

Edgar Filing: First Federal of Northern Michigan Bancorp, Inc. - Form 10QSB

First Federal of Northern Michigan Bancorp, Inc.
Form 10QSB
August 14, 2007

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-QSB

QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT
OF 1934

FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2007

OR

TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE
ACT OF 1934

For the transition period from _____ to _____

Commission File Number 000-31957

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

MARYLAND
(State or other jurisdiction of
incorporation or organization)

32-0135202
(I.R.S. Employer
Identification No.)

100 S. SECOND AVENUE, ALPENA, MICHIGAN 49707
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: (989) 356-9041

Check whether the issuer (1) filed all reports required to be filed by
Section 13 or 15(d) of the Securities Exchange Act of 1934 during the past 12
months (or for such shorter period that the registrant was required to file such
reports) and (2) has been subject to such filing requirements for the past 90
days. Yes No

Indicate by check mark whether the registrant is a shell company (as
defined in Rule 12b-2 of the Exchange Act). Yes No

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

Common Stock, Par Value \$0.01 (Title of Class)	Outstanding at August 8, 2007 2,883,749 shares
--	---

Transitional Small Business Disclosure Format: Yes No

Edgar Filing: First Federal of Northern Michigan Bancorp, Inc. - Form 10QSB

1

FIRST FEDERAL OF NORTHERN MICHIGAN BANCORP, INC.
FORM 10-QSB
QUARTER ENDED JUNE 30, 2007

INDEX

	PAGE

PART I -- FINANCIAL INFORMATION	
ITEM 1 - UNAUDITED FINANCIAL STATEMENTS	
Consolidated Balance Sheet at June 30, 2007 and December 31, 2006.....	3
Consolidated Statements of Income for the Three and Six Months Ended June 30, 2007 and June 30, 2006.....	4
Consolidated Statement of Changes in Stockholders' Equity for the Six Months Ended June 30, 2007.....	5
Consolidated Statements of Cash Flows for the Six Months Ended June 30, 2007 and June 30, 2006.....	6
Notes to Unaudited Consolidated Financial Statements.....	7
ITEM 2 - MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION.....	16
ITEM 3 - CONTROLS AND PROCEDURES.....	22
PART II - OTHER INFORMATION	
ITEM 1 - LEGAL PROCEEDINGS.....	23
ITEM 2 - UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS.....	23
ITEM 3 - DEFAULTS UPON SENIOR SECURITIES.....	23
ITEM 4 - SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.....	23
ITEM 5 - OTHER INFORMATION.....	23
ITEM 6 - EXHIBITS.....	24
Section 302 Certifications	
Section 906 Certifications	

When used in this Form 10-QSB or future filings by First Federal of Northern Michigan Bancorp, Inc. (the "Company") with the Securities and Exchange Commission ("SEC"), in the Company's press releases or other public or stockholder communications, or in oral statements made with the approval of an authorized executive officer, the words or phrases "would be," "will allow," "intends to," "will likely result," "are expected to," "will continue," "is anticipated," "estimate," "project," or similar expressions are intended to identify "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995.

The Company wishes to caution readers not to place undue reliance on any such forward-looking statements, which speak only as of the date made, and to advise readers that various factors, including regional and national economic conditions, changes in levels of market interest rates, credit and other risks of lending and investment activities and competitive and regulatory factors, could affect the Company's financial performance and could cause the Company's actual results for future periods to differ materially from those anticipated or projected.

Edgar Filing: First Federal of Northern Michigan Bancorp, Inc. - Form 10QSB

The Company does not undertake, and specifically disclaims any obligation, to update any forward-looking statements to reflect occurrences or unanticipated events or circumstances after the date of such statements.

2

PART I - FINANCIAL INFORMATION
ITEM 1 - FINANCIAL STATEMENTS

FIRST FEDERAL OF NORTHERN MICHIGAN BANCORP, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEET

	June 30, 2007	December 31, 2006
	-----	-----
	(Unaudited)	
ASSETS		
Cash and cash equivalents:		
Cash on hand and due from banks	\$ 3,224,509	\$ 4,448,661
Overnight deposits with FHLB	1,224,152	1,224,152
	-----	-----
Total cash and cash equivalents	4,448,661	4,448,661
Securities AFS	31,650,388	31,650,388
Securities HTM	2,795,000	2,795,000
Loans held for sale	226,447	226,447
Loans receivable, net of allowance for loan losses of \$2,201,398 and \$2,079,069 as of June 30, 2007 and December 31, 2006, respectively ..	204,346,405	209,346,405
Foreclosed real estate and other repossessed assets	561,173	561,173
Real estate held for investment	135,543	135,543
Federal Home Loan Bank stock, at cost	4,196,900	4,196,900
Premises and equipment	7,912,082	7,912,082
Accrued interest receivable	1,814,879	1,814,879
Intangible assets	2,341,269	2,341,269
Goodwill	1,396,854	1,396,854
Other assets	2,292,532	2,292,532
	-----	-----
Total assets	\$264,118,133	\$280,118,133
	=====	=====
LIABILITIES AND STOCKHOLDERS' EQUITY		
Liabilities:		
Deposits	\$169,520,641	\$177,520,641
Advances from borrowers for taxes and insurance	343,473	343,473
Federal Home Loan Bank advances and Note Payable	48,688,395	48,688,395
Borrowings at fair value	9,889,000	9,889,000
Accrued expenses and other liabilities	1,794,055	1,794,055
	-----	-----
Total liabilities	230,235,564	245,235,564
	-----	-----
Stockholders' equity:		
Common stock (\$0.01 par value 20,000,000 shares authorized 3,190,999 shares issued)	31,910	31,910
Additional paid-in capital	24,293,617	24,293,617
Retained earnings	14,144,168	14,144,168
Treasury stock at cost (307,750 and 156,000 shares, respectively)	(2,963,918)	(2,963,918)

Edgar Filing: First Federal of Northern Michigan Bancorp, Inc. - Form 10QSB

Unallocated ESOP	(1,009,277)	(1
Unearned compensation	(467,950)	
Accumulated other comprehensive loss	(145,981)	
	-----	-----
Total stockholders' equity	33,882,569	35
	-----	-----
Total liabilities and stockholders' equity	\$264,118,133	\$280
	=====	=====

See accompanying notes to consolidated financial statements.

3

FIRST FEDERAL OF NORTHERN MICHIGAN BANCORP, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF INCOME

	For the Three Months Ended June 30,		For the Six Ended June	
	2007	2006	2007	
	(Unaudited)		(Unaudite	
Interest income:				
Interest and fees on loans	\$3,601,249	\$3,607,804	\$7,187,176	\$7
Interest and dividends on investments	436,514	547,520	946,363	1
Interest on mortgage-backed securities	22,235	53,014	69,335	
	-----	-----	-----	-----
Total interest income	4,059,999	4,208,338	8,202,875	8
	-----	-----	-----	-----
Interest expense:				
Interest on deposits	1,377,441	1,326,612	2,809,351	2
Interest on borrowings	737,095	757,110	1,539,181	1
	-----	-----	-----	-----
Total interest expense	2,114,536	2,083,722	4,348,532	3
	-----	-----	-----	-----
Net interest income	1,945,463	2,124,617	3,854,343	4
Provision for loan losses	113,351	133,000	198,980	
	-----	-----	-----	-----
Net interest income after provision for loan losses	1,832,112	1,991,617	3,655,363	4
	-----	-----	-----	-----
Non Interest income:				
Service charges and other fees	215,961	283,984	412,975	
Mortgage banking activities	111,547	93,590	199,430	
Gain (loss) on sale of available-for-sale investments	--	(43,565)	--	
Net gain (loss) on sale of premises and equipment, real estate owned and other repossessed assets ...	(10,585)	1,750	(12,418)	
Other	13,409	1,708	25,337	
Net gain on trading activities	176,424	--	166,800	
Insurance & brokerage commissions	649,179	738,417	1,341,998	1
	-----	-----	-----	-----
Total other income	1,155,934	1,075,884	2,134,123	2
	-----	-----	-----	-----
Non interest expenses:				
Compensation and employee benefits	1,522,100	1,614,006	3,090,927	3
SAIF insurance premiums	5,366	6,045	10,866	

