

Northeast Indiana Bancorp, Inc.

Accountants' Report and Consolidated Financial Statements

December 31, 2008 and 2007

Northeast Indiana Bancorp, Inc.

December 31, 2008 and 2007

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Independent Accountants' Report

Audit Committee of the Board of Directors
Northeast Indiana Bancorp, Inc.
Huntington, Indiana

We have audited the accompanying consolidated balance sheets of Northeast Indiana Bancorp, Inc. as of December 31, 2008 and 2007, and the related consolidated statements of income, shareholders' equity and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these 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 financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Northeast Indiana Bancorp, Inc. as of December 31, 2008 and 2007, 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.

As discussed in Note 16, the Company changed its method of accounting for fair value measurements in accordance with Statement of Financial Accounting Standards No. 157 in 2008.

BKD, LLP

Indianapolis, Indiana
March 27, 2009

Northeast Indiana Bancorp, Inc.
Consolidated Balance Sheets
December 31, 2008 and 2007

Assets

	<u>2008</u>	<u>2007</u>
Interest-earning cash and cash equivalents	\$ 6,122,439	\$ 9,283,966
Noninterest-earning cash and cash equivalents	2,284,062	1,102,808
Cash and cash equivalents	8,406,501	10,386,774
Available-for-sale securities	28,168,302	30,349,086
Held-to-maturity securities	550,000	-
Loans receivable, net of allowance for loan losses of \$1,750,605 in 2008 and \$2,712,378 in 2007	204,171,179	186,412,561
Loans held for sale	709,400	-
Accrued interest receivable	1,070,708	1,101,878
Premises and equipment, net	2,178,416	2,352,834
FHLB Stock	4,704,200	4,704,200
Investments in limited liability partnerships	462,279	677,235
Cash surrender value of life insurance	6,253,417	6,008,230
Goodwill	130,972	130,972
Other intangible assets	87,354	112,326
Other assets	3,346,794	3,556,910
	<u>\$ 260,239,522</u>	<u>\$ 245,793,006</u>

Liabilities and Shareholders' Equity

Liabilities

Deposits		
Demand - noninterest-bearing	\$ 19,873,896	\$ 10,270,655
Savings	11,697,906	15,905,483
Negotiable order of withdrawal	33,792,126	29,809,755
Money market demand account	5,716,915	3,829,834
Time	84,617,922	81,312,835
Total deposits	<u>155,698,765</u>	<u>141,128,562</u>
Borrowed funds	79,982,575	79,563,712
Accrued expenses and other liabilities	2,782,849	2,073,715
Total liabilities	<u>238,464,189</u>	<u>222,765,989</u>

Shareholders' Equity

Preferred stock, no par value, 500,000 shares authorized; 0 shares issued	-	-
Common stock, \$.01 par value; 4,000,000 shares authorized; 2,593,988 shares issued - 2008 and 2007; 2008 - 1,230,670 shares outstanding; 2007 - 1,313,917 shares outstanding	26,407	26,407
Additional paid-in capital	29,790,224	29,760,894
Retained earnings, substantially restricted	13,336,427	13,933,331
Accumulated other comprehensive income (loss), net of tax	143,373	(170,156)
Treasury stock, at cost; 2008 - 1,363,318 shares 2007 - 1,280,071 shares	<u>(21,521,098)</u>	<u>(20,523,459)</u>
Total shareholders' equity	<u>21,775,333</u>	<u>23,027,017</u>
	<u>\$ 260,239,522</u>	<u>\$ 245,793,006</u>

Northeast Indiana Bancorp, Inc.
Consolidated Statements of Income
Years Ended December 31, 2008 and 2007

	2008	2007
Interest Income		
Loans, including fees	\$ 12,754,938	\$ 11,928,797
Taxable securities	1,470,906	1,547,720
Non-taxable securities	137,256	145,209
Deposits with financial institutions	98,840	334,307
Total interest income	14,461,940	13,956,033
Interest Expense		
Deposits	4,372,725	4,583,600
Borrowed funds	3,408,189	4,423,786
Total interest expense	7,780,914	9,007,386
Net Interest Income	6,681,026	4,948,647
Provision for Loan Losses	430,000	1,290,000
Net Interest Income After Provision for Loan Losses	6,251,026	3,658,647
Noninterest Income		
Service charges on deposit accounts	702,798	696,961
Net gains (loss) on securities	(84,594)	64,726
Other than temporary impairment - securities	(1,677,916)	-
Net gains on sales of loans	135,252	150,140
Increase in cash surrender value of life insurance	245,187	239,625
Brokerage fees	392,262	474,645
Other	532,872	544,819
Total noninterest income	245,861	2,170,916
Noninterest Expense		
Salaries and employee benefits	3,074,071	3,195,714
Occupancy	744,258	693,599
Data processing	675,922	643,974
Deposit insurance premium	98,653	14,915
Professional fees	177,470	167,849
Correspondent bank charges	132,536	230,267
Valuation allowances - repossessed assets	360,000	87,000
Other	837,429	905,275
Total noninterest expense	6,100,339	5,938,593
Income (Loss) Before Income Tax	396,548	(109,030)
Income tax expense (benefit)	154,481	(484,441)
Net Income	\$ 242,067	\$ 375,411
Basic Earnings Per Common Share	\$ 0.19	\$ 0.28
Diluted Earnings Per Common Share	\$ 0.19	\$ 0.28

Northeast Indiana Bancorp, Inc.
Consolidated Statements of Shareholders' Equity
Years Ended December 31, 2008 and 2007

	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss), Net of Tax	Treasury Stock	Total
Balance, January 1, 2007	\$ 26,407	\$ 29,730,475	\$ 14,419,334	\$ 9,413	\$ (19,994,224)	\$ 24,191,405
Comprehensive income						
Net income			375,411			375,411
Other comprehensive income						
Net change in unrealized losses on securities available for sale				25,684		25,684
Total tax effect				(205,253)		(205,253)
Total other comprehensive loss				(179,569)		(179,569)
Total comprehensive income						195,842
Cash dividends (\$.645 per share)			(861,414)			(861,414)
Purchase of 35,042 shares of treasury stock					(536,905)	(536,905)
Issuance of 750 shares of treasury stock upon exercise of stock options		1,089			7,670	8,759
Amortization of RRP contributions		29,330				29,330
Balance, December 31, 2007	26,407	29,760,894	13,933,331	(170,156)	(20,523,459)	23,027,017
Comprehensive income						
Net income			242,067			242,067
Other comprehensive income						
Net change in unrealized losses on securities available for sale				665,295		665,295
Total tax effect				(351,766)		(351,766)
Total other comprehensive income				313,529		313,529
Total comprehensive income						555,596
Cash dividends (\$.66 per share)			(838,971)			(838,971)
Purchase of 83,247 shares of treasury stock					(997,639)	(997,639)
Amortization of RRP contributions		29,330				29,330
Balance, December 31, 2008	\$ 26,407	\$ 29,790,224	\$ 13,336,427	\$ 143,373	\$ (21,521,098)	\$ 21,775,333

Northeast Indiana Bancorp, Inc.

