UNIVERSITY BANCORP, INC.
AND SUBSIDIARIES

AUDITED CONSOLIDATED FINANCIAL STATEMENTS

Years ended December 31, 2011 and 2010

UNIVERSITY BANCORP, INC. AND SUBSIDIARIES

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UHY LLP
Certified Public Accountants

INDEPENDENT AUDITOR'S REPORT

Board of Directors and Stockholders
University Bancorp, Inc. and Subsidiaries

We have audited the accompanying consolidated balance sheets of University Bancorp, Inc. and Subsidiaries (the "Company") as of December 31, 2011 and 2010, and the related consolidated statements of operations, equity, and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company'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 audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining on a test basis, evidence supporting the amounts and disclosures in the consolidated 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 financial position of University Bancorp, Inc. and Subsidiaries as of December 31, 2011 and 2010, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

UHY LLP

Farmington Hills, Michigan
March 31, 2012

UNIVERSITY BANCORP, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

	December 31, 2011	December 31, 2010
ASSETS		
Cash and due from banks	**$ 9,052,660**	$ 13,595,247
Certificates of deposit	**6,250,000**	6,250,000
Trading securities, at fair value	**785,211**	964,893
Investment securities available-for-sale, at fair value	**2,581,261**	2,934,369
Federal Home Loan Bank Stock, at cost	**1,072,300**	1,197,400
Loans and financings held for sale, at lower of cost or market	**2,617,180**	3,645,675
Loans and financings held for sale, at fair value	**29,858,888**	18,811,794
Loans and financings, net	**56,658,794**	57,603,267
Premises and equipment, net	**3,741,965**	2,979,735
Mortgage servicing rights, at fair value	**2,452,156**	2,929,514
Other real estate owned, net	**1,114,455**	1,425,821
Accounts receivable	**907,871**	966,055
Accrued interest and financing income receivable	**271,918**	195,277
Prepaid expenses	**806,280**	996,889
Derivatives, at fair value	**671,312**	107,012
Goodwill	**103,914**	103,914
Other assets	**1,473,230**	2,558,699
Total assets	**$ 120,419,395**	$ 117,265,561

	December 31, 2011	December 31, 2010
LIABILITIES AND EQUITY		
LIABILITIES		
Deposits:		
Demand - non-interest bearing	**$ 56,210,446**	$ 59,310,523
Demand - interest bearing and profit sharing	**31,405,953**	26,691,972
Savings	**314,160**	275,307
Time	**13,595,082**	13,335,788
Total deposits	**101,525,641**	99,613,590
Derivatives, at fair value	**110,331**	-
Accounts payable	**656,883**	412,817
Accrued interest and profit sharing payable	**37,010**	44,274
Other liabilities	**7,746,206**	5,986,100
Preferred stock subject to mandatory redemption	**960,050**	880,140
Total liabilities	**111,036,121**	106,936,921
EQUITY		
University Bancorp, Inc. stockholders' equity:		
Common stock, $.01 par value per share; 5,000,000 shares authorized; 4,757,782 and 4,391,062 shares issued as of December 31, 2011 and 2010, respectively	**47,578**	43,911
Additional paid-in capital	**6,524,099**	6,204,201
Treasury stock, at cost, 115,184 shares held	**(340,530)**	(340,530)
Accumulated deficit	**(432,016)**	(51,632)
Accumulated other comprehensive income	**88,027**	67,759
Equity attributable to stockholders of University Bancorp, Inc.	**5,887,158**	5,923,709
Noncontrolling interest	**3,496,116**	4,404,931
Total equity	**9,383,274**	10,328,640
Total liabilities and equity	**$ 120,419,395**	$ 117,265,561

UNIVERSITY BANCORP, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS

	Years ended December 31, 2011	2010
Interest and financing income:		
Interest and fees on loans and financing income	**$ 4,158,471**	$ 4,464,094
Interest on securities:		
U.S. Government agencies	**76,428**	10,703
Other securities	**29,447**	14,928
Interest on Federal funds and other	**193,183**	182,506
Total interest and financing income	**4,457,529**	4,672,231
Interest and profit sharing expense:		
Interest and profit sharing on deposits:		
Demand deposits	**284,914**	418,812
Savings deposits	**461**	651
Time deposits	**232,538**	327,422
Short-term borrowings	**13**	-
Total interest and profit sharing expense	**517,926**	746,885
Net interest and financing income	**3,939,603**	3,925,346
Provision for loan losses	**341,088**	891,094
Net interest and financing income after provision for loan losses	**3,598,515**	3,034,252
Other income:		
Loan servicing and sub-servicing fees	**5,607,224**	4,775,784
Initial loan set-up and other fees	**4,086,411**	4,998,388
Gain on sale of mortgage loans, net	**6,749,530**	5,571,048
Insurance & investment fee income	**189,209**	191,215
Deposit service charges and fees	**7,953**	13,987
Net realized gain (loss) on trading securities	**1,675**	(8,338)
Change in fair value of mortgage servicing rights	**(1,381,808)**	(145,152)
Change in fair value of loans held for sale, interest rate locks and forward commitments	**1,472,559**	126,464
Other income	**90,014**	242,097
Total other income	**16,822,767**	15,765,493

	Years ended December 31, 2011	2010
Other expenses:		
Salaries and benefits	**$ 13,955,797**	$ 10,803,594
Occupancy	**977,869**	762,114
Data processing and equipment expense	**1,169,027**	937,908
Legal and audit	**659,090**	907,726
Consulting fees	**711,600**	408,175
Mortgage banking	**1,166,962**	1,955,364
Advertising	**251,785**	142,272
Membership and training	**302,925**	242,608
Travel and entertainment	**342,810**	309,941
Supplies and postage	**612,506**	527,031
Insurance	**268,131**	243,185
Other operating expenses	**1,116,754**	1,252,318
Total other expenses	**21,535,256**	18,492,236
Income (loss) before income taxes	**(1,113,974)**	307,509
Income tax expense (benefit)	**(181,900)**	138,150
Net income (loss)	**(932,074)**	169,359
Net income (loss) attributable to the noncontrolling interests	**(634,280)**	410,564
Net loss attributable to common stockholders of University Bancorp, Inc.	**$ (297,794)**	$ (241,205)

See notes to consolidated financial statements.

UNIVERSITY BANCORP, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF EQUITY

	University Bancorp, Inc. Stockholders'		
	Common Stock $.01 Par value		Additional
	Number of Shares	Par Value	Paid-in Capital
Balance at January 1, 2010	4,391,062	$ 43,911	$ 6,204,201
Comprehensive income (loss):			
Net income (loss)			
Other comprehensive income			
Change in net unrealized gain on securities available-for-sale			
Total comprehensive income (loss)			
Distributions to noncontrolling interest			
Preferred stock dividend			
Balance at December 31, 2010	4,391,062	43,911	6,204,201
Comprehensive income (loss):			
Net loss			
Other comprehensive income			
Change in unrealized gain on securities available-for-sale			
Total comprehensive income (loss)			
Contributions by noncontrolling interest			
Issuance of common stock to acquire noncontrolling interest	366,720	3,667	319,898
Preferred stock dividend			
Balance at December 31, 2011	4,757,782	$ 47,578	$ 6,524,099

University Bancorp, Inc. Stockholders'					
Treasury Stock					
Number of Shares	Cost	Retained Earnings (Accumulated Deficit)	Accumulated Other Compre-hensive Income	Non-controlling Interest	Total
(115,184)	$ (340,530)	$ 266,943	$ 2,872	$ 4,767,809	$ 10,945,206
		(241,205)		410,564	169,359
			64,887		64,887
		(241,205)	64,887	410,564	234,246
				(773,442)	(773,442)
		(77,370)			(77,370)
(115,184)	(340,530)	(51,632)	67,759	4,404,931	10,328,640
		(297,794)		(634,280)	(932,074)
			20,268		20,268
		(297,794)	20,268	(634,280)	(911,806)
				49,030	49,030
				(323,565)	-
		(82,590)			(82,590)
(115,184)	$ (340,530)	$ (432,016)	$ 88,027	$ 3,496,116	$ 9,383,274

