from a net loss of $51,000 in 2005, as in April 2006, the Company agreed to modify a relationship with a company that assisted in the development of the Islamic Banking subsidiary and products. Under the original agreement, University Islamic Financial Corporation was to pay a share of revenue earned from all future mortgage alternative products sold in the secondary market. University Islamic Financial Corporation agreed to pay this company $100,000 in cash and the Company paid 100,500 shares of University Bancorp, Inc. common stock and stock options totaling 48,563 with a strike price starting at $2.50 and increasing to $3.50 through June 30, 2015 to eliminate this provision in the agreement, as well as to acquire the firm providing trustee services for some of the Islamic financings. By modifying the agreement, the Company will materially reduce future expenses related to the agreement.

The following table summarizes the pre-tax income (loss) of each profit center of the Company for the three and nine-months ended September 30, 2006 and 2005 (in thousands):

Pre-tax income (loss) summary for the three and nine-months ended September 30, 2006:

| | Three-Months | Nine-Months |
|---|---|---|
| Community Banking | $(95) | $ (261) |
| Midwest Loan Services | (11) | 238 |
| Corporate Office | (27) | (324) |
| Total | $ (133) | $ (347) |

Pre-tax income (loss) summary for the three and nine months ended September 30, 2005:

| | Three-Months | Nine-Months |
|---|---|---|
| Community Banking | $(101) | $ (58) |
| Midwest Loan Services | 145 | 221 |
| Corporate Office | (36) | (51) |
| Total | $ 8 | $ 112 |

RESULTS OF OPERATIONS

Net interest and financing income

Net interest and financing income increased 10.5% to $609,744 for the three-months ended September 30, 2006 from $551,676 for the three-months ended September 30, 2005. Net interest and profit income rose because of an increase in earning assets and an increase in the net interest margin.

Net interest and financing income increased 12.3% to $1,917,795 for the nine-months ended September 30, 2006 from $1,707,655 for the nine-months ended September 30, 2005. Net interest and financing income increased from a year ago as a result of an increase in earning assets.

Interest and financing income

Interest and financing income increased 11.2% to $922,483 for the quarter ended September 30, 2006 from $829,354 for the quarter ended September 30, 2005. An increase in the average balance of earning assets of $7,427,605 was a major factor in the increase in interest income. The average volume of interest and profit earning assets increased to $56,409,065 for the quarter ended September 30, 2006 from $48,981,460 for the same 2005 period. The growth in earning assets occurred in real estate loan and financings and federal funds and bank deposit categories. The overall yield on total interest and profit bearing assets decreased to 6.49% for the quarter ended September 30, 2006 as compared to 6.72% for the same 2005 period. This decrease occurred despite an increase in the prime and general federal lending rate throughout the period after September 30, 2005. This This decrease resulted primarily due to liquid funds being invested overnight in accounts earning rates lower than competing assets such as loans.

Interest and financing income increased 15.9% to $2,834,083 for the nine-months ended September 30, 2006 from $2,444,448 for the nine-months ended September 30, 2005. This increase resulted from an increase in the volume of average earning assets. The average volume of interest earning assets increased to $56,646,689 for the nine-months ended September 30, 2006 from $47,696,573 for the same 2005 period. The overall yield on total interest and profit bearing assets decreased to 6.69% for the nine-month period ended September 30, 2006 as compared to 6.85% for the same 2005 period. The decrease occurred despite an increase in the prime and general federal lending rate throughout the period after September 30, 2005. This decrease resulted primarily due to liquid funds being invested overnight in accounts earning rates lower than competing assets such as loans.

Interest and Profit Sharing Expense

Interest and profit sharing expense increased 12.6% to $312,739 for the three-months ended September 30, 2006 from $277,678 for the same 2005 period. The increase was due principally to an increase in interest and profit bearing liabilities and a slight increase in the rates paid on those liabilities. The average volume of interest and profit bearing liabilities increased to $52,598,462 from $47,116,919 in the same period in 2005. The cost of funds increased to 2.36% for the three-months ended September 30, 2006 from 2.34% for the same 2005 period.

Interest and profit sharing expense increased 24.4% to $916,288 for the nine-months ended September 30, 2006 from $736,793 for the same 2005 period. The rise in interest expense was due to an increase in the rate on and volume of average interest bearing liabilities. The rate increased to 2.37% for the nine-months ended September 30, 2006 from 2.15% for the same 2005 period. In 2006, the rates on deposits

were higher than in the nine-month period in 2005. The average volume of interest and profit bearing liabilities increased to $51,585,502 for the nine-months ended September 30, 2006 from $45,772,523 for the same 2005 period.