Consolidated Statements of Cash Flows

Years Ended December 31, 2008 and 2007

	2008	2007
Operating Activities		
Net income	\$ 242,067	\$ 375,411
Items not requiring (providing) cash		
Depreciation and amortization	414,136	415,733
Provision for loan losses	430,000	1,290,000
Deferred income tax expense	(388,309)	(306,784)
Net (gain) loss on sale of		
Foreclosed real estate and repossessed assets	43,079	26,513
Loans held for sale	(135,252)	(150,140)
Net gain (loss) on securities available for sale	84,594	(64,726)
Other than temporary impairment of securities	1,677,916	-
Originations of loans held for sale	(4,585,260)	(3,720,110)
Proceeds from loans sold	4,011,112	3,970,250
Amortization of RRP	29,330	29,330
Changes in		
Other assets	546,587	(7,141)
Accrued interest receivable	31,170	(55,496)
Accrued expenses and other liabilities	709,134	136,577
Net cash provided by operating activities	3,110,304	1,939,417
Investing Activities		
Purchases of available-for-sale securities	(6,556,289)	(17,993,743)
Purchases of held-to-maturity securities	(550,000)	-
Proceeds from maturities and principal payments of available-for-sale securities	6,566,000	11,770,731
Proceeds from the sales of available-for-sale securities	1,114,669	5,784,206
Purchases of loans	(9,268,047)	(5,567,517)
Proceeds from sale of participation loans	1,500,000	6,343,229
Net change in loans	(11,376,093)	(12,783,486)
Proceeds from sale of foreclosed real estate and repossessed assets	393,560	1,200,439
Expenditures on premises and equipment	(66,832)	(215,362)
Net cash used in investing activities	(18,243,032)	(11,461,503)
Financing Activities		
Net change in deposits	14,570,183	16,424,518
Advances from FHLB	33,000,000	28,750,000
Repayment of FHLB advances	(36,000,000)	(31,750,000)
Net change in other borrowed funds	3,418,882	3,394,031
Dividends paid	(838,971)	(861,414)
Purchase of treasury stock	(997,639)	(536,905)
Issuance of treasury stock	-	8,759
Net cash provided by financing activities	13,152,455	15,428,989
Net Change in Cash and Cash Equivalents	(1,980,273)	5,906,903
Cash and Cash Equivalents, Beginning of Year	10,386,774	4,479,871
Cash and Cash Equivalents, End of Year	\$ 8,406,501	\$ 10,386,774
Supplemental Cash Flows Information		
Interest paid	\$ 7,838,225	\$ 8,981,005
Income taxes paid (refunded)	399,000	(251,557)
Non-Cash Transactions		
Transfer from loans to other real estate and repossessed assets	955,523	445,881

Northeast Indiana Bancorp, Inc.
Notes to Consolidated Financial Statements
December 31, 2008 and 2007

Note 1: Nature of Operations and Summary of Significant Accounting Policies

Nature of Operations

The consolidated financial statements include the accounts of Northeast Indiana Bancorp, Inc. (Northeast Indiana Bancorp) and its wholly owned subsidiary, First Federal Savings Bank (First Federal) and its wholly owned subsidiary, Northeast Indiana Financial (Northeast Indiana Financial), together referred to as (Company). During 2008, the operations of Northeast Indiana Financial were collapsed into a division of First Federal. Northeast Indiana Bancorp, Inc. was organized for the purpose of owning all of the outstanding stock of First Federal.

The primary source of income for the Company is the origination of commercial and residential real estate loans in northeastern Indiana. Loans secured by real estate mortgages comprise approximately 73% and 74% of the loan portfolio at December 31, 2008 and 2007, and are primarily secured by residential mortgages.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company. All significant intercompany accounts and transactions have been eliminated in consolidation.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Material estimates that are particularly susceptible to significant change relate to the determination of the allowance for loan losses and the valuation of real estate acquired in connection with foreclosures or in satisfaction of loans. In connection with the determination of the allowance for loan losses and the valuation of foreclosed assets held for sale, management obtains independent appraisals for significant properties.

Cash Flow Reporting

Cash and cash equivalents are defined as cash and due from banks and short-term interest earning deposits in financial institutions with original maturities under 90 days. Net cash flows are reported for customer loan and deposit transactions as well as securities sold under agreements to repurchase with original maturities of 90 days or less.

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Securities

Securities are classified as held to maturity and carried at amortized cost when management has the positive intent and ability to hold them to maturity. Securities are classified as available for sale when they might be sold before maturity. Securities available for sale are carried at fair value, with unrealized holding gains and losses reported in other comprehensive income or loss and shareholders' equity, net of tax. Other securities such as Federal Home Loan Bank stock are carried at cost.

Interest income includes amortization of purchase premium or discount. Gains and losses on sales are based on the amortized cost of the security sold. Securities are written down to fair value when a decline in fair value is determined by management to be "other than temporary" as defined by FASB 115. In estimating other-than-temporary losses, management considers: (1) the length of time and extent that fair value has been less than cost, (2) the financial condition and near term prospects of the issuer, and (3) the Company's ability and intent to hold the security for a period sufficient to allow for any anticipated recovery in fair value.

Loans Held for Sale

Mortgage loans originated and intended for sale in the secondary market are carried at the lower of cost or fair value in the aggregate. Net unrealized losses, if any, are recognized through a valuation allowance by charges to income.

Loans

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are reported at the principal balance outstanding, net of unearned interest, deferred loan fees and costs and an allowance for loan losses. Loans held for sale are reported at the lower of cost or market, on an aggregate basis.

Interest income is reported on the interest method and includes amortization of net deferred loan fees and costs over the loan term. Interest income is not reported when full loan repayment is in doubt, typically when the loan is impaired or payments are past due over 90 days. Past due status is based on the contractual terms of the loan. Payments received on such loans are reported as principal reductions. In all cases, loans are placed on nonaccrual or charged-off at an earlier date if collection of principal or interest is considered doubtful.

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

Northeast Indiana Bancorp, Inc.
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Allowance for Loan Losses

The allowance for loan losses is a valuation allowance for probable incurred credit losses, increased by the provision for loan losses and decreased by charge-offs less recoveries incurred. Management estimates the allowance balance required using past loan loss experience, the nature and volume of 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, but the entire allowance is available for any loan that, in management's judgment, should be charged-off. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed.

A loan is impaired 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 basis for other loans. If a loan is impaired, a portion of the allowance is allocated so that the loan is reported, net, at the present value of estimated future cash flows using the loan's existing rate or at the fair value of collateral if repayment is expected solely from the collateral. Loans are evaluated for impairment when payments are delayed, typically 90 days or more, or when it is probable that all principal and interest amounts will not be collected according to the original terms of the loan.

Foreclosed Assets

Assets acquired through or instead of loan foreclosure are initially recorded at fair value less estimated costs to sell when acquired, establishing a new cost basis. If the value subsequently declines, a valuation allowance is recorded through expense. Costs after acquisition are expensed. Foreclosed assets totaled \$1,049,000 and \$889,000 at December 31, 2008 and 2007.

Investments in Limited Liability Partnerships

These represent the Company's investments in affordable housing projects for the primary purpose of available tax benefits. They are accounted for using the cost method of accounting. The excess of the carrying amount of the investment over its estimated residual value is amortized during the periods in which associated tax credits are allocated to the investor. The annual amortization of the investment is based on the proportion of tax credits received in the current year to total estimated tax credits to be allocated to the Company. These investments are reviewed for impairment when events indicate their carrying amounts may not be recoverable from future undiscounted cash flows. If impaired, the investments are reported at discounted amounts.