UNIVERSITY BANCORP, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

	Years ended December 31, 2011	2010
OPERATING ACTIVITIES		
Net income (loss)	**$ (932,074)**	$ 169,359
Adjustments to reconcile net income (loss) to net cash flows from operating activities:		
Depreciation and amortization	**495,995**	471,765
Change in fair value of mortgage servicing rights	**1,381,808**	145,152
Change in fair value of loans held for sale, interest rate locks and forward commitments	**(1,472,559)**	(126,464)
Deferred income tax expense (benefit)	**(181,900)**	138,150
Provision for loan losses	**341,088**	891,094
Net gain on sale of mortgages	**(6,749,530)**	(5,571,048)
Net realized (gain) loss on trading securities	**(1,675)**	8,338
Proceeds from maturities of trading securities	**181,358**	539,818
Net loss on sale of mortgage servicing rights	**-**	25,516
Net loss on sale of other real estate owned	**6,956**	4,949
Net amortization (accretion) on investment securities	**3,388**	(9,658)
Write down of other real estate owned	**47,545**	29,132
Originations of mortgage loans and financings	**(313,815,218)**	(381,380,905)
Proceeds from mortgage loan and financing sales	**310,898,599**	387,085,094
Net change in:		
Various other assets	**1,439,521**	(1,526,001)
Various other liabilities	**1,994,228**	1,825,590
Net cash provided by (used in) operating activities	**(6,362,470)**	2,719,881
INVESTING ACTIVITIES		
Proceeds from maturities of securities available-for-sale	**369,987**	31,114
Net proceeds from sale of Federal Home Loan Bank stock	**125,100**	127,600
Proceeds from sale of other real estate owned	**442,460**	433,375
Payments for improvements of other real estate owned	**-**	(8,594)
Loans granted and repayments, net	**417,790**	(1,344,296)
Purchase of mortgage servicing rights	**(238,310)**	(734,892)
Purchases of premises and equipment	**(1,108,225)**	(640,470)
Acquisition of business	**(150,000)**	-
Proceeds from sale of mortgage servicing rights	**-**	99,953
Purchase of certificates of deposit	**-**	(6,250,000)
Purchase of securities available-for-sale	**-**	(2,333,844)
Net cash used in investing activities	**(141,198)**	(10,620,054)

	Years ended December 31, 2011	2010
FINANCING ACTIVITIES		
Net change in deposits	**$ 1,912,051**	$ (18,420,969)
Contributions by noncontrolling interest	**49,030**	-
Distributions to noncontrolling interest	**-**	(773,442)
Net cash provided by (used in) financing activities	**1,961,081**	(19,194,411)
NET CHANGE IN CASH	**(4,542,587)**	(27,094,584)
Cash and Cash Equivalents, Beginning	**13,595,247**	40,689,831
Cash and Cash Equivalents, Ending	**$ 9,052,660**	$ 13,595,247
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Cash paid during the year for:		
Interest	**$ 525,190**	$ 753,228
Income taxes	**$ 3,770**	$ -
SUPPLEMENTAL DISCLOSURE OF NON-CASH TRANSACTIONS:		
Mortgage loans converted to other real estate owned and other assets	**$ 185,595**	$ 1,205,280
Dividends payable on preferred stock converted to additional shares of preferred stock	**$ 79,910**	$ 74,020
Dividends declared that were recorded as dividends payable	**$ 82,590**	$ 77,370
Issuance of common stock to acquire noncontrolling interest	**$ 323,565**	$ -

See notes to consolidated financial statements.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation and Nature of Operations

The consolidated financial statements of University Bancorp, Inc. (the "Company") include the operations of its wholly owned subsidiary, University Bank, Inc. (the "Bank"), the Bank's wholly owned subsidiaries, University Insurance & Investment Services, Inc. ("Agency") and Hoover, LLC ("Hoover"), the Bank's two 80% owned subsidiaries, Midwest Loan Services, Inc. ("Midwest") and University Islamic Financial Corporation ("UIFC"), and the Bank's majority owned subsidiary University Lending Group, LLC ("ULG"). As of December 31, 2010, the Bank owned 50.01% of ULG, and as of December 31, 2011, the Bank owned 87.5% of ULG. These consolidated financial statements also include the operations of Hoover's wholly owned subsidiary, Tuomy, LLC. The accounts are maintained on an accrual basis in accordance with generally accepted accounting principles and predominant practices within the banking and mortgage banking industries. All significant intercompany balances and transactions have been eliminated in preparing the consolidated financial statements.

The Company is a bank holding company. University Bank, which is located in Michigan, is a full service community bank, which offers all customary banking services, including the acceptance of checking, savings and time deposits. The Bank also makes commercial, real estate, personal, home improvement, automotive and other installment, credit card and consumer loans, and provides fee based services such as annuity and mutual fund sales, stock brokerage and money management, life insurance, property casualty insurance and foreign currency exchange. The Bank's customer base is primarily located in the Ann Arbor, Michigan area.

University Bank's loan portfolio is concentrated in Ann Arbor and Washtenaw County, Michigan. While the loan portfolio is diversified, the customers' ability to honor their debts is partially dependent on the local economy. The Ann Arbor area is primarily dependent on the education, healthcare, services and manufacturing (automotive and other) industries. Most real estate loans are secured by residential or commercial real estate and business assets secure most business loans. Generally, installment loans are secured by various items of personal property.

The Agency is engaged in the sale of insurance products including life, health, property and casualty, and investment products including annuities, mutual funds, stock brokerage and money management. The Agency is located in the Bank's Ann Arbor main office.

Hoover owns the Bank's headquarters facility. Tuomy owns commercial land with a rental building.

Midwest is engaged in the business of servicing and sub-servicing residential mortgage loans. Midwest began operations in 1992 and was acquired by University Bank in December 1995. Midwest is based in Houghton, Michigan, and also originates mortgage loans for itself and other financial institutions, including the Bank (See Note 5).

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Principles of Consolidation and Nature of Operations (Continued)

ULG commenced operations in April 2008 and is headquartered in Farmington Hills, Michigan. During 2011, ULG began operating in twelve new retail branches. As a result, ULG now operates thirteen retail branches throughout Michigan, Indiana and Florida. ULG is engaged in the business of marketing, processing, closing and selling retail mortgage loans. ULG is also engaged in the business of servicing mortgage loans as servicing rights are retained on selective loans that are sold.

UIFC is engaged in Islamic Banking and was formed on December 30, 2005. Its current products, which comply with Islamic (Sharia'a) law, are FDIC-insured deposits and home financings (as agent for the Bank), mutual funds (as agent for a third-party fund distribution company) and home financings (as principal for its own account). The Sharia'a compliant products are offered to service the large number of Muslim customers in the general area of the Company.

There are two distinct home financing products offered, the Ijara and the Murabaha.

Under the Ijara method, a single-asset trust is established by or on behalf of the originator (Bank/UIFC), as settlor, naming a special purpose entity as the trustee. The trust is subject to the terms of the written indenture designed for this specific purpose which is used generically for all financings in the redeemable lease (Ijara) program. The funds necessary to acquire the real property are deposited into the trust by the originator, as settlor, and used to fund the purchase of the property. The trust then enters into a combination lease/contract-for-deed agreement with the lessee/purchaser. The settlor is the initial beneficiary of the trust, but the beneficial interest in the payment stream arising from the trust is assignable to third parties. The power to remove and appoint trustees is granted to the beneficiary and the beneficiary has the power to direct the trustee with respect to foreclosure of the property. These rights are assignable with the payment stream.

The terms of the lease and contract-for-deed agreements, in combination, result in a payment stream and cost of the real property that are functionally equivalent to secured real estate lending for both the lessee/purchaser and the Company. The lease payment under the lease agreement is similar to an interest payment under a conventional mortgage. The contract-for-deed payments resemble a principal payment under a conventional mortgage.

The redeemable lease arrangement is treated as financing rather than leasing in accordance with generally accepted accounting principles ("GAAP"). A lease that transfers substantially all of the benefits and risks incident to the ownership of property should be accounted for as the acquisition of an asset by the lessee and as a financing by the lessor.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Principles of Consolidation and Nature of Operations (Continued)

Under lease accounting standards of the Accounting Standards Codification ("ASC"), a lease would generally be accounted for as a financing if:

1. The underlying property is transferred to the lessee at the end of the lease, or
2. The lease contains a bargain purchase that is reasonably assured of being exercised, and
3. It is reasonably certain that the lease payments will be collected, and
4. No uncertainties surround the amount of un-reimbursable costs yet to be incurred by the lessor under the lease.

Accordingly, the Company's accounting for this product is essentially the same as a conventional mortgage product. To reflect the legal substance of the Ijara transactions, the Company uses the balance sheet account title "Loans and financings" instead of a typical title of "Loans". In the statement of operations, "Interest and fees on loans" is modified to state "Interest and fees on loans and financing income".

The second form of home financing is the Murabaha. This form of financing is similar to an installment sale contract. As agent for the Federal Home Loan Mortgage Corporation ("Freddie Mac"), the Bank buys a home selected by a customer and then resells it to the customer, at a selling price higher than the purchase price. The difference between the Bank's purchase price and the selling price is the profit that the ultimate holder (Freddie Mac) of the installment contract will accrete into income over the life of the contract. After the contract is executed by the Bank and the customer, Freddie Mac reimburses the Bank for its outlay of cash to purchase the home and pays the Bank a fee for originating the transaction. The customer pays Freddie Mac for the home that was purchased on an installment basis, per an agreed repayment schedule.

The Company records these contracts at fair value for the short period of time that they are held before settlement with Freddie Mac. The installment contracts are sold with servicing retained. Thus, the value of the installment contract and value of the servicing is determined to calculate the fair value and any gain or loss on the sale of the underlying installment contract. See Note 19 for additional discussion of the determination of fair value.