MONTHLY AVERAGE BALANCE SHEET AND INTEREST MARGIN ANALYSIS

The following tables summarizes monthly average balances, revenues from earning assets, expenses of interest bearing and profit sharing liabilities, their associated yield or cost and the net return on earning assets for the three-months and nine-months ended September 30, 2006 and 2005.

| | Three-Months Ended | Three-M |
|---|---|---|
| | September 30, 2006 | Septem |

| | Average Balance | Interest Inc / Exp | Average Yield (1) | Average Balance |
|---|---|---|---|---|
| Interest and Profit Earning Assets: | | | | |
| Commercial Loans | 17,258,545 | 318,208 | 7.31% | 17,131 |
| Real Estate Loans | 29,863,476 | 487,343 | 6.47% | 26,459 |
| Installment/Consumer Loans | 1,141,044 | 21,097 | 7.34% | 1,937 |
| Total Loans | 48,263,065 | 826,648 | 6.80% | 45,528 |
| Investment Securities | 1,529,651 | 9,361 | 2.43% | 1,886 |
| Fed. Funds & Bank Deposits | 6,616,349 | 86,474 | 5.19% | 1,565 |
| Total Interest and Profit Earning Assets | 56,409,065 | 922,483 | 6.49% | 48,981 |
| Interest Bearing and Profit Sharing Liabilities: | | | | |
| Deposit Accounts: | | | | |
| Demand | 22,921,149 | 33,117 | 0.57% | 10,463 |
| Savings | 283,579 | 713 | 1.00% | 444 |
| Time | 11,027,071 | 147,590 | 5.31% | 14,542 |
| Money Market | 18,366,663 | 131,319 | 2.84% | 18,714 |
| Short-term Borrowings | - | - | 0.00% | 2,952 |
| Long-term Borrowings | - | - | 0.00% | |
| Total Interest and Profit Bearing Liabilities | 52,598,462 | 312,739 | 2.36% | 47,116 |
| Net Earning Assets, net interest and profit income, and net spread | 3,810,603 | 609,744 | 4.13% | 1,864 |
| Net Interest and Profit Margin | | | 4.29% | |

(1) Yield is annualized.

| | Nine-Months Ended September 30, | | | Nin |
|---|---|---|---|---|
| | 2006 | | | |
| | Average Balance | Interest Inc (Exp) | Average Yield (1) | Avera Balan |
| Interest and Profit Earning Assets: | | | | |

| | | | | |
|---|---|---|---|---|
| Loans: | | | | |
| Commercial | 7,614,754 | 1,083,598 | 8.22% | 17,0 |
| Real Estate | 30,516,440 | 1,416,992 | 6.21% | 25,8 |
| Installment/Consumer | 1,213,842 | 83,143 | 9.16% | 1,5 |
| Total Loans | 49,345,036 | 2,583,733 | 7.00% | 44,4 |
| Investment Securities | 1,640,035 | 40,355 | 3.29% | 1,9 |
| Federal Funds & Bank Deposits | 5,661,618 | 209,995 | 4.96% | 1,2 |
| Total Interest and Profit Earning Assets | 56,646,689 | 2,834,083 | 6.69% | 47,6 |
| Interest Bearing and Profit Sharing Liabilities: | | | | |
| Deposit Accounts: | | | | |
| Demand | 19,256,983 | 80,820 | 0.56% | 9,5 |
| Savings | 347,082 | 2,584 | 1.00% | 4 |
| Time | 14,201,336 | 482,125 | 4.54% | 14,2 |
| Money Market | 17,726,765 | 348,812 | 2.63% | 20,0 |
| Short-term borrowings | 53,336 | 1,947 | 4.88% | 1,4 |
| Long-term borrowings | - | - | 0.00% | |
| Total Interest and Profit Bearing Liabilities | 51,585,502 | 916,288 | 2.37% | 45,7 |
| Net Earning Assets, net interest and profit income, and net spread | 5,061,187 | 1,917,795 | 4.31% | 1,9 |
| Net Interest and Profit Margin | | | 4.53% | |

(1) Yield is annualized.