Premises and Equipment

Land is carried at cost. Premises and equipment are stated at cost less accumulated depreciation. Depreciation is computed over asset useful lives on the straight-line basis. The useful lives for buildings and leasehold improvements range from 10 to 40 years. The useful lives for furniture, fixtures and equipment range from 3 to 10 years.

Northeast Indiana Bancorp, Inc.
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Federal Home Loan Bank Stock

Federal Home Loan Bank stock is a required investment for institutions that are members of the Federal Home Loan Bank system. The required investment in the common stock is based on a predetermined formula, carried at cost and evaluated for impairment.

Company (or Bank) Owned Life Insurance

The Company has purchased life insurance policies on certain key executives. Company-owned life insurance is recorded at its cash surrender value, or the amount that can be realized.

Goodwill and Other Tangible Assets

Goodwill results from business acquisitions and represents the excess of the purchase price over the fair value of acquired tangible assets and liabilities and identifiable intangible assets. Goodwill is assessed at least annually for impairment and any such impairment will be recognized in the period identified.

Other intangible assets consist of acquired customer relationship intangible assets arising from business acquisitions. They are initially measured at fair value and then are amortized on an accelerated method over the estimated useful lives of eight years. Such assets are periodically evaluated as to the recoverability of their carrying value.

Mortgage Servicing Rights

Mortgage servicing rights on originated loans that have been sold are initially recorded at fair value. Capitalized servicing rights are amortized in proportion to and over the period of estimated servicing revenues. Impairment of mortgage servicing rights is assessed based on the fair value of these rights. The amount of impairment recognized would be the amount by which the capitalized mortgage servicing rights exceed their fair value.

Securities Sold Under Repurchase Agreements

Substantially all securities sold under repurchase agreements represent amounts advanced by various customers. Securities are pledged to cover these liabilities, which are not covered by federal deposit insurance.

Treasury Stock

Treasury stock is stated at cost. Cost is determined by the first-in, first-out (FIFO) method.

Stock Options

At December 31, 2008 and 2007, the Company has a share-based employer compensation plan, which is more fully described in Note 13. The Company accounts for this plan under the recognition and measurement principles of Statement of Financial Accounting Standards (SFAS) No. 123(R), *Share-Based Payment*.

Northeast Indiana Bancorp, Inc.
Notes to Consolidated Financial Statements
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Income Taxes

Income tax expense is the total of the current year income tax due or refundable and the change in deferred tax assets and liabilities. Deferred tax assets and liabilities are the expected future tax amounts for the temporary differences between carrying amounts and tax bases of assets and liabilities, computed using enacted tax rates. A valuation allowance, if needed, reduces deferred tax assets to the amount expected to be realized.

The Company has adopted the provisions of the Financial Accounting Standards Board (FASB) Interpretation No. 48 (FIN 48), *Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement No. 109*, on January 1, 2007. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods and disclosure and transition for uncertain tax positions. As a result of implementation of FIN 48, the Company did not identify any uncertain tax positions that it believes should be recognized in the financial statements. The tax years still subject to examination by taxing authorities are years subsequent to 2003.

Employee Stock Ownership Plan

The cost of shares issued to the Employee Stock Ownership Plan (ESOP), but not yet allocated to participants, is shown as a reduction of shareholders' equity. Compensation expense is based on the market price of shares as they are committed to be released to participants' accounts.

Dividends on allocated ESOP shares reduce retained earnings; dividends on unearned ESOP shares reduce debt and accrued interest.

Financial Instruments

Financial instruments include credit instruments, such as commitments to make loans and standby letters of credit, issued to meet customer financing needs. The face amount for these items represents the exposure to loss, before considering customer collateral or ability to repay. Such financial instruments are recorded when they are funded.

Northeast Indiana Bancorp, Inc.
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Earnings Per Common Share

Basic earnings per common share is net income divided by the weighted-average number of common shares outstanding during the period. ESOP and Recognition and Retention Plan (RRP) shares are considered outstanding for this calculation unless unearned. Diluted earnings per common share includes the dilutive effect of additional potential common shares issuable under stock options and RRP plans.

Stock Dividends

Common share amounts related to the ESOP plan, stock compensation plans and earnings and dividends per share are restated for stock dividends.

Comprehensive Income

Comprehensive income consists of net income and other comprehensive income or loss. Other comprehensive income or loss includes unrealized gains and losses on securities available for sale, net of tax, which are also recognized as separate components of shareholders' equity.

Loss Contingencies

Loss contingencies, including claims and legal actions arising in the ordinary course of business, are recorded as liabilities when the likelihood of loss is probable and an amount or range of loss can be reasonably estimated. Management does not believe there now are such matters that will have a material effect on the Company's consolidated financial statements.

Dividend Restriction

Banking regulations require maintaining certain capital levels and may limit the dividends paid by First Federal to Northeast Indiana Bancorp or by Northeast Indiana Bancorp to shareholders.

Fair Value of Financial Instruments

Fair values of financial instruments are estimated using relevant market information and other assumptions, as more fully disclosed in a separate note. Fair value estimates involve uncertainties and matters of significant judgment regarding interest rates, credit risk, prepayments and other factors, especially in the absence of broad markets for particular items. Changes in assumptions or in market conditions could significantly affect the estimates.

Northeast Indiana Bancorp, Inc.
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Current Economic Conditions

The current economic environment presents financial institutions with unprecedented circumstances and challenges which in some cases have resulted in large declines in the fair values of investments and other assets, constraints on liquidity and significant credit quality problems, including severe volatility in the valuation of real estate and other collateral supporting loans. The consolidated financial statements have been prepared using values and information currently available to the Company.

Given the volatility of current economic conditions, the values of assets and liabilities recorded in the consolidated financial statements could change rapidly, resulting in material future adjustments in asset values, the allowance for loan losses and capital that could negatively impact the Company's ability to meet regulatory capital requirements and maintain sufficient liquidity.

Reclassifications

Certain reclassifications have been made to the 2007 financial statements to conform to the 2008 financial statement presentation. These reclassifications had no effect on net income.

Note 2: Securities

The fair value of available-for-sale securities and the related gross unrealized gains and losses recognized in accumulated other comprehensive income (loss) were as follows:

	Fair Value	Gross Unrealized Gains	Gross Unrealized Losses
Available-for-Sale Securities:			
December 31, 2008:			
U.S. Government agencies	\$ 9,782,890	\$ 498,793	\$ -
Mutual funds	3,118,189	-	(452,778)
Mortgage-backed securities	11,472,099	454,103	(6,079)
State and political subdivision	3,795,124	47,407	(7,054)
	<u>\$ 28,168,302</u>	<u>\$ 1,000,303</u>	<u>\$ (465,911)</u>
December 31, 2007:			
U.S. Government agencies	\$ 9,607,968	\$ 182,472	\$ (1,436)
Mutual funds	4,724,581	-	(135,979)
Mortgage-backed securities	11,288,305	102,354	(61,494)
State and political subdivisions	3,958,232	23,073	(9,893)
Equity securities	770,000	-	(230,000)
	<u>\$ 30,349,086</u>	<u>\$ 307,899</u>	<u>\$ (438,802)</u>

Northeast Indiana Bancorp, Inc.
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There were securities held to maturity at December 31, 2008 with an amortized cost of \$550,000 and a fair value of \$550,000.