On the liability side of the balance sheet, the Bank offers FDIC–insured deposits that are compliant with Sharia'a. These deposits are specifically invested in Sharia'a compliant investments such as, but not limited to, the Ijara. Sharia'a compliant savings, money markets and certificates of deposit pay out earnings that are derived specifically from the revenues from the Sharia'a compliant investments net of certain expenses. In compliance with the FDIC definition of a deposit, balances in these accounts, like all deposit accounts, are FDIC insured. The sharing of earnings paid out to the depositors holding these accounts can fluctuate with the net earnings of the Ijara portfolio and or other Sharia'a compliant investments. The earnings paid to the depositors are accounted for as an expense.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Principles of Consolidation and Nature of Operations (Continued)

This expense is analogous to interest expense paid on deposits in conventional finance. To reflect the legal substance of the Sharia'a compliant deposits, the Company uses the balance sheet account title "Demand deposits – interest bearing and profit sharing" instead of the typical title of "Demand deposits – interest bearing". In the statement of operations, "Interest on deposits" is modified to state "Interest and profit sharing on deposits".

Use of Estimates

The preparation of consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions based upon available information. These estimates and assumptions affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the dates of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates.

The significant estimates incorporated into these consolidated financial statements, which are more susceptible to change in the near term, include the value of mortgage servicing rights, the allowance for loan losses, the identification and valuation of impaired loans, the valuation of other real estate owned, impairment analysis of goodwill, the valuation of deferred tax assets, the fair value of certain loans held for sale and derivative instruments such as mortgage interest rate locks and forward commitments, and the fair value of other financial instruments.

Cash Flow Reporting

For purposes of the consolidated statements of cash flows, cash and cash equivalents is defined to include the cash on hand, interest bearing deposits in other institutions, federal funds sold and other investments with an original maturity of three months or less. Net cash flows are reported for customer loan and deposit transactions and interest bearing deposits with other banks.

Securities

Securities are classified as trading securities or available-for-sale at the date of purchase. Securities available-for-sale are carried at fair value, with unrealized holding gains and losses reported in other comprehensive income or loss. Trading securities are carried at fair value with realized gains and losses recorded in earnings. Available-for-sale securities are written down to fair value through a charge to earnings when a decline in fair value is not temporary. Interest income includes amortization of purchase premium or discount. Other securities such as Federal Home Loan Bank stock are carried at cost.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Federal Home Loan Bank Stock

As a member of the Federal Home Loan Bank ("the FHLB"), the Bank is required to invest in FHLB stock, which is carried at cost since there is no readily available market value. When redeemed, the Bank receives an amount equal to the par value of the stock. Dividends paid on FHLB stock are subject to economic events, regulatory actions and other factors.

Loans and Financings

Loans are reported at the principal balance outstanding, net of unearned interest or profit sharing, deferred loan or financing fees and costs, and an allowance for loan losses. Interest income is reported on the interest method and includes amortization of net deferred loan fees and costs over the loan term. Profit sharing flows from lease income calculated monthly and includes amortization of net deferred financing fees and costs over the term of the financing. Interest or profit sharing income is not reported when full loan repayment is in doubt, typically when payments are past due over ninety days. Payments received on such loans are reported as principal reductions, unless all interest or profit sharing and principal payments in arrears are paid in full.

Allowance for Loan Losses

The allowance for loan losses is a valuation allowance for probable credit losses, increased by the provision for loan losses and recoveries and decreased by charge-offs. Management estimates the balance required based on past loan loss experience, known and inherent risks in the portfolio, information about specific borrower situations and estimated collateral values, economic conditions, and other factors. Allocations of the allowance may be made for specific loans or financings, but the entire allowance is available for any loan or financing that, in management's judgment, should be charged-off.

Loan or financing impairment is reported when full payment under the loan terms is not expected. Impairment is evaluated in total for smaller-balance loans of similar nature such as residential mortgage, consumer, and credit card loans, and on an individual loan or financing basis for other loans or financings. If a loan or financing is impaired, a portion of the allowance is allocated so that the loan or financing is reported, net, at the present value of estimated future cash flows using the loan's or financing's existing rate or at the fair value of collateral if repayment is expected solely from the collateral. Loans or financings are evaluated for impairment when payments are delayed, typically ninety days or more, or when it is probable that all principal and interest or profit sharing amounts will not be collected according to the original terms of the loan or financing.

Premises and Equipment, Net

Premises and equipment are stated at cost less accumulated depreciation. Depreciation is computed primarily on the straight-line method over the assets estimated useful lives.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Premises and Equipment, Net (Continued)

The Company used the following useful lives as of December 31, 2011 and 2010:

	Years
Building and building improvements	5-39
Leasehold improvements	Term of lease or 5-39 years
Equipment	3-10
Furniture and fixtures	3-7
Software	2-5

Mortgage Servicing Rights

Mortgage servicing rights (“MSRs”) represent both purchased rights and the allocated value of servicing rights retained on loans or financings originated and sold.

The Company accounts for its MSRs in accordance with the applicable standards under the ASC which requires that mortgage servicing rights be initially recognized at their fair value and by providing the option to either: (1) carry mortgage servicing rights at fair value with changes in fair value recognized in earnings; or (2) continue recognizing periodic amortization expense and assess the mortgage servicing rights for impairment. This option may be applied by class of servicing assets or liabilities. The Company has identified MSRs relating to mortgage loans as a class of servicing rights and has elected to apply fair value accounting to these assets.

Other Real Estate Owned

Real estate properties acquired in collection of a loan or financing are recorded at fair value upon foreclosure, establishing a new cost basis. Any reduction to fair value from the carrying value of the related loan or financing is accounted for as a loan loss. After foreclosure, management periodically performs valuations to ensure real estate is carried at the lower of cost or fair value, less estimated costs to sell. Expenses, gains and losses on disposition, and decreases in the fair value are reported in other expenses.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Mortgage Banking Activities

During 2011, the Company shifted its focus away from wholesale mortgage banking activities. The Company's mortgage banking activities now consist of retail and servicing operations. Mortgage loans held for sale are sold with selective loans having their servicing retained, and others on a servicing released basis. The Company elected to record ULG and UIFC mortgage loans held for sale at fair value as discussed in Note 19. All other loans held for sale are valued at the lower of cost or market as determined by bid prices for loans in the secondary market. Mortgage loans are sold without recourse, except in certain events as defined in the loan purchase documents.

An allowance was booked for potential recourse liabilities related to loans sold and loans held for sale in the amount of $316,783 and $298,586 as of December 31, 2011 and 2010, respectively. This allowance is included in "Other liabilities" on the face of the consolidated balance sheets.

Loan servicing and sub-servicing fees are contractually based and are recognized monthly as earned over the life of the loans.

Derivative Instruments

The Company enters into interest rate lock commitments ("IRLCs") in connection with its mortgage banking activities to fund residential mortgage loans at specified times in the future. IRLCs that relate to the origination of mortgage loans that will be held for sale are considered derivative instruments under the ASC. As such, these IRLCs are recorded at fair value (see Note 19) with changes in fair value recorded in earnings.

Outstanding IRLCs expose the Company to the risk that the price of the loans underlying the commitments might decline from inception of the interest rate lock to the funding of the loan. To protect against this risk, the Company utilizes forward loan sales commitments to economically hedge the risk of potential changes in the value of the loans that would result from the commitments. These forward commitments are valued at fair value (see Note 19) with net changes in fair value recorded in earnings. The Company documents its risk management strategy and hedge effectiveness at the inception of and during the term of the IRLCs and forward sales commitments within the portfolio.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Goodwill

The Company evaluates the carrying value of goodwill during each quarter of each year and between quarterly evaluations if events occur or circumstances change that would more likely than not reduce the fair value of the reporting unit below its carrying amount. When evaluating whether goodwill is impaired, the Company compares the fair value of the reporting unit to which the goodwill is assigned to the reporting unit's carrying amount, including goodwill. An impairment loss would be recognized when the carrying amount of goodwill exceeds its fair value. The Company's evaluations of goodwill completed during 2011 and 2010 resulted in no impairment losses.

Income Taxes

Deferred income tax assets and liabilities are recorded for estimated future tax consequences attributable to the differences between the financial carrying amounts of existing assets and liabilities and their respective tax bases. Deferred income taxes are to be computed on the liability method and deferred tax assets are recognized only when realization is certain. Deferred income tax assets and liabilities are measured using the tax rate in effect for the year in which those temporary differences are expected to turn around. If necessary, a valuation allowance is booked to reduce net deferred tax assets to a net amount that is more likely than not to be realized.