Edgar Filing: First Federal of Northern Michigan Bancorp, Inc. - Form 10QSB

Advertising	44,803	81,623	85,321	
Occupancy	376,323	332,806	743,940	
Amortization of intangible assets	123,314	124,880	248,195	
Service bureau charges	87,640	91,591	163,585	
Insurance & brokerage commission expense	233,398	279,133	474,198	
Professional services	90,627	75,083	170,906	
Other	327,667	314,513	612,998	
	-----	-----	-----	
Other expenses	2,811,238	2,919,681	5,600,937	5
	-----	-----	-----	
Income before income tax expense	176,808	147,820	188,549	
Income tax (benefit) expense	35,143	49,310	23,150	
	-----	-----	-----	
Net income	\$ 141,665	\$ 98,510	\$ 165,400	\$
	=====	=====	=====	=====
Per share data:				
Basic earnings per share	\$ 0.05	\$ 0.03	\$ 0.06	\$
Weighted average number of shares outstanding	2,900,329	3,136,545	2,966,449	3
Diluted earnings per share	\$ 0.05	\$ 0.03	\$ 0.06	\$
Weighted average number of shares outstanding, including dilutive stock options	2,899,318	3,137,591	2,965,634	3
Dividends per common share	\$ 0.050	\$ 0.05	\$ 0.10	\$

See accompanying notes to consolidated financial statements.

4

FIRST FEDERAL OF NORTHERN MICHIGAN BANCORP INC. AND SUBSIDIARIES
Consolidated Statement of Changes in Stockholders' Equity (Unaudited)

	Common Stock	Treasury Stock	Additional Paid-in Capital	Unearned Compensation	Retained Earnings	Unallocat ESOP
	-----	-----	-----	-----	-----	-----
Balance at December 31, 2006	\$31,910	\$ (1,565,359)	\$24,284,606	\$ (551,856)	\$14,576,468	\$ (1,059,1
Cumulative effect of change in accounting principal (Note 1)...					(303,938)	
Treasury Stock at Cost (151,750 shares).....	--	(1,398,559)	--	--	--	--
Stock Options/Awards Expensed.....	--	--	13,008	83,906	--	--
Unallocated ESOP.....	--	--	(3,997)	--	--	49,8
Net income for the period.....	--	--	--	--	165,400	--
Changes in unrealized loss: on available-for-sale securities (net of tax of \$60,749).....	--	--	--	--	--	--
Total comprehensive						

Edgar Filing: First Federal of Northern Michigan Bancorp, Inc. - Form 10QSB

income.....	--	--	--	--	--	--
Dividends declared.....	--	--	--	--	--	(293,762)
Balance at June 30,						
2007.....	\$31,910	\$(2,963,918)	\$24,293,617	\$(467,950)	\$14,144,168	\$(1,009,2
	=====	=====	=====	=====	=====	=====

See accompanying notes to the consolidated financial statements.

FIRST FEDERAL OF NORTHERN MICHIGAN BANCORP, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF CASH FLOWS

	For Six Months En June 30,	
	2007	2006
	(Unaudited)	
Cash flows from operating activities:		
Net income	\$ 165,400	\$ 3,000
Adjustments to reconcile net income to net cash from operating activities:		
Depreciation and amortization	553,651	5,000
Provision for loan loss	198,980	2,000
Amortization and accretion on securities	13,976	
Loss on sale of securities	--	
Net Gain from Trading Activities.....	(166,800)	
Originations of loans held for sale	(7,247,856)	(6,700,000)
Principal amount of loans sold	7,093,409	6,400,000
Proceeds from sale of real estate held for sale	74,138	2,000
Gain on sale of real estate held for investment	(937)	(2,000)
Loss on sale of premises and equipment	24,076	
Change in accrued interest receivable	323,788	3,000
Change in other assets	320,842	3,000
Change in accrued expenses and other liabilities.....	(567,517)	(8,000)
Stock options/awards expensed	96,914	
Net cash provided by operating activities	882,064	6,000
Net (increase) decrease in loans	4,972,683	(8,500,000)
Proceeds from maturity and sale of available-for-sale securities	11,502,911	8,500,000
Purchase of securities	(1,045,000)	(1,900,000)
Purchase of premises and equipment	(325,439)	(7,000)
Net cash provided by (used in) investing activities	15,105,155	(2,700,000)
Net Increase in deposits	(7,537,352)	(2,200,000)
Dividend paid on common stock	(293,762)	(3,000)
ESOP shares committed to be released	45,856	
Net increase in advances from borrowers	299,084	3,000
Additions to advances from Federal Home Loan Bank and notes payable ...	22,500,000	9,600,000
Repayments of Federal Home Loan Bank advances and notes payable	(30,146,626)	(4,100,000)
Stock retired	--	(
Proceeds from exercise of stock options	--	

Edgar Filing: First Federal of Northern Michigan Bancorp, Inc. - Form 10QSB

Purchase of treasury shares	(1,398,559)	(1,1
	-----	-----
Net cash provided by (used in) financing activities	(16,531,359)	2,1
	-----	-----
Net increase (decrease) in cash and cash equivalents	(544,140)	
Cash and cash equivalents at beginning of period	4,992,801	4,7
	-----	-----
Cash and cash equivalents at end of period	\$ 4,448,661	\$ 4,8
	=====	=====
Supplemental disclosure of cash flow information:		
Cash paid during the period for income taxes	\$ 165,500	\$
	=====	=====
Cash paid during the period for interest	\$ 4,381,252	\$ 1,9
	=====	=====

See accompanying notes to the consolidated financial statements.

6

FIRST FEDERAL OF NORTHERN MICHIGAN BANCORP, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

NOTE 1--SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES.

The accompanying consolidated financial statements have been prepared on an accrual basis of accounting and include the accounts of First Federal of Northern Michigan Bancorp, Inc. and its wholly owned subsidiary, First Federal of Northern Michigan (the "Bank") and the Bank's wholly owned subsidiaries Financial Service and Mortgage Corporation ("FSMC") and the InsuranCenter of Alpena ("ICA"). FSMC invests in real estate that includes leasing, selling, developing, and maintaining real estate properties. ICA is a licensed insurance agency engaged in the business of property, casualty and health insurance. All significant intercompany balances and transactions have been eliminated in the consolidation.

These interim financial statements are prepared without audit and reflect all adjustments, which, in the opinion of management, are necessary to present fairly the consolidated financial position of the Company at June 30, 2007, and its results of operations and statement of cash flows for the periods presented. All such adjustments are normal and recurring in nature. The accompanying consolidated financial statements do not purport to contain all the necessary financial disclosures required by generally accepted accounting principles that might otherwise be necessary and should be read in conjunction with the consolidated financial statements and notes thereto of the Company included in the Annual Report for the year ended December 31, 2006. Results for the three and six months ended June 30, 2007 are not necessarily indicative of the results that may be expected for the year ending December 31, 2007.

CRITICAL ACCOUNTING POLICIES

Our accounting and reporting policies are prepared in accordance with accounting principles generally accepted in the United States of America and conform to general practices within the banking industry. We consider accounting policies that require significant judgment and assumptions by management that have, or could have, a material impact on the carrying value of certain assets or on income to be critical accounting policies. Changes in underlying factors,

Edgar Filing: First Federal of Northern Michigan Bancorp, Inc. - Form 10QSB

assumptions or estimates could have a material impact on our future financial condition and results of operations. Based on the size of the item or significance of the estimate, the following accounting policies are considered critical to our financial results.

Allowance for Loan Losses. The allowance for loan losses is calculated with the objective of maintaining an allowance sufficient to absorb estimated probable loan losses. Management's determination of the adequacy of the allowance is based on periodic evaluations of the loan portfolio and other relevant factors. However, this evaluation is inherently subjective, as it requires an estimate of the loss content for each risk rating and for each impaired loan, an estimate of the amounts and timing of expected future cash flows, and an estimate of the value of collateral.