The amortized cost and fair value of available-for-sale securities at December 31, 2008, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Available-for-Sale	
	Amortized Cost	Fair Value
Within one year	\$ 185,244	\$ 185,911
One to five years	7,462,655	7,803,079
Five to ten years	4,840,969	5,039,024
After ten years	550,000	550,000
	<u>13,038,868</u>	<u>13,578,014</u>
Mutual funds	3,570,967	3,118,189
Mortgage-backed securities	11,024,075	11,472,099
Correspondent bank stock	4,854,300	4,854,300
	<u>32,488,210</u>	<u>33,022,602</u>
Totals	<u>\$ 32,488,210</u>	<u>\$ 33,022,602</u>

	Held-to-Maturity	
	Amortized Cost	Fair Value
One to five years	\$ 550,000	\$ 550,000
Totals	<u>\$ 550,000</u>	<u>\$ 550,000</u>

Sales of securities available for sale were as follows:

	2008	2007
Proceeds	\$ 1,114,669	\$ 5,784,206
Gross gains	12,909	244,638
Gross losses	(97,503)	(179,912)

Securities pledged at December 31, 2008 and 2007 had a carrying value of \$19,760,100 and \$16,691,000, and were pledged to secure securities sold under repurchase agreements and Federal Home Loan Bank advances.

Northeast Indiana Bancorp, Inc.
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The following table shows our investments' gross unrealized losses and fair value, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at December 31, 2008:

Description of Securities	Less Than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Mutual funds	\$ 3,118,189	\$ (452,778)	\$ -	\$ -	\$ 3,118,189	\$ (452,778)
Mortgage-backed securities	818,627	(5,475)	149,680	(605)	968,307	(6,080)
State and political subdivisions	850,091	(7,053)	-	-	850,091	(7,053)
Total temporarily impaired securities	<u>\$ 4,786,907</u>	<u>\$ (465,306)</u>	<u>\$ 149,680</u>	<u>\$ (605)</u>	<u>\$ 4,936,587</u>	<u>\$ (465,911)</u>

The following table shows our investments' gross unrealized losses and fair value, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at December 31, 2007:

Description of Securities	Less Than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. Government agencies	\$ -	\$ -	\$ 1,203,564	\$ (1,436)	\$ 1,203,564	\$ (1,436)
Mutual funds	-	-	4,724,581	(135,979)	4,724,581	(135,979)
Mortgage-backed securities	-	-	3,372,260	(61,494)	3,372,260	(61,494)
State and political subdivisions	-	-	1,587,560	(9,893)	1,587,560	(9,893)
Equity securities	770,000	(230,000)	-	-	770,000	(230,000)
Total temporarily impaired securities	<u>\$ 770,000</u>	<u>\$ (230,000)</u>	<u>\$ 10,887,965</u>	<u>\$ (208,802)</u>	<u>\$ 11,657,965</u>	<u>\$ (438,802)</u>

Certain investments in debt and marketable equity securities are reported in the consolidated financial statements at an amount less than their historical cost. Total fair value of these investments at December 31, 2008 and 2007 was \$4,937,000 and \$11,658,000, which is approximately 17% and 33% of the Company's investment portfolio. The marketable equity securities consist of units in an adjustable rate mortgage (ARM) fund. The fund has a portion of its assets invested in private label mortgage-backed securities (MBS). The funds net asset value (NAV) came under intense pressure during the volatility and dislocations that unfolded in the capital markets during 2008. Several of the fund's private label MBS were downgraded during this time and management elected to recognize other than temporary impairment (OTTI) of \$728,000 during the quarter ended September 30, 2008. The funds managers have ceased purchasing private label MBS and have instead re-invested amortized cash flows into government sponsored enterprise (GSE) MBS. As of December 31, 2008, 90% of the fund's assets are rated "A" or higher with 80% of the fund's assets rated "AA" or higher.

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The bank also had an investment in FHLMC preferred shares at the prior year ended December 31, 2007. The market value of this investment also saw sharp declines during the dislocations that developed in the capital markets during 2008. After FHLMC was placed under conservatorship with the U.S. Government and dividends ceased during the quarter ended September 30, 2008, there was very little market value left in this security. As such, management elected to recognize OTTI of \$950,000 during this same time frame. These shares were later sold at a small additional loss during the quarter ended December 31, 2008. After the sale, the bank has no further exposure to either FHLMC or FNMA common or preferred shares.

Note 3: Loans Receivable, Net

Categories of loans at December 31, include:

	2008	2007
Mortgage		
Secured by one-to-four family residences	\$ 91,410,226	\$ 91,444,691
Secured by other properties	56,660,276	44,646,592
Construction - residential	1,969,701	3,391,975
Construction - nonresidential	-	2,235,000
Automobile	10,914,642	10,170,492
Commercial	34,934,165	27,454,225
Home equity and second mortgage	8,644,816	9,294,873
Other consumer	2,307,363	2,150,035
Total loans	<u>206,841,189</u>	<u>190,787,883</u>
Less		
Loans in process	(123,496)	(159,908)
Undisbursed portion of construction loans	(528,226)	(1,294,154)
Net deferred loan origination fees	(267,683)	(208,882)
Allowance for loan losses	<u>(1,750,605)</u>	<u>(2,712,378)</u>
Net loans	<u>\$ 204,171,179</u>	<u>\$ 186,412,561</u>

Activity in the allowance for loan losses was as follows:

	2008	2007
Balance, beginning of year	\$ 2,712,378	\$ 1,964,467
Provision charged to expense	430,000	1,290,000
Charge-offs	(1,900,116)	(631,500)
Recoveries	<u>508,343</u>	<u>89,411</u>
Balance, end of year	<u>\$ 1,750,605</u>	<u>\$ 2,712,378</u>

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Impaired loans were as follows:

	2008	2007
Loans with no allocated allowance for loan losses	\$ -	\$ -
Loans with allocated allowance for loan losses	2,461,952	3,191,234
	\$ 2,461,952	\$ 3,191,234
	2008	2007
Amount of the allowance for loan losses allocated	\$ 320,362	\$ 1,737,805
Average of impaired loans during the year	2,380,553	3,165,893
Interest income recognized during impairment	65,144	59,681
Cash-basis interest income recognized	65,144	59,681

Nonperforming loans were as follows:

	2008	2007
Nonaccrual loans	\$ 2,565,589	\$ 3,166,662

Nonperforming loans and impaired loans are defined differently. Some loans may be included in both categories, whereas other loans may only be included in one category.

Note 4: Secondary Mortgage Marketing Activities

Activity for capitalized mortgage servicing rights was as follows:

	2008	2007
Servicing rights		
Carrying amount, beginning of year	\$ 237,004	\$ 229,234
Assumptions of servicing obligations	38,759	37,201
Amortized to expense	(40,715)	(29,431)
Carrying amount, end of year	\$ 235,048	\$ 237,004

Mortgage loans serviced for others are not included in the accompanying consolidated balance sheets. The unpaid principal balances of loans serviced for others totaled \$23,505,000 and \$23,700,000 at December 31, 2008 and 2007, respectively.