The ASC standards regarding accounting for uncertainty in income taxes clarifies the accounting for income taxes by prescribing the minimum recognition threshold an income tax position is required to meet before being recognized in the financial statements and applies to all income tax positions. Each income tax position is assessed using a two-step process. A determination is first made as to whether it is more likely than not that the income tax position will be sustained, based upon technical merits, upon examination by the taxing authorities. If the income tax position is expected to meet the more likely than not criteria, the benefit recorded in the financial statements equals the largest amount that is greater than 50% likely to be realized upon its ultimate settlement. At December 31, 2011 and 2010, there was no accrual for uncertain tax positions.

None of the Company's federal or state income tax returns are currently under examination by the Internal Revenue Service ("IRS") or state authorities. However, fiscal years 2008 and later remain subject to examination by the IRS and its respective states.

Michigan adopted a business tax which includes a tax on taxable income, a tax on adjusted gross receipts, and a franchise tax. Under the Michigan Business Tax law the Company is subject to the franchise tax. It is management's policy to include the franchise tax in other operating expenses.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Income Taxes (Continued)

The Michigan statute created a “joint and severally liable” unitary tax on entities which are commonly controlled and have inter-company “flow of value” transactions. Hence, the Company pays this tax on a consolidated basis just as it pays its federal tax on a consolidated basis.

The Company has a tax sharing agreement with some of its subsidiaries in which the subsidiaries record their share of federal and state taxes in accordance with the tax sharing agreements.

Retirement Plan

The Bank has a 401(K) Plan that allows employees of the Bank and the Bank’s subsidiaries to contribute up to 15% of salary pre-tax, to the allowable limit prescribed by the Internal Revenue Service. Management has discretion to make matching contributions to the Plan. The Bank made no matching contributions for each of the years ended December 31, 2011 and 2010.

Employee Stock Ownership Plan (“ESOP”)

The Company has a noncontributory ESOP covering all full-time employees who have met certain service requirements. The employees’ share in the Company’s contribution is based on their current compensation as a percentage of the total employee compensation. As shares are contributed to the plan they are allocated to employees and compensation expense is recorded at the shares’ fair value. The Company made no contribution during either year ended December 31, 2011 or 2010.

Stock Options

In accordance with the ASC, the Company is required to recognize the compensation cost relating to share-based payment transactions in the consolidated financial statements. That cost is to be measured based on the fair value of the equity or liability instruments issued. For each of the years ended December 31, 2011 and 2010, the Company recorded no compensation expense related to stock options.

Comprehensive Income (Loss)

Comprehensive income (loss) includes both net income (loss) and the change in unrealized gains and losses on securities available-for-sale.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Segment Reporting

The Company's segments are determined by the products and services offered, primarily distinguished between banking and its two separate mortgage banking operations. Loans, investments, deposits, servicing fees, underwriting fees and loan sales provide the revenues in the banking operation. Servicing fees, underwriting fees and loan sales provide the revenues in each of the mortgage banking operations. All operations are domestic.

Reclassifications

Certain amounts in the 2010 consolidated financial statements have been reclassified to conform to presentation adopted in 2011.

Subsequent Events

The Company has performed a review of events subsequent to the balance sheet date through March 31, 2012, the date the consolidated financial statements were available to be issued.

NOTE 2 – RESTRICTIONS ON CASH AND AMOUNTS DUE FROM BANKS

The Bank is required to maintain average balances on hand or with the Federal Reserve Bank. At December 31, 2011 and 2010, this reserve requirement amounted to $1,962,000 and $7,611,000, respectively.

NOTE 3 – INVESTMENT SECURITIES

Trading Securities

The Bank's trading securities portfolio had a net accumulated unrealized gain of $33,333 and $31,658 at December 31, 2011 and 2010, respectively.

Trading securities consist of the following:

	December 31, 2011	December 31, 2010
U.S. agency mortgage-backed securities	$ 785,211	$ 964,893

NOTE 3 – INVESTMENT SECURITIES (Continued)

Available-for-Sale Securities

The following is a summary of the amortized cost, gross unrealized gains, gross unrealized losses and fair value of securities available-for-sale.

Securities available-for-sale at December 31, 2011 consists of the following:

	Amortized Cost	Unrealized Gain	Fair Value
U.S. agency mortgage-backed securities	$ 2,493,234	$ 88,027	$ 2,581,261

Securities available-for-sale at December 31, 2010 consists of the following:

	Amortized Cost	Unrealized Gain	Fair Value
U.S. agency mortgage-backed securities	$ 2,866,610	$ 67,759	$ 2,934,369

At December 31, 2011 and 2010, the fair value of trading and available-for-sale securities pledged to secure certain borrowings were $3,366,472 and $3,899,262, respectively. The balance of these borrowings at both December 31, 2011 and 2010 was $-0-.

Actual maturities may differ from contractual maturities because issuers and borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. Proceeds from pay downs of mortgage-backed securities amounted to $551,345 and $570,932 for the years ended December 31, 2011 and 2010, respectively.

NOTE 4 – LOANS AND FINANCINGS, NET

Major classifications of loans are as follows:

	December 31, 2011	December 31, 2010
Commercial	$ 32,009,552	$ 31,296,085
Residential real estate	24,955,987	26,883,830
Installment	291,845	194,656
Credit cards	473,727	578,534
Gross loans	57,731,111	58,953,105
Allowance for loan losses	(1,072,317)	(1,349,838)
Net loans	$ 56,658,794	$ 57,603,267

Changes in the allowance for loan losses were as follows:

	December 31, 2011	December 31, 2010
Balance, beginning of year	$ 1,349,838	$ 909,356
Provision charged to operations	341,088	891,094
Recoveries	285,044	617,477
Charge-offs	(903,653)	(1,068,089)
Balance, end of year	$ 1,072,317	$ 1,349,838

Non-accrual loans are summarized as follows:

	December 31, 2011	December 31, 2010
Residential real estate	$ 788,195	$ 943,347
Commercial loans	717,418	827,718
Total	$ 1,505,613	$ 1,771,065

NOTE 4 – LOANS AND FINANCINGS, NET (Continued)

Information regarding impaired loans is as follows:

	December 31,	
	2011	2010
Impaired loans:		
Loans with allowance allocated	$ 3,135,596	$ 4,148,545
Amount of allowance for loan losses allocated	$ 740,114	$ 1,008,585
Impaired loans:		
Average balance during the year	$ 4,460,262	$ 3,120,665
Interest income recognized thereon	$ 248,705	$ 398,069
Cash basis interest income recognized	$ 230,806	$ 372,607

NOTE 5 – MORTGAGE BANKING ACTIVITIES

Midwest provides sub-servicing of real estate mortgage loans for several financial institutions. The unpaid principal balance of these loans was approximately $10.2 billion and $9.0 billion as of December 31, 2011 and 2010, respectively. The value of these mortgage servicing rights are not included in the accompanying consolidated financial statements.

University Bank, Midwest, UIFC and ULG sell residential mortgage loans to the secondary market with servicing rights retained for selective loans. These loans are owned by other institutions and are not included in the Company's consolidated balance sheets, but the mortgage servicing rights are included in the accompanying consolidated financial statements. Such mortgage loans have been sold predominately without recourse or with limited recourse. The unpaid principal balance of these loans was $394.5 million and $355.3 million at December 31, 2011 and 2010, respectively.

Custodial escrow balances maintained in connection with these loans were $142.6 million and $122.8 million, at December 31, 2011 and 2010, respectively, and were not included in the accompanying consolidated financial statements.

NOTE 5 – MORTGAGE BANKING ACTIVITIES (Continued)

The following summarizes the activity relating to mortgage servicing rights:

	December 31, 2011	December 31, 2010
Balance, January 1	$ 2,929,514	$ 2,465,243
Amount capitalized	904,450	734,892
Sale of servicing rights	-	(125,469)
Change in fair value	(1,381,808)	(145,152)
Balance, December 31	$ 2,452,156	$ 2,929,514

The Company enters into IRLCs in connection with its mortgage banking activities to fund residential mortgage loans at specified times in the future. As of December 31, 2011 and 2010, IRLCs amounted to $32.7 million and $21.4 million, respectively, of which management estimated $24.3 million and $15.1 million, respectively, to eventually close and be funded. These IRLCs were recorded in assets on the face of the consolidated balance sheet at a fair value of $671,312 and $105,342 as of December 31, 2011 and 2010, respectively.

The Company also utilizes forward loan sales commitments in order to economically hedge the risk of potential changes in the value of the loans that would result from the IRLCs. Forward sales commitments to fund loans at specified rates amounted to $24.6 million and $14.9 million as of December 31, 2011 and 2010, respectively, which were recorded in liabilities on the face of the consolidated balance sheet at a fair value of $110,331 as of December 31, 2011, and in assets at a fair value of $1,670 as of December 31, 2010.

The net change in fair value of the IRLCs and the related forward loan sales commitments held at December 31, 2011 and 2010 resulted in a gain of $453,969 and $6,474, respectively, which has been recognized in “Other income” in the consolidated statement of operations. These gains are due principally to the inclusion of day one gains associated with the adoption of fair value accounting as discussed in Note 19. Prior to companies being permitted to adopt fair value accounting, the recognition of such day one gains was prohibited and these gains were not recognized until realized through the sale of the related loans.

