

Huron Community Financial Services, Inc.

Consolidated Financial Report
December 31, 2009

Huron Community Financial Services, Inc.

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Independent Auditor's Report

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

We have audited the accompanying consolidated balance sheet of Huron Community Financial Services, Inc. (the "Corporation") as of December 31, 2009 and 2008 and the related consolidated statements of income, stockholders' equity, and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Huron Community Financial Services, Inc. at December 31, 2009 and 2008 and the consolidated results of its operations, changes in stockholders' equity, and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

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

Plante & Moran, PLLC

April 6, 2010

Huron Community Financial Services, Inc.

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

	December 31, 2009	December 31, 2008
Assets		
Cash and due from banks	\$ 10,823	\$ 5,159
Federal funds sold	35	129
Total cash and cash equivalents	10,858	5,288
Investment securities - Available for sale (Note 2)	23,508	10,083
Investment securities - Held to maturity (Note 2)	-	6,555
Other securities (Note 2)	1,554	1,554
Loans - Net of allowance for loan losses (Note 3)	147,257	151,098
Foreclosed assets	1,903	960
Premises and equipment (Note 5)	3,267	3,541
Intangible assets	520	749
Accrued interest receivable	741	670
Other assets	7,156	5,959
Total assets	\$ 196,764	\$ 186,457
Liabilities and Stockholders' Equity		
Liabilities		
Deposits:		
Noninterest-bearing	\$ 22,427	\$ 20,916
Interest-bearing (Note 6)	130,031	121,551
Total deposits	152,458	142,467
Short-term borrowings (Note 7)	8,362	5,385
Borrowings (Note 8)	13,000	17,000
Accrued and other liabilities	1,489	1,313
Total liabilities	175,309	166,165
Stockholders' Equity		
Common stock - \$1 par value:		
Authorized - 1,050,000 shares		
Issued and outstanding - 585,561 shares and 568,891 shares in 2009 and 2008, respectively	586	569
Additional paid-in capital	19,414	17,540
Undivided profits	1,064	2,147
Accumulated other comprehensive income	391	36
Total stockholders' equity	21,455	20,292
Total liabilities and stockholders' equity	\$ 196,764	\$ 186,457

See Notes to Consolidated Financial Statements.

Huron Community Financial Services, Inc.

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

	Year Ended	
	December 31, 2009	December 31, 2008
Interest Income		
Loans - Including fees	\$ 9,517	\$ 10,169
Investment securities	669	805
Federal funds sold	1	117
Total interest income	10,187	11,091
Interest Expense		
Deposits	2,153	3,023
Interest on FHLB advances	723	812
Interest on short-term borrowings	32	83
Total interest expense	2,908	3,918
Net Interest Income	7,279	7,173
Provision for Loan Losses (Note 3)	608	408
Net Interest Income After Provision for Loan Losses	6,671	6,765
Other Operating Income		
Service charges - Deposits	581	618
Impairment loss on investment securities	-	(863)
Loan servicing income - Net	519	292
Other	167	218
Total other operating income	1,267	265
Other Operating Expenses		
Salaries and employee benefits	2,943	2,943
Amortization of intangible assets	229	229
Occupancy expense	473	482
Service fees	216	227
Depreciation expense	354	360
Other	1,852	1,372
Total other operating expenses	6,067	5,613
Income - Before income taxes	1,871	1,417
Provision for Income Taxes (Note 9)	424	324
Net Income	<u>\$ 1,447</u>	<u>\$ 1,093</u>
Earnings per Share		
Basic earnings per common share	\$ 2.52	\$ 1.85
Diluted earnings per common share	2.46	1.78

See Notes to Consolidated Financial Statements.

Huron Community Financial Services, Inc.