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Note 5: Premises and Equipment, Net

Premises and equipment were as follows:

	2008	2007
Land	\$ 458,331	\$ 458,331
Automobiles	40,392	40,392
Buildings and leasehold improvements	2,489,354	2,487,362
Furniture, fixtures and equipment	<u>2,229,282</u>	<u>2,204,705</u>
	5,217,359	5,190,790
Less accumulated depreciation	<u>(3,038,943)</u>	<u>(2,837,956)</u>
Net premises and equipment	<u>\$ 2,178,416</u>	<u>\$ 2,352,834</u>

Depreciation expense was \$240,000 and \$270,000 for 2008 and 2007.

Note 6: Goodwill and Intangible Assets

Goodwill

The changes in the carrying amount of goodwill for the years ended December 31 were:

	2008	2007
Balance as of January 1	\$ 130,972	\$ 130,972
Acquired goodwill	<u>-</u>	<u>-</u>
Balance as of December 31	<u>\$ 130,972</u>	<u>\$ 130,972</u>

Acquired Intangible Assets

Acquired intangible assets at December 31 were:

	2008		2007	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Amortized intangible assets				
Customer relationship intangibles	<u>\$ 199,728</u>	<u>\$ 112,374</u>	<u>\$ 199,728</u>	<u>\$ 87,402</u>

Aggregate amortization expense was approximately \$25,000 for 2008 and 2007, respectively.

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Note 7: Deposits

Time deposits of \$100,000 or more were \$45,814,000 and \$39,169,000 at December 31, 2008 and 2007. Scheduled maturities of time deposits for the next five years were as follows:

2009	\$ 59,543,183
2010	22,761,523
2011	2,055,334
2012	140,435
2013	117,447
Thereafter	-
	<u>\$ 84,617,922</u>

Note 8: Borrowed Funds

Borrowed funds included the following at December 31:

	<u>2008</u>	<u>2007</u>
Federal Home Loan Bank (FHLB) advances	\$ 60,000,000	\$ 63,000,000
Securities sold under repurchase agreements	19,213,892	16,563,712
Note payable	768,683	-
	<u>\$ 79,982,575</u>	<u>\$ 79,563,712</u>

Securities sold under agreements to repurchase are secured by mortgage-backed securities with a carrying amount of \$19,760,000 and \$16,691,000 for the years ended December 31, 2008 and 2007.

Securities sold under agreements to repurchase are financing arrangements that mature within one day. At maturity, the securities underlying the agreements are returned to the Company.

Information concerning securities sold under agreements to repurchase is summarized as follows:

	<u>2008</u>	<u>2007</u>
Average daily balance during the year	\$ 10,346,571	\$ 16,968,622
Average interest rate during the year	1.47%	3.47%
Maximum month-end balance during the year	19,213,892	26,842,648
Weighted-average interest rate during the year	1.47%	3.29%

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FHLB Advances

FHLB advances have fixed and variable interest rates ranging from 2.86% to 6.88%. Scheduled maturities and the weighted-average interest rates by maturity for the years ended December 31, were as follows:

	2008		2007	
	Amount	Weighted-Average Interest Rate	Amount	Weighted-Average Interest Rate
2008	\$ -		\$ 15,000,000	4.93%
2009	14,500,000	4.81%	14,500,000	4.81%
2010	22,000,000	5.93%	20,000,000	6.58%
2011	14,000,000	3.96%	5,500,000	4.70%
2012	9,500,000	4.82%	8,000,000	6.34%
Thereafter	<u>-</u>		<u>-</u>	0.00%
	<u>\$ 60,000,000</u>	5.02%	<u>\$ 63,000,000</u>	5.55%

FHLB advances are secured by FHLB stock, eligible mortgage loans and specifically pledged securities. At December 31, 2008 and 2007, in addition to FHLB stock, collateral of approximately \$105,981,000 and \$105,667,000 was pledged to the FHLB to secure advances outstanding.

In addition, \$14,000,000 of the advances outstanding at December 31, 2008 contained options with dates ranging from March 1, 2010 to May 10, 2011, whereby the interest rate may be adjusted by the FHLB, at which time the advances may be repaid at the option of First Federal without penalty.

Debt

On May 8, 2008, the Company entered into a ten-year, \$800,150 note payable to The Citizens National Bank of Paris for the sole purpose of repurchasing 78,747 shares of First Federal Savings Bank stock. Terms of the agreement include twenty semi-annual payments of principal and interest at the prime rate as published in the Wall Street Journal. The following includes the payment schedule for the remainder of the note:

2009	\$ 65,739
2010	68,899
2011	72,210
2012	75,606
2013	79,315
Thereafter	<u>406,914</u>
	<u>\$ 768,683</u>

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Note 9: Employee Benefits

Employee Pension Plan

First Federal is part of a noncontributory multi-employer defined-benefit pension plan covering substantially all employees. The trustees of the Financial Institutions Retirement Fund administer the plan. There is no separate actuarial valuation of plan benefits nor segregation of plan assets specifically for First Federal because the plan is a multi-employer plan and separate actuarial valuations are not made with respect to each employer nor are the plan assets so segregated. Expense for 2008 and 2007 was approximately \$71,000 and \$113,000. The Board of Directors elected to freeze the pension plan accruals as of the plan year ended June 30, 2006. As a result of this move, all future accruals have been frozen for existing participating employees and no new employees will be admitted to the pension plan.

401(k) Plan

Northeast Indiana Bancorp has a 401(k) plan for all employees who have completed one year of service (1,000 hours) and attained a minimum age of 21 years. Participants may make deferrals up to 75% of compensation. Northeast Indiana Bancorp matches 50% of elective deferrals on the first 6% of the participant's compensation. Expense for 2008 and 2007 was approximately \$73,000 and \$56,000.

Supplemental Retirement Plans

First Federal has a supplemental retirement plan for the CEO and a deferred compensation plan for certain directors of First Federal. First Federal is recording an expense equal to the change in the present value of the payment due at retirement based on the projected remaining years of service using the projected unit credit method. The balance of the plans was approximately \$1,130,000 and \$1,008,000 at December 31, 2008 and 2007. Expense related to the plans was approximately \$146,000 and \$247,000 for 2008 and 2007.

First Federal has purchased insurance on the lives of the participants in the supplemental retirement plan and the deferred compensation plan with First Federal as beneficiary. In addition, life insurance was purchased on a pool of officers both during 2003 and 2004 with First Federal as beneficiary. The cash surrender value of the life insurance was approximately \$6,253,000 and \$6,008,000 at December 31, 2008 and 2007. The income derived from the investment in life insurance included in other income was approximately \$245,000 and \$240,000 for 2008 and 2007.

Employee Stock Ownership Plan (ESOP)

An ESOP exists for the benefit of substantially all employees. Contributions to the ESOP are made by Northeast Indiana Bancorp and are determined by the Board of Directors at their discretion. The contributions may be made in the form of cash or common stock. The annual contributions may not be greater than the amount deductible for federal income tax purposes and cannot cause Northeast Indiana Bancorp to violate regulatory capital requirements.