We have established a systematic method of periodically reviewing the credit quality of the loan portfolio in order to establish an allowance for losses on loans. The allowance for losses on loans is based on our current judgments about the credit quality of individual loans and segments of the loan portfolio. The allowance for losses on loans is established through a provision for loan losses based on our evaluation of the losses inherent in the loan portfolio, and considers all known internal and external factors that affect loan collectibility as of the reporting date. Our evaluation, which includes a review of all loans on which full collectibility may not be reasonably assured, considers among other matters, the estimated net realizable value or the fair value of the underlying collateral, economic conditions, historical loan loss experience, our knowledge of inherent losses in the portfolio that are probable and reasonably estimable and other factors that warrant recognition in providing an appropriate loan loss allowance. Management believes this is a critical accounting policy because this evaluation involves a high degree of complexity and requires us to make subjective judgments that often require assumptions or estimates about various matters. Historically, we believe our estimates and assumptions have proven to be relatively accurate.

7

The analysis of the allowance for loan losses has two components: specific and general allocations. Specific allocations are made for loans that are determined to be impaired. Impairment is measured by determining the present value of expected future cash flows or, for collateral-dependent loans, the fair value of the collateral adjusted for market conditions and selling expenses. The general allocation is determined by segregating the remaining loans by type of loan, risk weighting (if applicable) and payment history. We also analyze delinquency trends, which have remained stable, general economic conditions and geographic and industry concentrations. This analysis establishes factors that are applied to the loan groups to determine the amount of the general reserve. The principal assumption used in deriving the allowance for loan losses is the estimate of loss content for each risk rating. As an example, if recent loss experience dictated that the projected loss ratios would be changed by 10% (of the estimate) across all risk ratings, the allocated allowance as of June 30, 2007 would have changed by approximately \$205,000. Actual loan losses may be significantly more than the allowances we have established, which could have a material negative effect on our financial results.

Mortgage Servicing Rights. We sell to investors a portion of our originated one- to four-family residential real estate mortgage loans. When we acquire mortgage servicing rights through the origination and sale of mortgage loans with servicing rights retained, we allocate a portion of the total cost of the mortgage loans to the mortgage servicing rights based on their relative fair value. As of June 30, 2007, we were servicing loans sold to others totaling

Edgar Filing: First Federal of Northern Michigan Bancorp, Inc. - Form 10QSB

\$134.0 million. We amortize capitalized mortgage servicing rights as a reduction of servicing fee income in proportion to, and over the period of, estimated net servicing income by use of a method that approximates the level-yield method. We periodically evaluate capitalized mortgage servicing rights for impairment using a model that takes into account several variables including expected prepayment speeds and prevailing interest rates. If we identify impairment, we charge the amount of the impairment to earnings by establishing a valuation allowance against the capitalized mortgage servicing rights asset. The primary risk of material changes to the value of the servicing rights resides in the potential volatility in the economic assumptions used, particularly the prepayment speed. We monitor this risk and adjust the valuation allowance as necessary to adequately record any probable impairment in the portfolio. Management believes the estimation of these variables makes this a critical accounting policy. For purposes of measuring impairment, the mortgage servicing rights are stratified based on financial asset type and interest rates. In addition, we obtain an independent third-party valuation of the mortgage servicing portfolio on a quarterly basis. In general, the value of mortgage servicing rights increases as interest rates rise and decreases as interest rates fall. This is because the estimated life and estimated income from a loan increase as interest rates rise and decrease as interest rates fall. The key economic assumptions made in determining the fair value of the mortgage servicing rights at June 30, 2007 included the following:

Annual constant prepayment speed (CPR):	10.14%
Weighted average life remaining (in months):	245
Discount rate used:	8.50%

At the June 30, 2007 valuation, we calculated the value of our mortgage servicing rights to be \$1.4 million and the weighted average life remaining of those rights was 48 months. The book value of our mortgage servicing rights as of June 30, 2007 was \$550,000 which was \$844,000 less than the independent valuation, so there was no need to establish a valuation allowance.

Impairment of Intangible Assets. Goodwill arising from business acquisitions represents the value attributable to unidentifiable intangible elements in the business acquired. The fair value of goodwill is dependent upon many factors, including our ability to provide quality, cost-effective services in the face of competition. Because of these many factors, management believes this is a critical accounting policy. A decline in earnings as a result of business or market conditions or a run-off of customers over sustained periods could lead to an impairment of goodwill that could adversely affect earnings in future periods.

A significant portion of our intangible assets, including goodwill, relates to the acquisition premiums recorded with the purchase of the ICA and certain branches over the last several years. Intangible assets are reviewed periodically for impairment by comparing the fair value of the intangible asset to the book value of the intangible asset. If the book value is in excess of the fair value, impairment is indicated and the intangibles must be written down to their fair value.

In connection with our acquisition in 2003 of ICA, we allocated the excess of the purchase price paid over the fair value of net assets acquired to intangible assets, including goodwill. These intangible assets included the ICA

Edgar Filing: First Federal of Northern Michigan Bancorp, Inc. - Form 10QSB

customer list and a third-party contract to which ICA is a party. From the date of acquisition through April 30, 2005 we amortized the value assigned to the customer list and contract over a period of 20 years. On May 1, 2005 the former owner of ICA retired. As a result, the amortization period for these intangible assets was reduced to a 10 year period beginning May 1, 2005. Effective January 1, 2006, the exclusive third-party contract between ICA and Blue Cross Blue Shield of Michigan was terminated. Prior to January 1, 2006 the ICA exclusive agent contract with Blue Cross Blue Shield entitled ICA to an override commission of 1.9% on all health premiums written through local Chambers of Commerce in Northeast Michigan. On any health insurance contracts in place as of December 31, 2005, ICA will continue to receive the 1.9% commission; however, there will be no new groups added to this program effective January 1, 2006. Management considered the potential effect this could have on ICA health insurance commissions in future years and made the decision to reduce the amortization period of the third-party contract intangible asset to 5 years effective January 1, 2006.

Goodwill is not amortized. The impairment test of goodwill and identified intangible assets that have an indefinite useful life, performed as of June 30, 2007 and December 31, 2006 in accordance with SFAS No. 142, did not indicate that an impairment charge was required. If, through testing, we determine that there is impairment based, for example, on significant runoff of the customer list or material changes to the third-party contract, then we may determine to reduce the recorded value of those intangible assets, which would increase expense and reduce our earnings.

In connection with branch office acquisitions, we assigned the excess of the purchase price over the fair value of the assets acquired to a core deposit intangible. The core deposit intangible is tested periodically for impairment. Our original estimates for the expected life of the deposits have proven to be relatively accurate as evidenced by the fact that no impairment has been recorded. If we determine through testing that a significant portion of the acquired customers no longer do business with us, then the asset would be deemed to be impaired thereby requiring a charge to earnings to the extent appropriate given all of the known factors. We amortize core deposit intangibles over a period of between 10 and 15 years.

Financial Accounting Standard Number 159 -- The Fair Value Option for Financial Assets and Financial Liabilities. In February 2007, FASB issued FAS 159, The Fair Value Option for Financial Assets and Financial Liabilities. FAS 159 is effective for fiscal years beginning after November 15, 2007. Early adoption is permitted subject to specific requirements outlined in the new Statement. Calendar-year companies are able to adopt FAS 159 for their first quarter 2007 financial statements.

The new Statement allows entities to choose, at specified election dates, to measure eligible financial assets and liabilities at fair value that are not otherwise required to be measured at fair value. If a company elects the fair value option for an eligible item, changes in that item's fair value in subsequent reporting periods must be recognized in current earnings. FAS 159 also establishes presentation and disclosure requirements designed to draw comparison between entities that elect different measurement attributes for similar assets and liabilities.

The Company early adopted FAS 159 and FAS 157 as of January 1, 2007. Upon adoption of FAS 159, the Company selected the fair value measurement option for various existing financial assets, including certain "available-for-sale" securities and puttable FHLB advances.