Market interest rate conditions can quickly affect the fair value of mortgage servicing rights, IRLCs, and forward loan sales commitments in a positive or negative fashion, as long-term interest rates rise and fall. See Note 19 for further discussion of management’s assumptions used in determination of fair value of these assets and liabilities.

NOTE 6 – PREMISES AND EQUIPMENT, NET

Premises and equipment consist of the following:

	December 31, 2011	December 31, 2010
Land	$ 375,000	$ 375,000
Buildings and improvements	2,165,251	2,039,322
Furniture, fixtures, equipment and software	5,635,594	4,503,298
	8,175,845	6,917,620
Less accumulated depreciation and amortization	(4,433,880)	(3,937,885)
Premises and equipment, net	$ 3,741,965	$ 2,979,735

Depreciation and amortization expense related to premises and equipment amounted to $495,995 and $471,765 for the years ended December 31, 2011 and 2010, respectively.

Midwest, UIFC and ULG each lease office space for their respective operations. ULG and UIFC also lease office space for its retail branches. All of the retail branch lease agreements are short-term in nature, with some being month-to-month, and some allowing the Company to break the lease with a notice ranging from thirty to ninety days and a fee. The Company leases various other facilities at varying rates on a month-to-month basis. Total rent expense for all operating leases was approximately $436,000 and $214,000 in 2011 and 2010, respectively. The following table summarizes the future minimum payments under the contractual obligations of the Company as of December 31, 2011:

Year ended December 31,	Amount
2012	$ 394,185
2013	173,519
2014	178,595
2015	182,605
2016 and thereafter	20,672
	$ 949,576

NOTE 7 – TIME DEPOSITS

Time deposit liabilities issued in denominations of $100,000 or more were $8,743,584 and $8,700,236 at December 31, 2011 and 2010, respectively.

NOTE 7 – TIME DEPOSITS (Continued)

At December 31, 2011, stated maturities of time deposits were:

Year ended December 31,	Amount
2012	$ 7,326,288
2013	2,125,067
2014	1,370,664
2015	1,067,800
2016 and thereafter	1,705,263
	$ 13,595,082

NOTE 8 – OTHER LIABILITIES

Other liabilities consist of the following:

	December 31,	
	2011	2010
Liability to fund closed but undisbursed loans	$ 2,883,983	$ 1,941,992
Remittances	3,450,537	2,418,406
Escrow and mortgage insurance liability	299,626	230,607
Allowance for loan recourse	316,783	298,586
Other	795,277	1,096,509
	$ 7,746,206	$ 5,986,100

NOTE 9 – INCOME TAXES

Income tax expense (benefit) for the years ended December 31, 2011 and 2010 is summarized as follows:

	December 31,	
	2011	2010
Current	$ -	$ -
Deferred	(272,900)	138,150
Increase in valuation allowance	91,000	-
Income tax expense (benefit)	$ (181,900)	$ 138,150

NOTE 9 – INCOME TAXES (Continued)

The effective tax rate differs from the statutory income tax rate as a result of permanent differences in accounting for certain income and expense items for financial and tax reporting purposes, primarily meals and entertainment expense, the effect of the acquisition of a portion of the noncontrolling interest of ULG which is a flow-through entity for tax purposes, and the change in the valuation allowance. Based on management's estimates of future income, during 2011, management increased the valuation allowance in order to decrease the net deferred tax asset to an amount that is more likely than not to be realized.

Significant components of the Company's deferred income tax assets and liabilities as of December 31, 2011 and 2010 are as follows:

	December 31,	
	2011	2010
Deferred income tax assets:		
Allowance for loan losses	$ 236,477	$ 376,688
Net operating loss carry-forward	907,652	206,668
Tax credit carry-forward	1,241,866	1,241,866
Donation carry-forward	7,705	-
Depreciation	33,425	31,921
Other	27,397	27,283
Deferred tax asset	2,454,522	1,884,426
Deferred income tax liabilities:		
Mortgage servicing rights	754,440	872,221
Basis in ULG	390,302	102,391
Derivatives and LHFS	127,107	10,764
Other	10,723	-
Deferred tax liability	1,282,572	985,376
Net deferred tax asset	1,171,950	899,050
Valuation allowance	(91,000)	-
Net deferred tax asset	$ 1,080,950	$ 899,050

The net deferred tax asset is included in "Other assets" on the consolidated balance sheets.

NOTE 9 – INCOME TAXES (Continued)

The Company has the following unused net operating loss carry forwards and available credits as of December 31, 2011:

	Amount	Date of expiration
Federal net operating loss	$ 2,670,000	Beginning 2028
Low income housing credits	1,140,284	Beginning 2012
Minimum tax credits	101,582	N/A

NOTE 10 – MANDATORILY REDEEMABLE PREFERRED STOCK

As of December 31, 2011 and 2010, the Company had 500,000 shares of preferred stock authorized with a $.001 par value per share. There were 96,005 and 88,014 shares of this preferred stock issued and outstanding as of December 31, 2011 and 2010, respectively. The shares have a $10 per share liquidation value and accrue dividends quarterly at an annual rate of 9%. Additional shares of preferred stock are issued semi-annually for unpaid accrued dividends. The preferred stock is mandatorily redeemable by the Company no later than April 30, 2012, at $10 per share plus all accrued and unpaid dividends through the redemption date. As of December 31, 2011, none of the preferred stock had been redeemed.

During 2011 and 2010, the Company declared preferred dividends of $82,590 and $77,370, respectively. As of December 31, 2011 and 2010, the Company had unpaid preferred dividends of $42,610 and $39,930, respectively, which are included in "Other liabilities" on the consolidated balance sheets. The amount the Company would be required to pay to redeem the stock at December 31, 2011 is $960,050 plus accrued dividends of $42,610.

NOTE 11 – STOCK OPTIONS

In 1995, the Company adopted a stock option and stock award plan ("the 1995 Stock Plan"), which provides for the grant of incentive stock options, as defined in Section 422(b) of the Internal Revenue Code of 1986, as amended, as well as the grant of non-qualified stock options and other stock awards. The plan provides for the grant to officers, directors and key employees of the Company, and independent contractors providing services to the Company, of options to purchase common stock and other awards of common stock.

NOTE 11 – STOCK OPTIONS (Continued)

The exercise price of options granted under the plan shall be determined by the Board of Directors, or a compensation committee thereof. Options shall expire on the date specified by the Board of Directors or such committee, but not more than 10 years from the date of grant (or five years from the date of grant for incentive stock options if the grantee owned 10% of the Company's voting stock at the date of grant). The 1995 Stock Plan terminated on November 15, 2006; however, all outstanding options under the plan remain outstanding until expiration, exercise or forfeiture. Options continue to be granted outside of the 1995 Stock Plan.

The following tables summarize the activity relating to options to purchase the Company's common stock:

	Number of Options	Weighted Average Exercise Price
Outstanding at January 1, 2010	292,026	$ 1.83
Granted	-	-
Exercised	-	-
Forfeited	(118,463)	2.00
Outstanding at December 31, 2010	173,563	1.85
Granted	-	-
Exercised	-	-
Forfeited	-	-
Outstanding at December 31, 2011	173,563	$ 1.85

At December 31, 2011:	
Number of options immediately exercisable	173,563
Weighted average exercise price of immediately exercisable options	$1.85
Range of exercise price of options outstanding	$1.00 - $3.00
* Exercise price of 48,563 options will change from $3.00 to $3.50 in 2012	
Weighted average remaining life of options outstanding	1.30 years

NOTE 11 – STOCK OPTIONS (Continued)

The value of the options was determined pursuant to the Black Scholes model at the date of issuance. As the options vested, the Company recognized compensation expense in earnings. As of December 31, 2011 and 2010, all outstanding options had vested. The Company recognized no stock compensation expense during the years ended December 31, 2011 and 2010.

Subsequent to year end, the Company granted a total of 150,000 options to the Company's directors. These options vested immediately, have an exercise price of $1.80 per share, and have an expiration date of February 28, 2017.

NOTE 12 – EMPLOYEE STOCK OWNERSHIP PLAN ("ESOP")

The employees' allocation of ESOP assets is based on their current compensation, after one year of service and upon reaching the age of twenty-one. The annual contribution to the ESOP is at the discretion of the Board of Directors. Assets of the plan are comprised entirely of 62,349 shares of the Company's stock at December 31, 2011 and 2010, all of which were fully allocated at December 31, 2011. Upon retirement from the plan, participants can receive distributions of their allocated shares of the Company's stock. The assets of the ESOP are held in trust and were valued at $87,289, and $99,758 at December 31, 2011 and 2010, respectively.