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

	Common Stock	Additional Paid-in Capital	Undivided Profits	Accumulated Other Comprehensive Income	Total Stockholders' Equity
Balance - January 1, 2008	\$ 587	\$ 15,306	\$ 5,698	\$ 17	\$ 21,608
Comprehensive income:					
Net income	-	-	1,093	-	1,093
Change in net unrealized gain on securities available for sale - Net of tax benefit of \$15	-	-	-	19	19
Total comprehensive income					1,112
Change in accounting for split-dollar arrangements	-	-	(136)	-	(136)
Sale of common stock	45	2,117	-	-	2,162
Purchases of common stock	(63)	-	(3,096)	-	(3,159)
Tax effect of stock options exercised	-	106	-	-	106
Stock-based compensation	-	11	-	-	11
Dividends declared \$2.40 per common share	-	-	(1,412)	-	(1,412)
Balance - December 31, 2008	569	17,540	2,147	36	20,292
Comprehensive income:					
Net income	-	-	1,447	-	1,447
Defined benefit pension and postretirement	-	-	-	355	355
Total comprehensive income					1,802
Sale of common stock	45	1,786	-	-	1,831
Purchases of common stock	(28)	-	(1,253)	-	(1,281)
Tax effect of stock options exercised	-	78	-	-	78
Stock-based compensation	-	10	-	-	10
Dividends declared \$2.20 per common share	-	-	(1,277)	-	(1,277)
Balance - December 31, 2009	\$ 586	\$ 19,414	\$ 1,064	\$ 391	\$ 21,455

See Notes to Consolidated Financial Statements.

Huron Community Financial Services, Inc.

Consolidated Statement of Cash Flows (000s omitted)

	Year Ended	
	December 31, 2009	December 31, 2008
Cash Flows from Operating Activities		
Net income	\$ 1,447	\$ 1,093
Adjustments to reconcile net income to net cash from operating activities:		
Depreciation and amortization	583	589
Impairment loss on investment securities	-	863
Provision for loan losses	608	408
Amortization and accretion on securities	344	116
Deferred tax expense	(450)	-
Stock-based compensation	10	11
Net change in:		
Accrued interest receivable	(71)	147
Other assets	(1,874)	(2,530)
Accrued expenses and other liabilities	176	(378)
Net cash provided by operating activities	773	319
Cash Flows from Investing Activities		
Activity in available-for-sale securities:		
Maturities, prepayments, and calls	20,479	18,925
Purchases	(27,154)	(17,179)
Activity in held-to-maturity securities:		
Maturities, prepayments, and calls	-	1,478
Purchases	-	(2,887)
Net decrease (increase) in loans	3,233	(5,818)
Capital expenditures	(80)	(128)
Net cash used in investing activities	(3,522)	(5,609)
Cash Flows from Financing Activities		
Net increase in deposits	9,991	3,138
Net change in short-term borrowings	2,977	(855)
Proceeds from FHLB advances	-	5,000
Payments on FHLB advances	(4,000)	(1,000)
Proceeds from sale of common stock	1,831	2,162
Purchases of common stock	(1,281)	(3,159)
Tax effect of stock options exercised	78	106
Cash dividends paid on common stock	(1,277)	(1,412)
Net cash provided by financing activities	8,319	3,980
Net Increase (Decrease) in Cash and Cash Equivalents	5,570	(1,310)
Cash and Cash Equivalents - Beginning of year	5,288	6,598
Cash and Cash Equivalents - End of year	\$ 10,858	\$ 5,288
Supplemental Cash Flow Information - Cash paid for		
Interest	\$ 2,956	\$ 4,033
Income taxes	447	490

See Notes to Consolidated Financial Statements.

Huron Community Financial Services, Inc.

Notes to Consolidated Financial Statements December 31, 2009 and 2008

Note 1 - Nature of Business and Significant Accounting Policies

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

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

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

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

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

Huron Community Financial Services, Inc.

Notes to Consolidated Financial Statements December 31, 2009 and 2008

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

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

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

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

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

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

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

Huron Community Financial Services, Inc.

Notes to Consolidated Financial Statements December 31, 2009 and 2008

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

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

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

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

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

Huron Community Financial Services, Inc.

Notes to Consolidated Financial Statements December 31, 2009 and 2008

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

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

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

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

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

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