Allowance for Loan Losses

The provision for the allowance for loan losses was $106,395 for the nine-month period ended September 30, 2006 and $17,209 for the same period in 2005. The provision increased due to applying historical loss ratios to the growth in the loan portfolio and weak economic conditions in the southeastern Michigan area which increased management's estimates for future losses from economic factors. Net (charge-offs)/recoveries totaled $1,700 for the nine-month period ended September 30, 2006 as compared to $(21,327) for the same period in 2005. Illustrated below is the activity within the allowance for the nine-month period ended September 30, 2006 and 2005, respectively.

| | 2006 | 2005 |
|---|---|---|
| Balance, January 1 | $ 349,416 | $ 353,124 |
| Provision for loan losses | 106,395 | 17,209 |
| Loan charge-offs | (4,930) | (31,497) |

| | | |
|---|---|---|
| Recoveries | 6,630 | 10,170 |
| Balance, September 30 | $457,511 | $349,006 |

| | At September 30,2006 | At December 31, 2005 |
|---|---|---|
| Total loans (1) | $48,061,066 | $45,652,326 |
| Reserve for loan losses | $457,511 | $ 349,416 |
| Reserve/Loans % (1) | 0.95% | 0.76% |

The Bank's overall loan portfolio is geographically concentrated in Ann Arbor and surrounding Washtenaw County Michigan and the future performance of these loans is dependent upon the performance of this relatively limited geographical area.

The following schedule summarizes the Company's non-performing assets:

| | At September 30, 2006 | At December 31, 20 |
|---|---|---|
| Past due 90 days and over | | |
| and still accruing (1) | $98,242 | |
| Nonaccrual loans (1): | | |
| Real estate/construction loans | 133,268 | |
| Installment | - | |
| Commercial | - | |
| Subtotal | 133,268 | |
| Other real estate owned | 496,290 | |
| Total nonperforming assets | $727,800 | |

| | September 30, 2006 | At December 31, 2005 |
|---|---|---|
| Ratio of non-performing loans to total loans(1) | 0.48% | 0.77% |

| | | |
|---|---|---|
| Ratio of loans past due over 90 days and non-accrual loans to loan loss reserve | 51% | 100 |

(1) Excludes loans held for sale which are valued at the lower of cost or fair market value.

Management believes that the current allowance for loan losses is adequate to absorb losses inherent in the loan portfolio, although the ultimate adequacy of the allowance is dependent upon future economic factors beyond the Company's control. A downturn in the general nationwide economy will tend to aggravate, for example, the problems of local loan customers currently facing some difficulties, and could decrease residential home prices. A general nationwide business expansion could conversely tend to diminish the severity of any such difficulties.

Non-Interest Income

Total non-interest income increased to $1,197,433 for the three-months ended September 30, 2006 from $1,054,016 for the three-months ended September 30, 2005.

Total non-interest income increased to $3,284,422 for the nine-months ended September 30, 2006 from $3,099,479 for the nine-months ended September 30, 2005. As compared with the nine-month period in 2005, Midwest has increased its subservicing operations and income generated in this area, offsetting a decline in the initial loan set up and other fees due to a decrease in loan originations. At September 30, 2006, Midwest was subservicing 31,519 mortgages, an increase of 20.6% from 26,144 mortgages subserviced at December 31, 2005.

Non-Interest Expense

Non-interest expense increased to $1,882,737 for the three-months ended September 30, 2006 from $1,597,732 for the three-months ended September 30, 2005 primarily due to an impairment charge related to mortgage servicing rights. During the third quarter of 2006, the Company reported an impairment charge of $150,000. In 2005, the Company reversed $149,000 of a previously recorded mortgage serving rights impairment.

Non-interest expense increased to $5,443,059 for the nine-months ended September 30, 2006 from $4,677,862 for the nine-months ended September 30, 2005. In general the increase was due to start up expenses related to the Islamic banking subsidiary and a contract modification agreement where, in April 2006, the Company agreed to modify a relationship with a company that assisted in the development of the Islamic Banking subsidiary and products. The cost of this agreement in the second quarter of 2006 totaled $241,822. This amount is included in other expense.