The available-for-sale securities totaled \$4.9 million and represented 10.9% of the securities portfolio. The initial fair value measurement of the securities elected for FAS 159 resulted in a \$140,000 pre-tax cumulative-effect

Edgar Filing: First Federal of Northern Michigan Bancorp, Inc. - Form 10QSB

adjustment recorded as a reduction in retained earnings as of January 1, 2007. Under SFAS 159, this one-time charge will not be recognized in current earnings.

As a result of the fair value measurement election for these securities, the Company recorded gains in first six months of 2007 of \$7,000. The Company has since sold these investments at a gain of \$21,000. The Company intends to replace these investments with like investments, which will be recorded at fair value. We

9

believe that the adoption of the standard will have a positive impact on our ability to manage interest rate risk and potentially benefit interest income during the remainder of 2007 as well as future periods.

The Company also elected the adoption of FAS 159 for \$10.0 million in putable Federal Home Loan Bank advances. The initial fair value measurement of the advances resulted in a \$320,000 pre-tax, charge to retained earnings. In the first six month of 2007 the Company recorded \$139,000 in pre-tax mark-to-market gains related to these advances.

The above investment securities and advances were chosen for the fair value option based on the desire of the Company to improve its net interest margin and reduce interest rate risk. Subsequent to the adoption of SFAS 159, the Company plans on repositioning its balance sheet by obtaining new investment securities and Federal Home Loan Bank advances that improve overall interest rate margin and mitigate future interest rate risk. The Company anticipates that the replacement of the securities and advances with new instruments will achieve the reduced interest rate risk since they will be better matched in relation to maturity. The new investment securities and advances will both be carried at fair value. The Company anticipates that by the end of the third calendar quarter approximately \$8.0 to \$10.0 million of securities and advances will be carried at fair value on the balance sheet.

The early adoption of SFAS 159 also allows management more flexibility in mitigating interest rate risk on subsequent transactions. The Company is considering the use of the fair value option on future investment security transactions, loan transactions and the related funding instruments.

The Company will continue to separately recognize interest income and expense in accordance with existing policies for the items selected.

The following table represents all items in which the fair value option was elected as of January 1, 2007 and the impact on the financial statements.

Par Value		Impact on Retained Earnings Effective 1/1/2007	Impact on Net Income Three Months Ended 6/30/2007	Impact on Net Income Six Months Ended 6/30/2007
(dollars in thousands)		(dollars in thousands)		
\$ 4,856	Investment Securities	(\$140)	\$ 21	\$ 28
\$10,000	FHLB Advances	(\$320)	\$155	\$139
	Total	(\$460)	\$176	\$167

Edgar Filing: First Federal of Northern Michigan Bancorp, Inc. - Form 10QSB

Adjusted for Taxes (\$304) \$116 \$110

Financial Accounting Standard Number 157 Fair Value Measurements. In September 2006, FASB issued FAS 157, Fair Value Measurements. This statement establishes a framework for measuring fair value in accordance with generally accepted accounting principles, clarifies the definition of fair value within that framework, and expands disclosures about the use of fair value measurements. FAS 157 is effective for fiscal years beginning after November 15, 2007. Upon adoption of FAS 159, the Company concurrently adopted the provisions of FAS 157 as of January 1, 2007. Accordingly, the Company has developed a framework to measure the fair value of financial assets and financial liabilities and expanded disclosures in accordance with the requirements.

The following information pertains to assets and liabilities measured by fair value on a recurring basis:

10

Description	Fair Value as of January 1, 2007	Change in fair value recognized in other income for the six month period ended June 30, 2007	Fair Value as of June 30, 2007	Quoted Prices in active markets for Identical Assets/Liabilities (Level 1)	Significant Other Observations Input (Level 1)
(Dollars in thousands)					
Investments accounted for under FVO	\$ 4,864	\$ 21	\$ 0	\$ 0	
FHLB advances	\$10,044	\$155	\$9,889	\$9,889	

RECENT ACCOUNTING PRONOUNCEMENTS

In March 2006, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standard No. 156, Accounting for Servicing of Financial Assets - an amendment of FASB Statement No. 140. SFAS 156 amends SFAS Statement No.140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities", with respect to the accounting for separately recognized servicing assets and servicing liabilities. The Statement addresses the recognition and measurement of separately recognized servicing assets and liabilities and provides an approach to simplify efforts to obtain hedge-like (offset) accounting. SFAS 156 was adopted by the Company on January 1, 2007 as required by the statement. The adoption of SFAS 156 did not have a material effect on the financial position, results of operations, or cash flows.

In July 2006, the FASB issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes -- an interpretation of FASB Statement No. 109 (FIN 48), which clarifies the accounting for uncertainty in tax positions. This Interpretation requires that the Company recognize in the financial statements the impact of a tax position if that position is more likely than not to be sustained on audit based on technical merits of the position. The provisions of FIN 48 are effective as of the beginning of the Company's 2007 fiscal year, with the cumulative effect of the change in accounting principle recorded as an adjustment to operating retained earnings. The adoption of FIN 48 did not have a material effect on the financial position, results of operations, or cash flows.

Edgar Filing: First Federal of Northern Michigan Bancorp, Inc. - Form 10QSB

NOTE 2--REORGANIZATION.

On April 1, 2005, we consummated the second-step mutual-to-stock conversion of Alpena Bancshares, M.H.C., in which shares of common stock representing Alpena Bancshares, M.H.C.'s ownership interest in Alpena Bancshares, Inc. were sold to investors. As a result of the conversion and stock offering, Alpena Bancshares, M.H.C. ceased to exist and Alpena Bancshares, Inc. was succeeded by First Federal of Northern Michigan Bancorp, Inc., a Maryland corporation and new holding company for First Federal of Northern Michigan.

The plan of conversion and reorganization of Alpena Bancshares, M.H.C. and the issuance and contribution of cash and common stock to First Federal Community Foundation, a charitable foundation established by the Company, were approved by the stockholders of Alpena Bancshares, Inc. and the members of Alpena Bancshares, M.H.C. on March 23, 2005.

First Federal of Northern Michigan Bancorp, Inc. accepted orders to purchase 1,699,869 shares of common stock at a purchase price of \$10.00 per share. As a part of the conversion, public stockholders of the Company as of the consummation date received 1.8477 shares of First Federal of Northern Michigan Bancorp, Inc. common stock in exchange for each of their existing shares of Alpena Bancshares, Inc. common stock. Cash was issued in lieu of any fractional shares. The share exchange occurred on April 1, 2005.

NOTE 3--DIVIDENDS.

Payment of dividends on the common stock is subject to determination and declaration by the Board of Directors and depends upon a number of factors, including capital requirements, regulatory limitations on

11

the payment of dividends, the Company's results of operations and financial condition, tax considerations and general economic conditions.

On June 12, 2007, the Company declared a cash dividend on its common stock, payable on or about July 20, 2007, to shareholders of record as of June 30, 2007, equal to \$0.05 per share. The dividend on all shares outstanding totaled \$144,187.

NOTE 4--1996 STOCK OPTION PLAN, 1996 RECOGNITION AND RETENTION PLAN AND 2006 STOCK-BASED INCENTIVE PLAN.

Effective January 1, 2006, the Company adopted Statement of Financial Accounting Standard (SFAS) No. 123 (Revised) "Shareholder Based Payments", which requires that the grant-date fair value of awarded stock options be expensed over the requisite service period. The Company's 1996 Stock Option Plan (the "1996 Plan"), which was approved by shareholders, permits the grant of share options to its employees for up to 127,491 shares of common stock (retroactively adjusted for the exchange ratio applied in the Company's 2005 stock offering and related second-step conversion). The Company's 2006 Stock-Based Incentive Plan (the "2006 Plan"), which was approved by the shareholders on May 17, 2006, permits the award of up to 242,740 shares of common stock of which the maximum number to be granted as Stock Options is 173,386 and the maximum that can be granted as Restricted Stock Awards is 69,354. Option awards are granted with an exercise price equal to the market price of the Company's stock at the date of grant; those option awards generally vest based on five years of continual service and have ten year contractual terms. Certain options provide for

Edgar Filing: First Federal of Northern Michigan Bancorp, Inc. - Form 10QSB

accelerated vesting if there is a change in control (as defined in the Plans).