NOTE 13 – NONCONTROLLING INTEREST

The Bank owns an 80% interest in the common stock of Midwest, with the remaining 20% owned by the President of Midwest. At December 31, 2011 and 2010, total equity of Midwest was $7,847,816 and $6,887,281, respectively, resulting in a $1,569,563 and $1,377,455 noncontrolling interest reflected on the Company's consolidated balance sheets, respectively.

Also, included in the consolidated financial statements are the results for UIFC. The Bank owns 80% of the common stock of UIFC. An outside investor owns the remaining 20%. At December 31, 2011 and 2010, total equity of UIFC was $42,946,468 and $42,649,207, respectively, which includes $10,000,000 in common stock and $33,315,000 of preferred stock as of both December 31, 2011 and 2010. The noncontrolling interest at December 31, 2011 and 2010 was $1,926,553 and $1,866,843, respectively.

Also, included in the consolidated financial statements are the results for ULG. As of December 31, 2010, the Bank owned 50.01% of ULG. During 2011, the Company acquired 37.5% of the noncontrolling interest in ULG in exchange for $249,370 and 366,720 shares of University Bancorp, Inc. common stock. As a result, as of December 31, 2011 the Bank owned 87.5% of ULG, with the remaining amounts owned by an executive of ULG.

NOTE 13 – NONCONTROLLING INTEREST (Continued)

At December 31, 2011 and 2010, total members' equity of ULG was $1,361,658 and $2,320,909, respectively. At December 31, 2011 and 2010, the noncontrolling interest was $-0- and $1,160,633, respectively. The noncontrolling interest is $-0- as of December 31, 2011 because under certain provisions, the ULG noncontrolling interest is to incur losses associated with the startup of the retail branches in 2011, but would be the first to recoup the losses once income is earned.

In accordance with ULG's operating agreement, ULG is to make annual distributions to its members to be used to pay the members' tax liability associated with the members' ownership in ULG. ULG made distributions to the noncontrolling interest of $-0- and $773,442 during the years ended December 31, 2011 and 2010, respectively.

The results of Midwest's, UIFC's, and ULG's operations for the years ended December 31, 2011 and 2010 are included in the Company's consolidated statements of operations.

NOTE 14 – COMMITMENTS AND CONTINGENCIES

Commitments

The Bank is party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to fund lines of credit and credit card limits. The Bank's exposure to credit loss in the event of non-performance is equal to or less than the contractual amount of these instruments. The Bank follows the same credit policy to make such commitments as that followed by loans recorded in the consolidated financial statements.

The following is a summary of commitments:

	December 31,	
	2011	2010
Unused lines of credit	$ 1,609,744	$ 1,264,442
Unused credit card limits	569,683	827,124
	$ 2,179,427	$ 2,091,566

Legal Contingencies

Various legal claims may arise from time to time in the normal course of business, which, in the opinion of management, will not have a material effect on the Company's financial statements.

NOTE 15 – RELATED PARTY TRANSACTIONS

The Bank had loans outstanding of $74,999 and $-0- to officers and directors at December 31, 2011 and 2010, respectively. Available lines of credit to related parties at both December 31, 2011 and 2010, totaled $161,000, of which $94,806 and $102,904 had been borrowed against, respectively. Related party loans were made in the normal course of business and were performing pursuant to terms at December 31, 2011 and 2010.

The Bank had demand deposits of $295,722 and $443,110 from directors, officers and their affiliates as of December 31, 2011 and 2010, respectively.

NOTE 16 – FEDERAL HOME LOAN BANK ADVANCES

The Bank has a line of credit available from the FHLB in the amount of $3,000,000 as of both December 31, 2011 and 2010. There were no advances on this line of credit as of December 31, 2011 and 2010. Borrowings are secured by the pledge of specific mortgage loans held for investment along with FHLB stock, trading securities, and available-for-sale securities. As of both December 31, 2011 and 2010, the Bank had $3,000,000 of unutilized and available credit under the line of credit.

NOTE 17 – REGULATORY MATTERS

Dividend Restriction

Banking regulations require the maintenance of certain capital levels and limits the amount of dividends that may be paid by a bank to a holding company or by a holding company to shareholders. The Bank is currently required to get written consent prior to declaring or paying any dividend. The Bank paid $-0- and $50,000 dividends to the holding company, University Bancorp, Inc., during 2011 and 2010, respectively. University Bancorp, Inc. did not pay any dividends to common shareholders during 2011 or 2010.

Regulatory Capital Requirements

The Bank is subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional, discretionary actions by regulators that, if undertaken, could have a direct material effect on the Company’s consolidated financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of the Bank’s assets, liabilities, and certain off-balance-sheet items as calculated under regulatory accounting practices. The Bank’s capital amounts and classification are also subject to qualitative judgments by regulators about components, risk weightings, and other factors.

NOTE 17 – REGULATORY MATTERS (Continued)

Regulatory Capital Requirements (Continued)

The Bank is also subject to prompt corrective action capital requirement regulations set forth by the FDIC. The FDIC requires the Bank to maintain a minimum of total capital and Tier 1 capital (as defined) to risk-weighted assets (as defined), and of Tier 1 capital (as defined) to average total assets (as defined). As of December 31, 2011 and 2010, respectively, the Bank met all capital adequacy requirements to which it is subject.

The Bank's required and actual ratios and amounts of Tier 1 leverage, Tier 1 risk-weighted and total risk-weighted capital as of December 31 are as follows:

	Actual		To Be Adequately Capitalized Under Prompt Corrective Action Provisions		To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratios	Amount	Ratios	Amount	Ratios
As of December 31, 2011:						
Total capital (to risk-weighted assets)	$ 10,741,000	16.51%	$ 8,457,000	13.00%	$ 8,457,000	13.00%
Tier 1 capital (to risk-weighted assets)	9,922,000	15.25%	2,602,000	4.00%	3,903,000	6.00%
Tier 1 capital (to average assets)	9,922,000	8.90%	9,192,000	8.25%	9,192,000	8.25%
As of December 31, 2010:						
Total capital (to risk-weighted assets)	$ 11,519,000	18.74%	$ 7,989,000	13.00%	$ 7,989,000	13.00%
Tier 1 capital (to risk-weighted assets)	10,785,000	17.55%	2,458,000	4.00%	3,687,000	6.00%
Tier 1 capital (to average assets)	10,785,000	9.27%	9,594,000	8.25%	9,594,000	8.25%

NOTE 18 – OTHER CAPITAL REQUIREMENTS

The Bank, Midwest and ULG are subject to certain capital requirements in connection with seller/servicer agreements that these entities have entered into with secondary market investors. Failure to maintain minimum capital requirements could result in these entities' inability to originate and service loans for the respective investor and, therefore, could have a direct material effect on the Company's consolidated financial statements.

NOTE 18 – OTHER CAPITAL REQUIREMENTS (Continued)

The Bank's, Midwest's and ULG's actual capital amounts and the minimum amounts required for capital adequacy purposes, by investor, are as follows as of December 31, 2011:

	Actual Capital	Minimum Capital
Bank		
HUD	$ 10,493,791	$ 1,000,000
FHLMC	10,493,791	2,000,000
FNMA	10,493,791	2,585,316
Midwest		
HUD	$ 7,847,829	$ 1,000,000
FHLMC	7,847,829	2,000,000
FNMA	7,847,829	3,033,128
ULG		
HUD	$ 1,361,658	$ 1,000,000

As of December 31, 2011, Midwest and ULG were also each required to have a minimum of $200,000 in liquid assets under HUD liquidity requirements. As of December 31, 2011, Midwest was in compliance with this requirement, but ULG was not. As a result, in accordance with HUD requirements, management has instituted a corrective action plan to become compliant.

NOTE 19 - FAIR VALUE MEASUREMENTS

The ASC standards provide a single definition of fair value, together with a framework for measuring it, and require additional disclosure about the use of fair value to measure assets and liabilities. The standards also emphasize that fair value is a market-based measurement, not an entity-specific measurement, and sets out a fair value hierarchy with the highest priority being quoted prices in active markets. Under the standards, fair value measurements are disclosed by level within that hierarchy.

NOTE 19 - FAIR VALUE MEASUREMENTS (Continued)

The fair value standards define fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. A fair value measurement assumes that the transaction to sell the asset or transfer the liability occurs in the principal market for the asset or liability or, in the absence of a principal market, the most advantageous market for the asset or liability. The price in the principal (or most advantageous) market used to measure the fair value of the asset or liability shall not be adjusted for transaction costs. An orderly transaction is a transaction that assumes exposure to the market for a period prior to the measurement date to allow for marketing activities that are usual and customary for transactions involving such assets and liabilities; it is not a forced transaction. Market participants are buyers and sellers in the principal market that are (i) independent, (ii) knowledgeable, (iii) able to transact and (iv) willing to transact.