At September 30, 2006 the Bank and Midwest owned the rights to service mortgages for other institutions, most of which were owned by Midwest. The balance of

mortgages serviced for these institutions was approximately $148 million. The carrying value of these servicing rights was $1,525,282 at September 30, 2006. The servicing rights are recorded at the lower of cost or market. The impairment reserves at September 30, 2006 and 2005 are $389,000 and $509,000, respectively. Market interest rate conditions can quickly affect the value of mortgage servicing rights in a positive or negative fashion, as long-term interest rates rise and fall. The amortization of these rights is based upon the level of principal pay downs received and expected prepayments of the mortgage loans. During 2006, Mortgage rates rose during the first six months of the year and then declined during the third quarter. As a result, impairment reserve remained unchanged from December 31, 2005. During the nine-months ended September 30, 2005, management recorded a $7,000 impairment charge due to a decrease in the mortgage rates during 2005.

Following is an analysis of the change in the Company's mortgage servicing rights for the nine-months ended September 30, 2006 and 2005

| | 2006 | 2005 |
|---|---|---|
| Balance, January 1 | $1,471,808 | $1,097,786 |
| Additions - originated | 220,590 | 389,952 |
| Amortization expense | (167,116) | (198,183) |
| Adjustment for asset impairment change | - | 7,000 |
| Balance, September 30 | $1,525,282 | $1,296,555 |

Capital Resources

Capital Resources

The table below sets forth the Bank's risk based assets, capital ratios and risk-based capital ratios of the Bank. At September 30, 2006 and December 31, 2005, the Bank was considered "well-capitalized" and exceeded the regulatory guidelines.

| | Actual | | To Be Adequately Capitalized Under Prompt Corrective Action Provisions | |
|---|---|---|---|---|
| | Amount | Ratio | Amount | Ratio |
| As of September 30, 2006: | | | | |
| Total capital (to risk weighted assets) | 8,127,000 | 19.3% | $3,370,000 | 8.0 % |
| Tier I capital (to risk weighted assets) | 7,654,000 | 18.2% | 1,685,000 | 4.0 % |
| Tier I capital (to average assets) | 7,654,000 | 12.2% | 2,511,000 | 4.0 % |
| As of December 31, 2005: | | | | |
| Total capital (to risk weighted assets) | $7,947,000 | 18.4% | $3,448,000 | 8.0 % |
| Tier I capital (to risk weighted assets | 7,598,000 | 17.6% | 1,724,000 | 4.0 % |
| Tier I capital (to average assets) | 7,598,000 | 14.0% | 2,171,000 | 4.0 % |

Liquidity

Bank Liquidity. The Bank's primary sources of liquidity are customer deposits, scheduled payments and prepayments of loan principal, cash flow from operations, maturities of various investments, borrowings from correspondent lenders secured by securities, residential mortgage loans and/or commercial loans. In addition, the Bank invests in overnight federal funds. At September 30, 2006, the Bank had cash and cash equivalents of $8,690,556. The Bank's lines of credit include the following:

- $3.5 million from the Federal Home Loan Bank of Indianapolis secured by investment securities and residential mortgage loans, and
- $6.9 million from the Federal Reserve Bank of Chicago secured by commercial loans.

In order to bolster liquidity from time to time, the Bank also sells brokered time deposits. At September 30, 2006, the Bank had zero brokered deposits outstanding.

Bancorp Liquidity. Management does not expect that the Bank will pay dividends to the Company during 2006. At September 30, 2006, Bancorp had $4,970 in cash and investments on hand to meet its working capital needs.

## Impact of Inflation

The primary impact of inflation on the Company's operations is reflected in increased operating costs. Since the assets and liabilities of the Company are primarily monetary in nature, changes in interest rates have a more significant impact on the Company's performance than the general effects of inflation. However, to the extent that inflation affects interest rates, it also affects the net income of the Company.

## ITEM 3. CONTROLS AND PROCEDURES

(a) Evaluation of Disclosure Controls and Procedures.

Disclosure controls are procedures that are designed with an objective of ensuring that information required to be disclosed in our periodic reports filed with the SEC, such as this report on Form 10-QSB, is recorded, processed, summarized, and reported within the time periods specified by the SEC. Disclosure controls also are designed with an objective of ensuring that such information is accumulated and communicated to our management, including our chief executive officer and chief financial officer, in order to allow timely consideration regarding required disclosures.

During the nine-months ended September 30, 2006, the Company did not file on a timely basis, certain of its quarterly Forms 10-Q and its 2005 annual Form 10-K with the Securities Exchange Commission (SEC) within the required due dates. The Company's auditor advised the Company's management and its Board of Directors that this is an identified significant deficiency which is designated as a "reportable condition" and constitutes a material weakness in the Company's internal controls over financial reporting under Section 404 of the Sarbanes Oxley Act.