During the three months ended June 30, 2007 the Company awarded 5,000 shares under the Recognition and Retention Plan ("RRP"). Shares issued under the RRP and exercised pursuant to the exercise of the stock option plan may be either authorized but unissued shares or reacquired shares held by the Company as treasury stock.

STOCK OPTIONS - A summary of option activity under the Plan during the six months ended June 30, 2007 is presented below:

Options -----	Shares -----	Weighted- Average Exercise Price -----	Weighted-Average Remaining Contractual Term (Years) -----	Aggregate Intrinsic Value -----
Outstanding at January 1, 2007	204,532	\$9.50		
Granted	5,000	\$9.07		
Exercised	0	N/A		
Forfeited or expired	(8,140)	\$9.54		
Outstanding at June 30, 2007	201,392	\$9.25	8.61	\$ 0
Exercisable at June 30, 2007	43,712	\$9.29	7.30	-\$11,802

A summary of the status of the Company's nonvested shares as of June 30, 2007, and changes during the six months ended June 30, 2007, is presented below:

12

Nonvested Shares -----	Shares -----	Weighted-Average Grant-Date Fair Value -----
Nonvested at January 1, 2007	200,099	\$2.11
Granted	5,000	\$2.07
Vested	(39,359)	\$2.10
Forfeited	(8,140)	-\$2.10
Nonvested at June 30, 2007	157,600	\$2.11

As of June 30, 2007 there was \$352,000 of total unrecognized compensation cost, net of expected forfeitures, related to nonvested options under the Plan. That cost is expected to be recognized over a weighted-average period of 4.45 years. The total fair value of shares vested during the six months ended June 30, 2007 was \$82,650.

RESTRICTED STOCK AWARDS - As of June 30, 2007 there was \$477,000 of unrecognized compensation cost related to nonvested restricted stock awards under the plan.

NOTE 5 -- COMMITMENTS TO EXTEND CREDIT

Edgar Filing: First Federal of Northern Michigan Bancorp, Inc. - Form 10QSB

The Company is a party to credit-related financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit, stand by letters of credit, and commercial lines of credit. Such commitments involve, to varying degrees, elements of credit and interest rate risk in excess of the amounts recognized in the consolidated balance sheet. The Company's exposure to credit loss is represented by the contracted amount of these commitments. The Company follows the same credit policies in making commitments as it does for on-balance sheet instruments.

At June 30, 2007, the Company had outstanding commitments to originate loans of \$39.2 million. These commitments included \$7.5 million for permanent one-to-four family dwellings, \$10.5 million for non-residential loans, \$1.0 million of undisbursed loan proceeds for construction of one-to-four family dwellings, \$8.1 million of undisbursed lines of credit on home equity loans, \$1.7 million of unused credit card lines, \$6.2 million of unused commercial lines of credit, \$2.3 million of undisbursed commercial construction, \$275,000 of unused letters of credit and \$1.7 million in unused Bounce Protection.

NOTE 6 -- SUBSEQUENT EVENTS

NONE

NOTE 7 -- SEGMENT REPORTING

The Company's principal activities include banking through its wholly owned subsidiary, First Federal of Northern Michigan, and the sale of insurance products through its indirect wholly owned subsidiary, ICA, purchased in 2003. The Bank provides financial products including retail and commercial loans as well as retail and commercial deposits. ICA receives commissions from the sale of various insurance products including health, life, and property. The segments were determined based on the nature of the products provided to customers.

The financial information for each operating segment is reported on the basis used internally to evaluate performance and allocate resources. The allocations have been consistently applied for all periods presented. Revenues and expenses between affiliates have been transacted at rates that unaffiliated parties would pay. The only transaction between the segments thus far relates to a deposit on behalf of ICA included in the Bank. The interest income and interest expense for this transaction has been eliminated. All other transactions are with external customers. The performance measurement of the operating segments is based on the management structure of the Company and is not necessarily comparable with similar information for

13

any other financial institution. The information presented is also not necessarily indicative of the segment's financial condition and results of operations if they were independent entities.

For the Three Months Ended
June 30, 2007
(Dollars in Thousands)

Bank	ICA	Eliminations	Tot

Edgar Filing: First Federal of Northern Michigan Bancorp, Inc. - Form 10QSB

INTEREST INCOME	\$ 4,060	\$ 5	\$ (5)	\$ 4,
INTEREST EXPENSE	2,118	2	(5)	2,
	-----	-----	-----	-----
NET INTEREST INCOME - Before provision for loan losses	1,942	3	--	1,
PROVISION FOR LOAN LOSSES	113	--	--	
	-----	-----	-----	-----
NET INTEREST INCOME - After provision for loan losses	1,829	3	--	1,
OTHER INCOME	499	657	--	1,
OPERATING EXPENSES	2,132	679	--	2,
	-----	-----	-----	-----
INCOME - Before federal income tax	196	(19)	--	
FEDERAL INCOME TAX	42	(7)	--	
	-----	-----	-----	-----
NET INCOME	\$ 154	\$ (12)	\$ --	\$
	=====	=====	=====	=====
DEPRECIATION AND AMORTIZATION	\$ 189	\$ 86	\$ --	\$
	=====	=====	=====	=====
ASSETS	\$260,371	\$4,468	\$ (721)	\$264,
	=====	=====	=====	=====
EXPENDITURES RELATED TO LONG-LIVED ASSETS:				
Goodwill	\$ --	\$ --	\$ --	\$
Intangible assets	--	--	--	
Property and equipment	97	7	--	
	-----	-----	-----	-----
TOTAL	\$ 97	\$ 7	\$ --	\$
	=====	=====	=====	=====

For the Three Months Ended
June 30, 2006
(Dollars in Thousands)

	Bank	ICA	Eliminations	Tot
	-----	-----	-----	-----
INTEREST INCOME	\$ 4,209	\$ 3	\$ (3)	\$ 4,
INTEREST EXPENSE	2,082	5	(3)	2,
	-----	-----	-----	-----
NET INTEREST INCOME - Before provision for loan losses	2,127	(2)	--	2,
PROVISION FOR LOAN LOSSES	132	--	--	
	-----	-----	-----	-----
NET INTEREST INCOME - After provision for loan losses	1,995	(2)	--	1,
OTHER INCOME	336	740	--	1,
OPERATING EXPENSES	2,095	825	--	2,
	-----	-----	-----	-----
INCOME - Before federal income tax	236	(87)	--	
FEDERAL INCOME TAX	80	(30)	--	
	-----	-----	-----	-----
NET INCOME	\$ 156	\$ (57)	\$ --	\$
	=====	=====	=====	=====
DEPRECIATION AND AMORTIZATION	\$ 171	\$ 86	\$ --	\$
	=====	=====	=====	=====
ASSETS	\$280,378	\$4,464	\$ (572)	\$284,
	=====	=====	=====	=====
EXPENDITURES RELATED TO LONG-LIVED ASSETS:				
Goodwill	\$ --	\$ --	\$ --	\$
Intangible assets	--	--	--	
Property and equipment	456	3	--	
	-----	-----	-----	-----
TOTAL	\$ 456	\$ 3	\$ --	\$

Edgar Filing: First Federal of Northern Michigan Bancorp, Inc. - Form 10QSB

14

	For the Six Months Ended June 30, 2007 (Dollars in Thousands)			
	Bank	ICA	Eliminations	Tot
INTEREST INCOME	\$ 8,203	\$ 11	\$ (11)	\$ 8,
INTEREST EXPENSE	4,355	5	(11)	4,
NET INTEREST INCOME - Before provision for loan losses	3,848	6	--	3,
PROVISION FOR LOAN LOSSES	199	--	--	
NET INTEREST INCOME - After provision for loan losses	3,649	6	--	3,
OTHER INCOME	783	1,351	--	2,
OPERATING EXPENSES	4,241	1,360	--	5,
INCOME - Before federal income tax	191	(3)	--	
FEDERAL INCOME TAX	24	(1)	--	
NET INCOME	\$ 167	\$ (2)	\$ --	\$
DEPRECIATION AND AMORTIZATION	\$ 382	\$ 172	\$ --	\$
ASSETS	\$260,371	\$4,468	\$ (721)	\$264,
EXPENDITURES RELATED TO LONG-LIVED ASSETS:				
Goodwill	\$ --	\$ --	\$ --	\$
Intangible assets	--	--	--	
Property and equipment	144	23	--	
TOTAL	\$ 144	\$ 23	\$ --	\$