The fair value standards require the use of valuation techniques that are consistent with the market approach, the income approach and/or the cost approach. The market approach uses prices and other relevant information generated by market transactions involving identical or comparable assets and liabilities. The income approach uses valuation techniques to convert future amounts, such as cash flows or earnings, to a single present amount on a discounted basis. The cost approach is based on the amount that currently would be required to replace the service capacity of an asset (replacement cost). Valuation techniques should be consistently applied. Inputs to valuation techniques refer to the assumptions that market participants would use in pricing the asset or liability.

Inputs may be observable, meaning those that reflect the assumptions market participants would use in pricing the asset or liability developed based on market data obtained from independent sources, or unobservable, meaning those that reflect the reporting entity’s own assumptions about the assumptions market participants would use in pricing the asset or liability developed based on the best information available in the circumstances.

In that regard, the standards establish a fair value hierarchy for valuation inputs that gives the highest priority to quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. Determining which hierarchical level an asset or liability falls within requires significant judgment. The Company’s management evaluates its hierarchy disclosures. Hierarchical levels, as defined by the standards and directly related to the amount of subjectivity associated with the inputs to fair valuation of these assets and liabilities are as follows:

> Level 1: Quoted prices in active markets for identical assets or liabilities.
>
> Level 2: Observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

NOTE 19 - FAIR VALUE MEASUREMENTS (Continued)

Level 3: Unobservable inputs that are supported by little or no market activity and are significant to the fair value of the assets or liabilities.

Because valuation methodologies require the use of subjective assumptions, changes in these assumptions can materially affect fair value. Furthermore, the reported fair value amounts have not been comprehensively revalued since the presentation dates, and therefore, estimates of fair value after the balance sheet date may differ significantly from the amounts presented herein. A description of the valuation methodologies used by the Company for instruments measured at fair value, as well as the general classification of such instruments pursuant to the valuation hierarchy, is set forth below.

Trading and Available-for-Sale Securities

The fair value of the securities represents the amount the Company would realize upon sale of the mortgage backed securities currently in the portfolio. The Company receives current market values from The Federal Home Loan Bank on a monthly basis as part of its collateral positions. The securities are then marked to market every month based on these values. These securities are considered to be level 2 assets in the valuation hierarchy. Net unrealized gains and losses on available-for-sale securities are included in other comprehensive income. Net unrealized gains and losses on trading securities are included in earnings.

Loans Held for Sale – ULG and UIFC

The Company elected to account for ULG's and UIFC's loans held for sale at fair value under the ASC standards that permit the Company to choose to measure eligible items at fair value at specified election dates. Unrealized gains and losses on items for which the fair value measurement option has been elected are reported in earnings at each subsequent reporting date. The fair value option (i) may be applied instrument by instrument, with certain exceptions, thus the Company may record identical financial assets and liabilities at fair value or by another measurement basis permitted under GAAP, (ii) is irrevocable (unless a new election date occurs) and (iii) is applied only to entire instruments and not to portions of instruments.

Loans held for sale are recorded at fair value based on quoted market prices, where available, or are determined by discounting cash flows using interest rates approximating the Company's current origination rates for similar loans and adjusted to reflect the inherent credit risk. In most situations, these loans are locked into buckets to be sold under forward loan sales commitments (as discussed below), in which case the fair value of these loans held for sale are approximated by the value to be received soon thereafter under the forward sales commitments. Loans held for sale are considered to be level 2 assets in the valuation hierarchy. Net changes in the fair value of the Company's loans held for sale are included in earnings. The net gain on change in fair value of loans held for sale at December 31, 2011 and 2010 was $1,018,590 and $119,989, respectively, which is included in "Other income" in the consolidated statements of operations.

NOTE 19 - FAIR VALUE MEASUREMENTS (Continued)

Derivatives – Interest Rate Lock Commitments and Forward Commitments

The Company enters into IRLCs in connection with its mortgage banking activities to fund mortgage loans at specified times in the future. IRLCs that relate to the origination of mortgage loans that will be held for sale are considered derivative instruments as discussed in Note 1. As such, in accordance with ASC standards for derivative instruments, these IRLCs are recorded at fair value with changes in fair value recorded in earnings.

The Company estimates the fair value of an IRLC subsequent to inception of the commitment. In estimating the fair value of an IRLC, the Company assigns a probability to the loan commitment based on an expectation that it will be exercised and the loan will be funded. The fair value of IRLCs, while based on interest rates observable in the market, is highly dependent on the ultimate closing of the loans. These “pull-through” rates are based on ULG’s historical data and reflect an estimate of the likelihood that a commitment will ultimately result in a closed loan.

Also, the fair value of these commitments is derived from the fair value of the related mortgage loans which is based on unobservable data. Because these inputs are not transparent in market trades, IRLCs are considered to be level 3 assets or liabilities in the valuation hierarchy. Changes in the fair value of the IRLCs are recognized based on interest rate changes, changes in the probability that the commitment will be exercised, and the passage of time. Changes from the expected future cash flows related to the customer relationship or loan servicing are excluded from the valuation of IRLCs.

Outstanding IRLCs expose the Company to the risk that the price of the loans underlying the commitments might decline from inception of the interest rate lock to the funding of the loan. To protect against this risk, the Company utilizes forward loan sales commitments to economically hedge the risk of potential changes in the value of the loans that would result from the commitments. These forward sales commitments are considered derivative instruments as discussed in Note 1, and hence are valued at fair value with changes in fair value recorded in earnings.

The fair value of forward sales commitments is based primarily on the fluctuation of interest rates between the date on which the particular forward sales commitment was entered into and year end. Forward commitments are considered to be level 3 assets or liabilities in the valuation hierarchy.

NOTE 19 - FAIR VALUE MEASUREMENTS (Continued)

Mortgage Servicing Rights

The Company accounts for MSRs at fair value in accordance with the ASC standards for servicing rights as discussed in Note 1. The fair value of MSRs represents the amount that the Company would receive upon the sale of the MSRs. The Company receives an independent valuation of its MSRs on a quarterly basis. The fair value of MSRs is determined by projecting cash flows which are then discounted to estimate an expected fair value. The fair value of MSRs is impacted by a variety of factors, including prepayment assumptions, discount rates, delinquency rates, contractual specified servicing fees and underlying portfolio characteristics. Because these inputs are not transparent in market trades, MSRs are considered to be level 3 assets in the valuation hierarchy. Net changes in fair value of MSRs are included in earnings.

Other Real Estate Owned

Real estate properties acquired in collection of a loan are recorded at fair value upon foreclosure, establishing a new cost basis. After foreclosure, management periodically performs valuations to ensure real estate is carried at lower of cost or fair value, less estimated costs to sell. Fair value of the collateral is estimated by considering appraisals, which are updated on a periodic basis to reflect current housing market conditions.

The following tables summarize financial assets and liabilities measured at fair value on a recurring basis as of December 31, 2011 and 2010, segregated by the level of the valuation inputs within the fair value hierarchy utilized to measure fair value:

	Quoted Prices In Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
December 31, 2011			
Assets:			
Trading and available-for-sale securities	$ -	$ 3,366,472	$ -
Loans held for sale - ULG,UIFC	-	29,858,888	-
Mortgage servicing rights	-	-	2,452,156
Interest rate lock commitments	-	-	671,312
Total assets at fair value	$ -	$ 33,225,360	$ 3,123,468
Liabilities:			
Forward sales commitments	$ -	$ -	$ 110,331

NOTE 19 - FAIR VALUE MEASUREMENTS (Continued)

	Quoted Prices In Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
December 31, 2010			
Assets:			
Trading and available-for-sale securities	$ -	$ 3,899,262	$ -
Loans held for sale - ULG,UIFC	-	18,811,794	-
Mortgage servicing rights	-	-	2,929,514
Interest rate lock commitments	-	-	105,342
Forward sales commitments	-	-	1,670
Total assets at fair value	$ -	$ 22,711,056	$ 3,036,526

The table below includes a roll forward of the fair value of financial instruments that are classified by the Company within level 3 of the valuation hierarchy:

	Mortgage Servicing Rights	Interest Rate Lock Commitments	Forward Sales Commitments
Fair value at January 1, 2010	$ 2,465,243	$ (14,905)	$ 115,442
Purchases, sales, issuances, settlements, net	609,423	14,905	(115,442)
Net gains (losses)	(145,152)	105,342	1,670
Fair value December 31, 2010	2,929,514	105,342	1,670
Purchases, sales, issuances, settlements, net	904,450	(105,342)	(1,670)
Net gains (losses)	(1,381,808)	671,312	(110,331)
Fair value December 31, 2011	$ 2,452,156	$ 671,312	$ (110,331)

NOTE 19 - FAIR VALUE MEASUREMENTS (Continued)

The following table summarizes financial assets and liabilities measured at fair value on a nonrecurring basis:

	Quoted Prices In Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Year ended December 31, 2011			
Other real estate owned	$ -	$ 185,595	$ -
Year ended December 31, 2010			
Other real estate owned	$ -	$ 1,205,280	$ -

Other ASC standards require disclosure of the fair value of financial assets and financial liabilities, including those financial assets and financial liabilities that are not measured and reported at fair value on a recurring basis or non-recurring basis. The methodologies for estimating the fair value of financial assets and financial liabilities that are measured at fair value on a recurring or non-recurring basis are discussed above. The estimated fair value approximates carrying value for cash and cash equivalents, certificates of deposit, and Federal Home Loan Bank stock. The methodologies for other financial assets and financial liabilities are discussed below.