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Cash contributions, including dividends on unearned ESOP shares, were approximately \$0 during 2008 and 2007. ESOP compensation expense was \$0 for 2008 and 2007.

ESOP shares at December 31 are as follows:

	2008	2007
Allocated shares	127,848	134,530
Shares acquired with ESOP cash	21,321	-
Shares vested and withdrawn	83,413	76,731
 Total shares	 232,582	 211,261
 Fair value of unreleased shares	 \$ -	 \$ -

There were no cash contributions or expense associated with the ESOP plan as of December 31, 2008 and 2007. The Company is obligated at the option of each beneficiary to repurchase shares of the ESOP. At December 31, 2008, the fair value of the 149,169 allocated shares held by the ESOP was \$985,000. The fair value of the 134,530 allocated shares held by the ESOP at December 31, 2007 was \$1,823,000.

Recognition and Retention Plan (RRP)

The RRP provides for issue of shares to directors, officers and employees. The maximum total shares available under the RRP was 105,620, and 9,276 shares are available for future grants. The shares awarded will vest 20% per year over a period of five years. There were no new RRP grants awarded in 2008 and 2007. The expense associated with the RRP was approximately \$29,000 and \$29,000 in 2008 and 2007, respectively.

	2008	
	Shares	Weighted-Average Grant-Date Fair Value
Nonvested, beginning of year	5,000	\$ 18.59
Vested	(1,550)	19.15
 Nonvested, end of year	 3,450	 \$ 18.24

Unearned compensation at December 31, 2008 and 2007 related to the RRP shares is \$63,000 and \$93,000, respectively, will be recognized over a weighted-average period of four years.

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Note 10: Income Taxes

The provision (credit) for income taxes includes these components:

	2008	2007
Federal		
Current	\$ 454,924	\$ (185,474)
Deferred	(374,746)	(255,828)
State		
Current	87,866	7,817
Deferred	<u>(13,563)</u>	<u>(50,956)</u>
Income tax expense (benefit)	<u>\$ 154,481</u>	<u>\$ (484,441)</u>

Effective tax rates differ from federal statutory rates applied to financial statement income due to the following:

	2008	2007
Federal statutory rate of 34% times financial statement income before income taxes	\$ 134,826	\$ (37,070)
Tax effect of		
State tax, net of federal income tax effect	49,040	(28,472)
Low income housing credit	(164,984)	(201,326)
Tax exempt income	(42,014)	(43,223)
Utilization of capital loss carryforward	268,462	(83,177)
Other, net	<u>(90,849)</u>	<u>(91,173)</u>
Income tax expense (benefit)	<u>\$ 154,481</u>	<u>\$ (484,441)</u>

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The components of the net deferred tax assets shown on the consolidated balance sheets were:

	<u>2008</u>	<u>2007</u>
Deferred tax assets		
Deferred compensation	\$ 479,537	\$ 427,706
Bad debts	686,046	493,210
Deferred loan fees	111,258	77,781
Interest on nonaccrual loans	24,497	43,009
Low income housing credit carryforwards	996,575	1,070,154
Other	244,641	91,195
	<u>2,542,554</u>	<u>2,203,055</u>
Deferred tax liabilities		
Unrealized gains on available-for-sale securities	(391,032)	(39,252)
Depreciation	(142,788)	(177,697)
Prepays	(64,423)	(66,291)
FHLB stock dividends	(193,460)	(193,341)
Pension and employee benefits	(8,448)	(20,599)
	<u>(800,151)</u>	<u>(497,180)</u>
Net deferred tax asset	<u>\$ 1,742,403</u>	<u>\$ 1,705,875</u>

Retained earnings at December 31, 2008 and 2007 include approximately \$1,300,000 for which no deferred federal income tax liability has been recognized. This amount represents an allocation of income to bad debt deductions for tax purposes only. Reduction of amounts so allocated for purposes other than tax bad debt losses or adjustments arising from carryback of net operating losses would create income for tax purposes only, which would be subject to the then-current corporate income tax rate. The unrecorded deferred income tax liability on the above amount was approximately \$442,000 at December 31, 2008 and 2007, respectively. The Company has low income housing credits carryover of \$1,070,000 that will begin to expire if unused in 2023.

Note 11: Regulatory Matters

First Federal is subject to regulatory capital requirements administered by federal regulatory agencies. Capital adequacy guidelines and prompt corrective action regulations involve quantitative measures of assets, liabilities and certain off-balance-sheet items calculated under regulatory accounting practices.

Capital amounts and classifications are also subject to qualitative judgments by regulators about components, risk weightings, and other factors, and the regulators can lower classifications in certain cases. Failure to meet various capital requirements can initiate regulatory action that could have a direct material effect on the financial statements.

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Prompt corrective action regulations provide five classifications: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized and critically undercapitalized, although these terms are not used to represent overall financial condition. If only adequately capitalized, regulatory approval is required to accept brokered deposits. If under-capitalized, capital distributions are limited, as is asset growth and expansion, and capital restoration plans are required.

At December 31, actual First Federal capital levels (in millions) and minimum required levels were:

	Actual		Minimum Required For Capital Adequacy Purposes		Minimum Required To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2008						
Total capital						
(to risk-weighted assets)	\$ 22.4	12.0%	\$ 15.0	8.0%	\$ 18.7	10.0%
Tier I (core) capital						
(to risk-weighted assets)	20.9	11.2%	7.5	4.0%	11.2	6.0%
Tier I (core) capital						
(to adjusted total assets)	20.9	8.1%	10.4	4.0%	13.0	5.0%
Tier I (core) capital						
(to average assets)	20.9	8.1%	10.0	4.0%	12.5	5.0%
As of December 31, 2007						
Total capital						
(to risk-weighted assets)	\$ 22.6	13.6%	\$ 13.3	8.0%	\$ 16.7	10.0%
Tier I (core) capital						
(to risk-weighted assets)	21.5	12.9%	6.7	4.0%	10.0	6.0%
Tier I (core) capital						
(to adjusted total assets)	21.5	8.8%	9.8	4.0%	12.3	5.0%
Tier I (core) capital						
(to average assets)	21.5	9.0%	9.8	4.0%	12.0	5.0%

First Federal was categorized as well capitalized at December 31, 2008 and 2007. There are no conditions or events since that notification that management believes have changed First Federal's category.

Regulations of the Office of Thrift Supervision limit the amount of dividends and other capital distributions that may be paid by savings institutions without prior approval of the Office of Thrift Supervision. The regulatory restriction is based on a three-tiered system with the greatest flexibility being afforded to well-capitalized (Tier 1) institutions. First Federal is currently a Tier 1 institution. Accordingly, First Federal can make, without prior regulatory approval, distributions during a calendar year up to 100% of its retained net income for the calendar year-to-date plus retained net income for the previous two calendar years as long as First Federal would remain well-capitalized, as defined by the Office of Thrift Supervision prompt corrective action regulations, following the proposed distribution. At December 31, 2008, the Bank had no retained earnings available for distribution without regulatory approval.