	For the Six Months Ended June 30, 2006 (Dollars in Thousands)			
	Bank	ICA	Eliminations	Tot
INTEREST INCOME	\$ 8,242	\$ 7	\$ (7)	\$ 8,
INTEREST EXPENSE	3,990	10	(7)	3,
NET INTEREST INCOME - Before provision for loan losses	4,252	(3)	--	4,
PROVISION FOR LOAN LOSSES	202	--	--	
NET INTEREST INCOME - After provision for loan losses	4,050	(3)	--	4,
OTHER INCOME	692	1,510	--	2,

Edgar Filing: First Federal of Northern Michigan Bancorp, Inc. - Form 10QSB

OPERATING EXPENSES	4,334	1,447	--	5,
	-----	-----	-----	-----
INCOME - Before federal income tax	408	60	--	
FEDERAL INCOME TAX	137	20	--	
	-----	-----	-----	-----
NET INCOME	\$ 271	\$ 40	\$ --	\$
	=====	=====	=====	=====
DEPRECIATION AND AMORTIZATION	\$ 343	\$ 172	\$ --	\$
	=====	=====	=====	=====
ASSETS	\$280,378	\$4,464	\$ (572)	\$284,
	=====	=====	=====	=====
EXPENDITURES RELATED TO LONG-LIVED ASSETS:				
Goodwill	\$ --	\$ --	\$ --	\$
Intangible assets	--	--	--	
Property and equipment	748	21	--	
	-----	-----	-----	-----
TOTAL	\$ 748	\$ 21	\$ --	\$
	=====	=====	=====	=====

15

FIRST FEDERAL OF NORTHERN MICHIGAN BANCORP, INC. AND SUBSIDIARIES

PART I - FINANCIAL INFORMATION

ITEM 2 - MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATIONS

The following discussion compares the consolidated financial condition of the Company at June 30, 2007 and December 31, 2006, and the results of operations for the three- and six-month periods ended June 30, 2007 and 2006. This discussion should be read in conjunction with the interim financial statements and footnotes included herein.

OVERVIEW

For the quarter ended June 30, 2007, the Company's earnings were \$141,700, or \$0.05 per basic and diluted share, compared to earnings of \$98,500, or \$0.03 per basic and diluted share, for the year earlier period, an increase of \$43,200.

Total assets decreased by \$16.8 million, or 6.0% from December 31, 2006 to June 30, 2007. Investment securities available for sale decreased by \$11.4 million from December 31, 2006 to June 30, 2007. Net loans receivable decreased \$5.2 million during the six months ended June 30, 2007. Total deposits decreased \$7.5 million, or 4.3% from December 31, 2006 to June 30, 2007. Federal Home Loan Bank advances decreased by \$17.4 million from December 31, 2006 to June 30, 2007, which included a reclassification of \$10.3 million to a trading account as part of our early adoption of FAS 159. Equity decreased by \$1.6 million, or 4.4% from December 31, 2006 to June 30, 2007.

COMPARISON OF FINANCIAL CONDITION AT JUNE 30, 2007 AND DECEMBER 31, 2006

ASSETS: Total assets decreased \$16.8 million, or 6.0%, to \$264.1 million at June 30, 2007 from \$280.9 million at December 31, 2006. Investment securities available for sale decreased \$11.5 million, or 26.6% from December 31, 2006 to June 30, 2007, due to the maturity of \$6.6 million in AFS investment securities during the six months ended June 30, 2007, the proceeds of which were used to

Edgar Filing: First Federal of Northern Michigan Bancorp, Inc. - Form 10QSB

pay-down high-cost FHLB advances, and due to the reclassification of \$4.7 million in AFS securities to trading securities in connection with our early adoption of FAS 159 effective January 1, 2007. As noted above, the trading securities were subsequently sold during the quarter ended June 30, 2007. Net loans receivable decreased \$5.2 million, or 2.5%, to \$204.3 million at June 30, 2007 from \$209.5 million at December 31, 2006. The decrease in net loans was attributable primarily to the payoff of a few large commercial loans.

LIABILITIES: Deposits decreased \$7.5 million, or 4.3%, to \$169.5 million at June 30, 2007 from \$177.1 million at December 31, 2006. The decrease was primarily in certificate of deposit balances, reflecting continued competition for deposits and increased pressure on market deposit rates. Total FHLB advances decreased \$7.4 million to \$57.5 million at June 30, 2007 from December 31, 2006 due to the maturity and sale of investment securities, the proceeds of which were used to pay down advances. At January 1, 2007 we reclassified \$10.3 million in FHLB advances to a trading account in connection with our early adoption of FAS 159.

EQUITY: Stockholders' equity decreased to \$33.9 million at June 30, 2007 from \$35.5 million at December 31, 2006, a decline of \$1.6 million. During the three months ended June 30, 2007, the Company repurchased 113,150 shares of its common stock at a total cost of \$1,040,073, concluding its stock repurchase program which was announced and commenced in March 2007. As a result of this program, the Company repurchased a total of 151,750 shares at a total cost of \$1,398,558. Dividends

16

were \$144,000 and \$294,000 for the three and six months ended June 30, 2007, respectively. As mentioned in the previous quarter, the Company chose to restructure its balance sheet through an early adoption of FAS 159, resulting in a \$461,000 one-time cumulative-effect adjustment to retained earnings during the quarter ended March 31, 2007. The unrealized loss on available for sale securities, net of tax, was \$146,000 at June 30, 2007 as compared to \$264,000 at December 31, 2006, an improvement of \$118,000. The cumulative loss in value on securities was due to changes in interest rates and was not considered by management to be other than temporary.

RESULTS OF OPERATIONS

THREE MONTHS ENDED JUNE 30, 2007 COMPARED TO THREE MONTHS ENDED JUNE 30, 2006

GENERAL: Net income increased by \$43,200 to \$141,700 for the three months ended June 30, 2007 from \$98,500 for the same period ended June 30, 2006.

INTEREST INCOME: Interest income decreased to \$4.1 million for the three months ended June 30, 2007 from \$4.2 million for the year earlier period, due mainly to a decrease of \$20.4 million in the average balance of interest-earnings assets to \$248.1 million for the three month period ended June 30, 2007 from \$268.5 million for the three month period ended June 30, 2006. This was partially offset by an increase in the yield on interest earning assets of 28 basis points to 6.56% three month period over three month period.

INTEREST EXPENSE: Interest expense increased to \$2.1 million for the three months ended June 30, 2007 from \$2.0 million for the three months ended June 30, 2006. The increase in interest expense for the three month period was due primarily to an increase in the cost of our certificates of deposits. The cost of these deposits increased from 3.94% from the three months ended June 30, 2006 to 4.50% for the three months ended June 30, 2007 as lower costing deposits matured and were re-priced at a higher rate, reflecting continued upward market

Edgar Filing: First Federal of Northern Michigan Bancorp, Inc. - Form 10QSB

pressure on deposit rates. In addition, the cost of our FHLB advances increased 3 basis points from 4.88% for the three months ended June 30, 2006 to 4.91% for the three months ended June 30, 2007.

NET INTEREST INCOME: Net interest income decreased to \$1.9 million for the three month period ended June 30, 2007 compared to \$2.1 million for the same period in 2006. For the three months ended June 30, 2007, average interest-earning assets decreased \$20.4 million, or 7.7%, when compared to the same period in 2006. Average interest-bearing liabilities decreased \$17.9 million, or 7.5%, to \$218.9 million for the quarter ended June 30, 2007 from \$236.7 million for the quarter ended June 30, 2006. The yield on average interest-earning assets increased to 6.56% for the three month period ended June 30, 2007 from 6.28% for the same period ended in 2006 while the cost of average interest-bearing liabilities increased to 3.86% from 3.51% for the three month periods ended June 30, 2007 and 2006, respectively. The net interest margin decreased to 3.15% for the three month period ended June 30, 2007 from 3.18% for same period in 2006.