Loans and Financings Held for Sale, At Lower of Cost or Market and Loans and Financings, Net

The fair value of fixed-rate loans is estimated by discounting the future cash flows for each loan category using the current rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities. The fair value of adjustable-rate loans are assumed to approximate their carrying amount.

Deposits

The fair value of demand deposits and savings accounts is the amount payable on demand at the reporting date. The fair value of time deposits is estimated by discounting the future cash flows using the market rates offered for similar deposits with the same remaining maturities.

NOTE 19 - FAIR VALUE MEASUREMENTS (Continued)

The estimated fair values of financial instruments as of December 31, 2011 and 2010 are as follows (in thousands):

	December 31,			
	2011		2010	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Significant financial assets:				
Cash and due from banks	$ 9,053	$ 9,053	$ 13,595	$ 13,595
Certificates of deposit	6,250	6,250	6,250	6,250
Trading securities	785	785	965	965
Securities available-for-sale	2,581	2,581	2,934	2,934
Federal Home Loan Bank stock	1,072	1,072	1,197	1,197
Loans and financings, held for sale, at lower of cost or market	2,617	2,666	3,646	3,696
Loans and financings, held for sale, at fair value	29,859	29,859	18,812	18,812
Loans and financings, net	56,659	56,657	57,603	58,025
Mortgage servicing rights	2,452	2,452	2,930	2,930
Derivatives	671	671	107	107
Significant financial liabilities:				
Deposits:				
Demand - non-interest bearing	$ 56,210	$ 56,210	$ 59,311	$ 59,311
Demand - interest bearing and profit sharing	31,406	31,406	26,692	26,692
Savings	314	314	275	275
Time	13,595	13,832	13,336	13,508
Derivatives	110	110	-	-

NOTE 20 – BUSINESS COMBINATION

On March 9, 2011, ULG purchased 100% of the assets of Community Central Mortgage Company, LLC (the “Seller”) for total cash consideration of $150,000. This acquisition brought the Company four additional loan processing branches. As part of the Asset Purchase Agreement, the Company assumed all assets, all contracts, and real estate leases for three Indiana locations and one Michigan location. The identifiable assets acquired and liabilities assumed were recorded at fair value as of the acquisition date. The identifiable net assets acquired include office furniture and equipment with a fair value of $150,000. There were no liabilities assumed.

NOTE 21 – SEGMENT REPORTING

The Company's operations include four primary segments: retail banking (the Bank), retail mortgage banking (Midwest), retail mortgage banking (ULG), and the holding company, as discussed in Note 1. The Company's four reportable segments are strategic business units that are separately managed as they offer different products and services and have different marketing strategies. In addition, the Bank, Midwest and ULG each service a different customer base.

The segment financial information provided below has been derived from the internal profitability reporting system used by management to monitor and manage the financial performance of the Company. The accounting policies of the segments are the same as those described in the summary of significant accounting policies. The Company evaluates segment performance based on profit or loss before income taxes, not including nonrecurring gains and losses. Certain indirect expenses have been allocated based on actual volume measurements and other criteria, as appropriate. The Company accounts for transactions between segments at current market prices. Information about reportable segments as of and for the years ended December 31, 2011 and 2010 is as follows (in thousands):

2011

	Bank	Midwest	ULG	Holding Company	Consolidating Entries	Total
Interest and financing income	$ 4,225	$ 82	$ 519	$ -	$ (368)	$ 4,458
Net gain on sale of mortgage loans	1,661	698	4,391	-	-	6,750
Other non-interest income	(149)	7,532	1,960	-	730	10,073
Interest and profit sharing expense	498	30	374	-	(384)	518
Provision for loan losses	288	-	53	-	-	341
Salaries and benefits	4,382	3,920	5,654	-	-	13,956
Occupancy	371	216	391	-	-	978
Other operating expenses	2,498	2,662	1,956	14	(528)	6,602
Income (loss) before tax expense	(2,300)	1,484	(1,558)	(14)	1,274	(1,114)
Income tax expense (benefit)	(182)	522	-	-	(522)	(182)
Net income (loss)	(2,118)	962	(1,558)	(14)	1,796	(932)
Net income (loss) attributable to noncontrolling interests	-	-	-	-	(634)	(634)
Segment profit (loss)	$ (2,118)	$ 962	$ (1,558)	$ (14)	$ 2,430	$ (298)
Segment assets	$ 121,045	$ 11,099	$ 25,918	$ 6,947	$ (44,590)	$ 120,419
Capital expenditures	236	376	496	-	-	1,108
Depreciation and amortization	216	165	115	-	-	496

NOTE 21 – SEGMENT REPORTING (Continued)

2010	Bank	Midwest	ULG	Holding Company	Consolidating Entries	Total
Interest and financing income	$ 4,325	$ 120	$ 665	$ -	$ (438)	$ 4,672
Net gain on sale of mortgage loans	883	1,045	3,643	-	-	5,571
Other non-interest income	2,879	7,919	1,645	-	(2,249)	10,194
Interest and profit sharing expense	739	23	423	-	(438)	747
Provision for loan losses	877	-	14	-	-	891
Salaries and benefits	3,356	3,902	3,546	-	-	10,804
Occupancy	366	204	192	-	-	762
Other operating expenses	2,803	3,068	1,530	9	(484)	6,926
Income (loss) before tax expense	(54)	1,887	248	(9)	(1,765)	307
Income tax expense (benefit)	138	656	-	-	(656)	138
Net income (loss)	(192)	1,231	248	(9)	(1,109)	169
Net income (loss) attributable to noncontrolling interests	-	-	-	-	410	410
Segment profit (loss)	$ (192)	$ 1,231	$ 248	$ (9)	$ (1,519)	$ (241)
Segment assets	$ 121,942	$ 13,334	$ 19,595	$ 7,077	$ (44,682)	$ 117,266
Capital expenditures	382	186	72	-	-	640
Depreciation and amortization	277	141	54	-	-	472

NOTE 22 – PARENT COMPANY ONLY CONDENSED FINANCIAL INFORMATION

CONDENSED BALANCE SHEETS

	December 31, 2011	December 31, 2010
ASSETS		
Cash and cash equivalents	$ 19,692	$ 37,482
Investment in University Bank	6,881,112	6,821,598
Other assets	5,000	699
Total assets	$ 6,905,804	$ 6,859,779
LIABILITIES AND EQUITY		
Accounts payable and other liabilities	$ 58,596	$ 55,930
Preferred stock subject to mandatory redemption	960,050	880,140
Total liabilities	1,018,646	936,070
Total equity	5,887,158	5,923,709
Total liabilities and equity	$ 6,905,804	$ 6,859,779

NOTE 22 – PARENT COMPANY ONLY CONDENSED FINANCIAL INFORMATION (Continued)

CONDENSED STATEMENTS OF OPERATIONS

	December 31,	
	2011	**2010**
OTHER INCOME		
Interest and dividend income	$ 11	$ 9
EXPENSES		
Public listing	7,289	899
Professional fees	4,834	4,176
Other miscellaneous	1,798	3,521
Total expenses	13,921	8,596
Net loss before income taxes and net income of subsidiary	(13,910)	(8,587)
Income tax expense	-	-
Net loss before net income of subsidiary	(13,910)	(8,587)
Net loss of subsidiary	(283,884)	(232,618)
Net loss	$ (297,794)	$ (241,205)

NOTE 22 – PARENT COMPANY ONLY CONDENSED FINANCIAL INFORMATION (Continued)

CONDENSED STATEMENTS OF CASH FLOWS

	December 31, 2011	December 31, 2010
OPERATING ACTIVITIES		
Net loss	$ (297,794)	$ (241,205)
Adjustments to reconcile net loss to net cash flows from operating activities:		
Net change in:		
Other assets	(4,301)	-
Accounts payable and other liabilities	421	(4,509)
Net loss of subsidiary	283,884	232,618
Net cash used in operating activities	(17,790)	(13,096)
INVESTING ACTIVITY		
Dividend from University Bank	-	50,000
NET CHANGE IN CASH	(17,790)	36,904
Cash and Cash Equivalents, Beginning	37,482	578
Cash and Cash Equivalents, Ending	$ 19,692	$ 37,482
SUPPLEMENTAL DISCLOSURE OF NON-CASH TRANSACTIONS:		
Dividends payable on preferred stock converted to additional shares of preferred stock	$ 79,910	$ 74,020
Dividends declared that were recorded as dividends payable	$ 82,590	$ 77,370
Issuance of common stock to acquire Bank's noncontrolling interest	$ 323,565	$ -