As of the end of the period covered by this report, an evaluation was carried out under the supervision and with the participation of the Company's management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) under the Securities Exchange Act of 1934). Based upon that evaluation the Chief Executive Officer and Chief Financial Officer concluded that the design and operation of these disclosure controls and procedures were effective. No significant changes were made in our internal controls or in other factors that could significantly affect these controls subsequent to the date of their evaluation.

The filing of the 2005 annual Form 10-K was delayed because the Company was working with their prior auditors to get their consent to include their audit opinions for 2004 and 2003 in the Form 10K. For the first quarter of 2006, the Company delayed its filing of the Form 10QSB because additional time was required to consider the financial implications of the buyout of a consulting agreement.

(b) Changes in Internal Controls.

During the period covered by this report, there have been no changes in the Company's internal control over financial reporting that have materially affected or are reasonably likely to materially affect the Company's internal control over financial reporting.

PART II OTHER INFORMATION

Item 1. Legal Proceedings

None

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

None

Item 3. Defaults upon Senior Securities

None

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

None

Item 5. Other information

None

Item 6. Exhibits and Reports on Form 8-K.

(a) Exhibits.

31.1 Certification of the President and Chief Executive Officer of University Bancorp, Inc. pursuant to 15 U.S.C.Section 7241, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

31.2 Certification of the Chief Financial Officer of University Bancorp, Inc. pursuant to 15 U.S.C. Section 7241, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32.1 Certification of the Chief Executive Officer of University Bancorp, Inc. pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

32.2 Certification of the Chief Financial Officer of University Bancorp, Inc. pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

## SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

UNIVERSITY BANCORP, INC.

Date: November 14, 2006

/s/ Stephen Lange Ranzini

Stephen Lange Ranzini
President and Chief Executive Officer

/s/ Nicholas K. Fortson
Nicholas K. Fortson
Chief Financial Officer

## EXHIBIT INDEX

| Exhibit | Description |
|---|---|
| 31.1 | Certification of the President and Chief Executive Officer of University Bancorp, Inc. pursuant to 15 U.S.C.Section 7241, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
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| 32.2 | Certification of the Chief Financial Officer of University Bancorp, Inc. pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |

Exhibit 31.1

10-QSB 302 CERTIFICATION

I, Stephen Lange Ranzini, certify that:

1) I have reviewed this quarterly report on Form 10-QSB of University Bancorp, Inc.;

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

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

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

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

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

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

5) The registrant's other certifying officer and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):

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

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

Date: November 14, 2006

/s/Stephen Lange Ranzini

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Stephen Lange Ranzini
President and Chief Executive Officer

Exhibit 31.2
10-QSB 302 CERTIFICATION

I, Nicholas K. Fortson, certify that:

1) I have reviewed this quarterly report on Form 10-QSB of University Bancorp, Inc.;
2) Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;
3) Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;
4) The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:

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

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

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

5) The registrant's other certifying officer and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):

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

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

Date: November 14, 2006 /s/Nicholas K. Fortson

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Nicholas K. Fortson

Chief Financial Officer

Exhibit 32.1

CERTIFICATION PURSUANT
TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

I, Stephen Lange Ranzini, the President and Chief Executive Officer of University Bancorp, Inc., certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Quarterly Report of University Bancorp, Inc. on Form 10-QSB for the quarter ended Septemeber 30, 2006 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in such report on Form 10-QSB fairly presents in all material respects the financial condition and results of operations of University Bancorp, Inc.

University Bancorp, Inc

Date: November 14, 2006 By: /s/ Stephen Lange Ranzini

Stephen Lange Ranzini
President and Chief Executive Officer

Exhibit 32.2

CERTIFICATION PURSUANT
TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

I, Nicholas K. Fortson, Chief Financial Officer of University Bancorp, Inc., certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Quarterly Report of University Bancorp, Inc. on Form 10-QSB for the quarter ended September 30, 2006 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in such report on Form 10-QSB fairly presents in all material respects the financial condition and results of operations of University Bancorp, Inc.

University Bancorp, Inc

Date: November 14, 2006
By: /s/ Nicholas K. Fortson
Nicholas K. Fortson
Chief Financial Officer