PROVISION FOR LOAN LOSSES: The allowance for loan losses is established 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 provision for loan losses amounted to \$113,400 for the three month period ended June 30, 2007 and \$133,000 for the comparable period in 2006. Although the provision for loan loss was moderately lower in the quarter ended June 30, 2007 than in the year earlier period, the Company does continue to experience a high level of classified assets due to the current somewhat weak economic conditions in the northern Michigan market as well as declining real estate values. Classified assets are monitored quarterly and the loan loss reserve is adjusted as needed to reflect any changes in the

17

status of classified assets.

NON INTEREST INCOME: Non interest income increased from \$1.1 million for the three months ended June 30, 2006 to \$1.2 million for the three months ended June 30, 2007, primarily due to the gain on trading activities associated with our early adoption of FAS 159, partially offset by decreases in insurance brokerage income and service charges and other fees.

NON INTEREST EXPENSE: Non interest expense decreased from \$2.9 million for the three months ended June 30, 2006 to \$2.8 million for the three months ended June 30, 2007. The decreases period over period were mainly the result of a reduction in compensation and benefit expenses due to the closure last year of one of our under-performing branches and other cost-cutting measures, as well as a reduction in insurance brokerage commission expense.

INCOME TAXES: The Company had a federal income tax expense of \$35,100 for the three months ended June 30, 2007 due to tax-exempt interest income in excess of pre-tax income, compared to federal income tax expense of \$49,300 for the same period in 2006. Effective for tax years beginning on or after January 1, 2008,

Edgar Filing: First Federal of Northern Michigan Bancorp, Inc. - Form 10QSB

the State of Michigan has repealed the Single Business Tax and replaced it with the Michigan Business Tax. This change is not expected to materially impact the Company's earnings.

SIX MONTHS ENDED JUNE 30, 2007 COMPARED TO SIX MONTHS ENDED JUNE 30, 2006

GENERAL: Net income decreased by \$145,000 to \$165,400 for the six months ended June 30, 2007 from \$310,700 for the same period ended June 30, 2006.

INTEREST INCOME: Interest income remained stable six month period over six month period, despite a decrease in the average balance of interest-earning assets of \$12.9 million to \$253.9 million from the six month period ended June 30, 2006 from the six month period ended June 30, 2007. This was attributable to an increase in yield on interest earning assets of 29 basis points to 6.49% six month period over six month period. Notably, the yield on mortgage loans increased 10 basis points six month period over six month period to 6.19% over an average balance of \$103.2 million while the yield on investment securities increased 53 basis points to 4.51% over an average balance of \$35.3 million.

INTEREST EXPENSE: Interest expense for the six months ended June 30, 2007 increased to \$4.3 million from \$4.0 million for the six months ended June 30, 2006. The increase in interest expense for the six month period was due primarily to an increase in the cost of our certificates of deposit. The cost of these deposits increased from 3.82% for the six months ended June 30, 2006 to 4.51% for the six months ended June 30, 2007, as lower costing deposits matured and were re-priced at a higher rate, reflecting continued upward market pressure on deposit rates. In addition, the cost of our FHLB advances increased 20 basis points from 4.80% for the six months ended June 30, 2006 to 5.00% for the six months ended June 30, 2007.

NET INTEREST INCOME: Net interest income decreased to \$394,000 for the six month period ended June 30, 2007 compared to the same period in 2006. For the six months ended June 30, 2007, average interest-earning assets decreased \$12.9 million, or 4.8%, when compared to the same period in 2006. Average interest-bearing liabilities decreased \$11.1 million, or 4.7%, to \$224.3 million for the six month period ended June 30, 2007 from \$235.4 million for the six month period ended June 30, 2006. The yield on average interest-earning assets increased to 6.49% for the six month period ended June 30, 2007 from 6.20% for the same period ended in 2006 while the cost of average interest-bearing liabilities increased to 3.90% from 3.40% for the six month periods ended June 30, 2007 and 2006, respectively. The net interest margin decreased to 3.05% for the six month period ended June 30, 2007 from 3.20% for same period in 2006.

DELINQUENT LOANS AND NONPERFORMING ASSETS. The following table sets forth information regarding loans delinquent 90 days or more and real estate owned/other repossessed assets of the Bank at the dates indicated. As of the dates indicated, the Bank did not have any material restructured loans within the meaning of SFAS 15.

18

	JUNE 30, 2007	DECEMBER 31, 2006
	-----	-----
	(Dollars in thousands)	
Total non-accrual loans	\$3,885	\$2,490

Edgar Filing: First Federal of Northern Michigan Bancorp, Inc. - Form 10QSB

	-----	-----
Accrual loans delinquent 90 days or more:		
One- to four-family residential	231	645
Other real estate loans	40	221
Consumer/Commercial	681	624
	-----	-----
Total accrual loans delinquent 90 days or more ..	\$ 952	\$1,490
	-----	-----
Total nonperforming loans (1)	4,837	3,980
Total real estate owned-residential mortgages (2)	483	437
Total real estate owned-Consumer and other (2)	78	38
	=====	=====
Total nonperforming assets	\$5,398	\$4,455
	=====	=====
Total nonperforming loans to loans receivable	2.34%	1.90%
Total nonperforming assets to total assets	2.04%	1.59%

(1) All of the Bank's loans delinquent more than 90 days are classified as nonperforming.

(2) Represents the net book value of property acquired by the Bank through foreclosure or deed in lieu of foreclosure. Upon acquisition, this property is recorded at the lower of its fair market value or the principal balance of the related loan.

PROVISION FOR LOAN LOSSES: The provision for loan losses amounted to \$198,900 for the six month period ended June 30, 2007 and \$202,500 for the comparable period in 2006. The ratio of nonperforming loans to total loans was 2.34% and 1.90% at June 30, 2007 and December 31, 2006, respectively. As a percent of total assets, nonperforming loans increased to 2.04% at June 30, 2007 from 1.59% at December 31, 2006. Total nonperforming assets increased to \$5.4 million at June 30, 2007 from \$4.5 million at December 31, 2006.

NON INTEREST INCOME: Non interest income decreased from \$2.2 million for the six months ended June 30, 2006 to \$2.1 million for the six months ended June 30, 2007. The decrease was primarily in the areas of insurance brokerage commission and service charges and other fees, offset by a gain on trading activities during the six months ended June 30, 2007.

NON INTEREST EXPENSE: Non interest expense decreased from \$5.8 million for the six months ended June 30, 2006 to \$5.6 million for the six months ended June 30, 2007. The decrease period over period was mainly the result of a reduction in compensation and benefit expenses due to the closure last year of one of our under-performing branches and other cost-cutting measures, as well as a reduction in insurance brokerage commission expense.

INCOME TAXES: The Company had a federal income tax expense of \$23,100 for the six months ended June 30, 2007 due to tax-exempt interest income in excess of pre-tax income, compared to federal income tax expense of \$156,700 for the same period in 2006.

LIQUIDITY

The Company's current liquidity position is expected to be more than adequate to fund expected asset growth. The Company's primary sources of funds are deposits, FHLB advances, proceeds from principal and interest payments, prepayments on loans and mortgage-backed and investment securities and sale of long-term fixed-rate mortgages into the secondary market. While maturities and scheduled amortization of loans and mortgage-backed securities are a predictable source of funds, deposit flows, mortgage prepayments and sale of mortgage loans into the secondary market are greatly influenced by general interest rates, economic

Edgar Filing: First Federal of Northern Michigan Bancorp, Inc. - Form 10QSB

conditions and competition.