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Note 12: Commitments and Contingencies and Financial Instruments With Off-Balance-Sheet Risk

Some financial instruments, such as loan commitments, credit lines, letters of credit and overdraft protection, are issued to meet customer financing needs. These agreements to provide credit or to support the credit of others, as long as conditions established in the contract are met, usually have expiration dates. Commitments may expire without being used. Off-balance-sheet risk to credit loss exists up to the face amount of these instruments, although material losses are not anticipated. The same credit policies are used to make such commitments as are used for loans, including obtaining collateral at exercise of the commitment.

Financial instruments with off-balance-sheet risk were as follows:

	<u>2008</u>	<u>2007</u>
Fixed rate commitments	\$ 3,622,076	\$ 4,719,010
Variable rate commitments	18,515,458	19,651,550
Letter of credit	2,520,316	2,661,263

Most loan commitments have terms up to 60 days. At December 31, 2008, fixed commitments have contractual interest rates ranging from 4.75% to 9.25%. Most variable rate arrangements are tied either to the national monthly median cost of funds, prime rate or the U.S. Treasury bill rate and have spreads between 5.625% and 5.750%.

Certain executives of the Bank have employment contracts, which are based upon changes of control. The employment contracts provide for the payment of one to three years worth of the officers' salaries upon a change of control.

Note 13: Stock Options

Options to buy stock have been granted to directors, officers and employees under two different stock option and incentive plans. Exercise price is the market price at date of grant. The maximum option term is ten years and options vest over five years under both plans. The Board of Directors passed a special resolution during 2005 immediately vesting all non-vested outstanding shares granted from the 2002 Omnibus Incentive Plan making 9,500 options immediately exercisable. The Company had almost awarded all stock options under the original stock option plan by the year ended 2001. As such, the 2002 Omnibus Incentive Plan was added to the Company's proxy statement and approved by the shareholders at the May 1, 2002 Northeast Indiana Bancorp, Inc. Annual Meeting. There were 158,753 new stock options approved under the new plan. At December 31, 2008 and 2007, respectively, there were 148,604 and 144,974 shares authorized for future grants.

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A summary of option activity under the Plan as of December 31, 2008, and changes during the year then ended, is presented below:

	Shares	2008 Weighted- Average Exercise Price	Weighted- Average Remaining Contractual Term
Outstanding, beginning of year	21,630	\$ 17.75	3.91
Forfeitures	<u>(3,630)</u>	<u>19.06</u>	
Outstanding and exercisable, end of year	<u>18,000</u>	<u>\$ 17.69</u>	<u>3.64</u>

Note 14: Related Party Transactions

Certain directors and officers of First Federal are loan customers. In management's opinion, such loans and other extensions of credit and deposits were made in the ordinary course of business and were made on substantially the same terms (including interest rates and collateral) as those prevailing at the time for comparable transactions with other persons. Further, in management's opinion, these loans did not involve more than normal risk of collectibility or present other unfavorable features. A summary of related party loan activity for loans aggregating \$60,000 or more to any one related party is as follows:

	2008	2007
Balance as of January 1	\$ 2,470,738	\$ 3,119,140
New loans	1,715,259	1,003,186
Repayments	<u>(1,331,387)</u>	<u>(1,651,588)</u>
Balance as of December 31	<u>\$ 2,854,610</u>	<u>\$ 2,470,738</u>

Related party deposits were approximately \$373,000 and \$569,000 at December 31, 2008 and 2007.

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Note 15: Earnings Per Common Share

A reconciliation of the numerators and denominators of the basic earnings per common share and diluted earnings per common share computations for the years ended December 31, is presented below:

	<u>2008</u>	<u>2007</u>
Basic earnings per common share		
Net income available to common shareholders	\$ 242,067	\$ 375,411
Weighted-average common shares outstanding before adjustment	1,259,552	1,333,628
Less: non-vested RRP shares	<u>(3,450)</u>	<u>(5,000)</u>
Weighted-average common shares outstanding for basis earnings per common shares	<u>1,256,102</u>	<u>1,328,628</u>
Basic earnings per common share	<u>\$ 0.19</u>	<u>\$ 0.28</u>
Diluted earnings per common share		
Net income available to common shareholders, per above	\$ 242,067	\$ 375,411
Weighted-average common shares outstanding	1,256,102	1,328,628
Add: dilutive effects of assumed conversions and exercises of stock options and RRP shares	<u>540</u>	<u>907</u>
Weighted-average common and dilutive shares outstanding for dilutive earnings per common shares	<u>1,256,642</u>	<u>1,329,535</u>
Diluted earnings per common share	<u>\$ 0.19</u>	<u>\$ 0.28</u>

Stock options for 18,000 and 21,262 shares of common stock were not considered in computing diluted earnings per common shares for the years ended December 31, 2008 and 2007, respectively, because they were not dilutive.

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Note 16: Disclosures About Fair Values of Financial Instruments

Effective January 1, 2008, the Company adopted Statement of Financial Accounting Standards No. 157 (FAS 157), *Fair Value Measurements*. FAS 157 defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. FAS 157 has been applied prospectively as of the beginning of the year.

FAS 157 defines 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 at the measurement date. FAS 157 also establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value:

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

Following is a description of the valuation methodologies used for assets and liabilities measured at fair value on a recurring basis and recognized in the accompanying consolidated balance sheets, as well as the general classification of such assets and liabilities pursuant to the valuation hierarchy.

Available-for-Sale Securities

Where quoted market prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. Level 1 securities consist of the publicly traded Shay AMF Ultra Short Mortgage Fund. The net asset value prices each day with changes in market conditions. If quoted market prices are not available, then fair values are estimated by using pricing models, quoted prices of securities with similar characteristics or discounted cash flows. Level 2 securities include U.S. Government agency securities, mortgage-backed securities and municipal securities. In certain cases where Level 1 or Level 2 inputs are not available, securities are classified within Level 3 of the hierarchy.

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The following table presents the fair value measurements of assets and liabilities recognized in the accompanying consolidated balance sheets measured at fair value on a recurring basis and the level within the FAS 157 fair value hierarchy in which the fair value measurements fall at December 31, 2008:

	Fair Value	Fair Value Measurements Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Available-for-sale securities	\$ 28,168,302	\$ 3,118,189	\$ 25,050,113	\$ -

Impaired Loans

Loans for which it is probable that the Company will not collect all principal and interest due according to contractual terms are measured for impairment in accordance with the provisions of Financial Accounting Standard No. 114 (FAS 114), *Accounting by Creditors for Impairment of a Loan*. Allowable methods for estimating fair value include using the fair value of the collateral for collateral dependent loans or, where a loan is determined not to be collateral dependent, using the discounted cash flow method.

If the impaired loan is identified as collateral dependent, then the fair value method of measuring the amount of impairment is utilized. This method requires obtaining a current independent appraisal of the collateral and applying a discount factor to the value.

If the impaired loan is determined not to be collateral dependent, then the discounted cash flow method is used. This method requires the impaired loan to be recorded at the present value of expected future cash flows discounted at the loan's effective interest rate. The effective interest rate of a loan is the contractual interest rate adjusted for any net deferred loan fees or costs, premiums or discount existing at origination or acquisition of the loan.

The following table presents the fair value measurement of assets and liabilities measured at fair value on a nonrecurring basis and the level within the FAS 157 fair value hierarchy in which the fair value measurements fall at December 31, 2008:

	Fair Value	Fair Value Measurements Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Impaired loans	\$ 2,141,590	\$ -	\$ -	\$ 2,141,590

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Following methods were used to estimate the fair value of all other financial instruments recognized in the accompanying consolidated balance sheets at amounts other than fair value.

Cash and Cash Equivalents, Interest-bearing Deposits and Federal Home Loan Bank Stock

The carrying amount approximates fair value.

Held-to-Maturity Securities

Fair value is based on quoted market prices, if available. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities.

Loans Held for Sale

The fair value for loans held for sale is based on market quotes.

Loans

The fair value of loans is estimated by discounting the future cash flows using the current rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities. Loans with similar characteristics were aggregated for purposes of the calculations. The carrying amount of accrued interest approximates its fair value.

Deposits

Deposits include demand deposits, savings accounts, NOW accounts and certain money market deposits. The carrying amount approximates fair value. The fair value of fixed-maturity time deposits is estimated using a discounted cash flow calculation that applies the rates currently offered for deposits of similar remaining maturities.

Interest Payable and Investments in Limited Liability Partnerships

The carrying amount approximates fair value.

Long-Term Debt and Federal Home Loan Bank Advances

Rates currently available to the Company for debt with similar terms and remaining maturities are used to estimate the fair value of existing debt.

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Commitments to Originate Loans, Forward Sale Commitments, Letters of Credit and Lines of Credit

The fair value of commitments to originate loans is estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present creditworthiness of the counterparties. For fixed-rate loan commitments, fair value also considers the difference between current levels of interest rates and the committed rates. The fair value of forward sale commitments is estimated based on current market prices for loans of similar terms and credit quality. The fair values of letters of credit and lines of credit are based on fees currently charged for similar agreements or on the estimated cost to terminate or otherwise settle the obligations with the counterparties at the reporting date.

The following table presents estimated fair values of the Company's financial instruments in accordance with FAS 107.

	2008		2007	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Financial assets				
Cash and cash equivalents	\$ 8,407	\$ 8,407	\$ 10,387	\$ 10,387
Available-for-sale securities	28,168	28,168	35,203	35,203
Loans held for sale	709	709	-	-
Loans receivable, net	204,171	212,702	186,413	189,807
Accrued interest receivable	1,071	1,071	1,102	1,102
Investment in limited liability partnerships	462	462	677	677
Financial liabilities				
Deposits	155,699	157,650	141,129	141,697
Borrowed funds	79,983	81,624	79,564	80,926
Accrued interest payable	335	335	392	392

While these estimates of fair value are based on management's judgment of the most appropriate factors, there is no assurance that were Northeast Indiana Bancorp to have disposed of such items at December 31, 2008 and 2007, the estimated fair values would necessarily have been achieved at that date, since market values may differ depending on various circumstances. The estimated fair values at December 31, 2008 and 2007 should not necessarily be considered to apply at subsequent dates.

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Note 17: Condensed Financial Information (Parent Company Only)

Presented below is condensed financial information as to financial position, results of operations and cash flows of Northeast Indiana Bancorp:

Condensed Balance Sheets

	2008	2007
Assets		
Cash and due from banks	\$ 286,029	\$ 314,733
Available-for-sale securities	-	150,035
Investment in subsidiary bank	22,190,797	22,517,093
Other assets	82,171	49,640
	<u>\$ 22,558,997</u>	<u>\$ 23,031,501</u>
Liabilities		
Notes payable	\$ 768,683	\$ -
Accrued expenses	14,981	4,484
Total liabilities	783,664	4,484
	<u>21,775,333</u>	<u>23,027,017</u>
Shareholders' Equity		
Total liabilities and shareholders' equity	<u>\$ 22,558,997</u>	<u>\$ 23,031,501</u>

Condensed Statements of Income

	2008	2007
Income		
Interest	\$ -	\$ 6,569
Dividends from subsidiaries	1,000,000	1,500,000
Total income	1,000,000	1,506,569
	<u>145,444</u>	<u>118,303</u>
Expenses		
Income Before Income Tax and Equity in Undistributed		
Income of Subsidiaries	854,556	1,388,266
Income Tax Benefit	(56,687)	(45,756)
	<u>911,243</u>	<u>1,434,022</u>
Income Before Equity in Undistributed Income of		
Subsidiaries	911,243	1,434,022
Equity in Undistributed (Distribution in excess of) Income of	(669,176)	(1,058,611)
Subsidiaries	<u>(669,176)</u>	<u>(1,058,611)</u>
	<u>\$ 242,067</u>	<u>\$ 375,411</u>
Net Income	<u>\$ 242,067</u>	<u>\$ 375,411</u>

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Condensed Statements of Cash Flows

	2008	2007
Operating Activities		
Net income	\$ 242,067	\$ 375,411
Items not requiring (providing) cash		
Amortization	-	(1,455)
Equity in undistributed (distributions in excess of) earnings in subsidiaries	669,176	1,058,611
Change in		
Other assets	(32,517)	(43,347)
Accrued expenses	10,497	1,656
Net cash provided by operating activities	889,223	1,390,876
Investing Activity - maturities of available-for-sale securities	150,000	100,867
Financing Activities		
Dividends	(838,971)	(861,414)
Purchase of treasury stock	(997,639)	(536,905)
Proceeds from notes payable	800,150	-
Principal payments on notes payable	(31,467)	-
Sale of treasury stock	-	8,759
Net cash used in financing activities	(1,067,927)	(1,389,560)
Net Change in Cash and Due From Banks	(28,704)	102,183
Cash and Due From Banks at Beginning of Year	314,733	212,550
Cash and Due From Banks at End of Year	\$ 286,029	\$ 314,733

Note 18: Significant Estimates and Concentrations

Accounting principles generally accepted in the United States of America require disclosure of certain significant estimates and current vulnerabilities due to certain concentrations. Estimates related to the allowance for loan losses are reflected in the footnote regarding loans. Current vulnerabilities due to certain concentrations of credit risk are discussed in the footnote on commitments and credit risk.

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Note 19: Risks and Uncertainties

The Company's allowance for loan losses contains certain assumptions on the value of collateral dependent loans as well as certain economic and industry conditions which may be subject to change within the near term. These changes could have an adverse impact on the allowance for loan loss in the near term.

Note 20: Subsequent Event

In February 2009, the Board of Directors of the Federal Deposit Insurance Corporation (FDIC) voted to amend the restoration plan for the Deposit Insurance Fund (DIF). The amended restoration plan extended the period of time to raise the DIF reserve ratio to 1.15 percent from five to seven years. The amended restoration plan also includes a final rule that sets assessment rates. Under this final rule, beginning on April 1, 2009 the Company expects the FDIC premium assessed to the Company to increase.

The Board of the FDIC also adopted an interim rule imposing a 10 basis point special assessment on insured institutions as of June 30, 2009 which will be payable on September 30, 2009. The interim rule would also allow the assessment of additional special assessments of up to 10 basis points after June 30, 2009 as deemed necessary. Comments on the interim rule are due within 30 days of publication in the Federal Register.

While the Company has not fully evaluated the impact the increased assessment rates and the pending special assessment will have on the 2009 financial results, it is anticipated the impact will be material to the 2009 results of operations.