Liquidity represents the amount of an institution's assets that can be quickly and easily converted into cash without significant loss. The most liquid assets are cash, short-term U.S. Government securities, U.S. Government agency securities and certificates of deposit. The Company is required to maintain sufficient levels of liquidity as defined by OTS regulations. This requirement may be varied at the direction of the

19

OTS. Regulations currently in effect require that the Bank must maintain sufficient liquidity to ensure its safe and sound operation. The Company's objective for liquidity is to be above 20%. Liquidity as of June 30, 2007 was \$49.5 million, or 30.5% compared to \$52.2 million, or 29.5% at December 31, 2006. The levels of these assets are dependent on the Company's operating, financing, lending and investing activities during any given period. The liquidity calculated by the Company includes additional borrowing capacity available with the FHLB. This borrowing capacity is based on the FHLB stock owned by the Bank along with pledged collateral. As of June 30, 2007, the Bank had unused borrowing capacity totaling \$25.8 million at the FHLB based on the FHLB stock ownership.

The Company intends to retain for its portfolio certain originated residential mortgage loans (primarily adjustable rate, balloon and shorter term fixed rate mortgage loans) and to generally sell the remainder in the secondary market. The Bank will from time to time participate in or originate commercial real estate loans, including real estate development loans. During the six month period ended June 30, 2007 the Company originated \$12.1 million in residential mortgage loans, of which \$7.2 million were retained in portfolio while the remainder were sold in the secondary market or are being held for sale. This compares to \$17.2 million in originations during the first six months of 2007 of which \$10.0 million were retained in portfolio. The Company also originated \$14.9 million of commercial loans and \$5.2 million of consumer loans in the first six months of 2007 compared to \$12.6 million of commercial loans and \$8.3 million of consumer loans for the same period in 2006. Of total loans receivable, excluding loans held for sale, mortgage loans comprised 49.5% and 40.4%, commercial loans 36.1% and 37.6% and consumer loans 14.4% and 14.0% at June 30, 2007 and June 30, 2006, respectively.

Deposits are a primary source of funds for use in lending and for other general business purposes. At June 30, 2007 deposits funded 64.2% of the Company's total assets compared to 63.0% at December 31, 2006. Certificates of deposit scheduled to mature in less than one year at June 30, 2007 totaled \$80.8 million. Management believes that a significant portion of such deposits will remain with the Bank. The Bank monitors the deposit rates offered by competition in the area and sets rates that take into account the prevailing market conditions along with the Bank's liquidity position. Moreover, management believes that the growth in assets is not expected to require significant in-flows of liquidity. As such, the Bank does not expect to be a market leader in rates paid for liabilities.

Borrowings may be used to compensate for seasonal or other reductions in normal sources of funds or for deposit outflows at more than projected levels. Borrowings may also be used on a longer-term basis to support increased lending or investment activities. At June 30, 2007 the Company had \$57.5 million in FHLB advances. FHLB borrowings as a percentage of total assets were 21.8% at June 30, 2007 as compared to 15.3% at December 31, 2006. The Company has sufficient available collateral to obtain additional advances of \$16.3 million. When this

Edgar Filing: First Federal of Northern Michigan Bancorp, Inc. - Form 10QSB

is combined with current FHLB stock ownership the Company could obtain up to an additional \$25.8 million in advances from the FHLB.

CAPITAL RESOURCES

Stockholders' equity at June 30, 2007 was \$33.9 million, or 12.8% of total assets, compared to \$35.5 million, or 12.6% of total assets, at December 31, 2006 (See "Consolidated Statement of Changes in Stockholders' Equity"). The Bank is subject to certain capital-to-assets levels in accordance with OTS regulations. The Bank exceeded all regulatory capital requirements at June 30, 2007. The following table summarizes the Bank's actual capital with the regulatory capital requirements and with requirements to be "Well Capitalized" under prompt corrective action provisions, as of June 30, 2007:

20

	Actual		Regulatory Minimum		Minimum to be Well Capitalized	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
Dollars in Thousands						
Tier 1 (Core) capital						
(to risk - weighted assets)	\$28,435	10.93%	\$10,410	4.00%	\$13,012	5.00%
Total risk-based capital						
(to risk - weighted assets)	\$30,704	16.55%	\$14,844	8.00%	\$18,555	10.00%
Tier 1 risk-based capital						
(to tangible assets)	\$28,435	15.32%	\$ 7,422	4.00%	\$11,133	6.00%
Tangible Capital						
(to tangible assets)	\$28,435	10.93%	\$ 3,904	1.50%	\$ 5,205	2.00%

21

FIRST FEDERAL OF NORTHERN MICHIGAN BANCORP, INC.
FORM 10-QSB
QUARTER ENDED JUNE 30, 2007

PART I - FINANCIAL INFORMATION

ITEM 3 - CONTROLS AND PROCEDURES

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

Edgar Filing: First Federal of Northern Michigan Bancorp, Inc. - Form 10QSB

SEC's rules and forms and in timely alerting them to material information relating to the Company (or its consolidated subsidiaries) required to be included in its periodic SEC filings.

There were no significant changes made in the Company's internal control over financial reporting or in other factors that could significantly affect the Company's internal controls over financial reporting during the period covered by this report that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

22

FIRST FEDERAL OF NORTHERN MICHIGAN BANCORP, INC.
FORM 10-QSB
QUARTER ENDED JUNE 30, 2007

PART II -- OTHER INFORMATION

Item 1 - Legal Proceedings:

There are no material legal proceedings to which the Company is a party or of which any of its property is subject. From time to time the Company is a party to various legal proceedings incident to its business.

Item 2 - Unregistered Sales of Equity Securities and Use of Proceeds:

- (a) Not applicable
- (b) Not applicable
- (c) On March 15, 2007 the Company announced a share repurchase program authorizing the repurchase of up to 151,750 shares of the Company's outstanding common stock. All repurchases under the Company's share repurchase program were transacted in the open market and were within the scope of Rule 10b-18, which provides a safe harbor for purchases in a given day if an issuer of equity securities satisfies the manner, timing, price and volume conditions of the rule when repurchasing its own common shares in the open market. The following table summarizes the Company's share repurchase activity for the three months ended June 30, 2007.

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Max Shares Purc Pla
4/1/2007 to 4/30/2007	113,150	9.19	--	
5/1/2007 to 5/31/2007	--	--	--	
6/1/2007 to 6/30/2007	--	--	--	
Total	113,150	9.19	--	

Edgar Filing: First Federal of Northern Michigan Bancorp, Inc. - Form 10QSB

Item 3 - Defaults upon Senior Securities: Not applicable.

Item 4 - Submission of Matters to a Vote of Security Holders:

The annual meeting of the shareholders of the Company was held on May 17, 2006. The results of the vote were as follows:

1. The following individual was elected as director for a three (3) year term:

	Votes For -----	Votes Withheld -----
Keith D. Wallace	2,032,171	591,957

2. The ratification of the appointment of Plante & Moran, PLLC as independent auditors of the Company for the fiscal year ending December 31, 2007:

	For -----	Against -----	Abstain -----
Number of Votes	2,489,561	111,358	23,209

Item 5 - Other Information: Not applicable

23

Item 6 - Exhibits

Exhibit 31.1 Certification by Chief Executive Officer pursuant to section 302 of the Sarbanes-Oxley Act of 2002

Exhibit 31.2 Certification by Chief Financial Officer pursuant to section 302 of the Sarbanes-Oxley Act of 2002

Exhibit 32.1 Statement of Chief Executive Officer furnished pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

Exhibit 32.2 Statement of Chief Financial Officer furnished pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

24

FIRST FEDERAL OF NORTHERN MICHIGAN BANCORP, INC.
FORM 10-QSB
QUARTER ENDED JUNE 30, 2007

SIGNATURES

Edgar Filing: First Federal of Northern Michigan Bancorp, Inc. - Form 10QSB

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

FIRST FEDERAL OF NORTHERN MICHIGAN BANCORP, INC.

By: /s/ Martin A. Thomson

Martin A. Thomson
Chief Executive Officer

Date: August 14, 2007

By: /s/ Amy E. Essex

Amy E. Essex, Chief Financial Officer
(Principal Financial and Accounting Officer)

Date: August 14, 2007