

FFW CORPORATION  
Wabash, Indiana

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Crowe Horwath LLP  
Member Horwath International

## REPORT OF INDEPENDENT AUDITORS

Board of Directors and Shareholders  
FFW Corporation  
Wabash, Indiana

We have audited the accompanying consolidated balance sheets of FFW Corporation as of June 30, 2008 and 2007 and the related consolidated statements of income, changes in shareholders' equity and cash flows for each of the three years in the period ended June 30, 2008. 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 FFW Corporation as of June 30, 2008 and 2007 and the results of its operations and its cash flows for each of the three years in the period ended June 30, 2008 in conformity with accounting principles generally accepted in the United States of America.

*Crowe Horwath LLP*

Crowe Horwath LLP

South Bend, Indiana  
September 12, 2008

FFW CORPORATION  
CONSOLIDATED BALANCE SHEETS  
June 30, 2008 and 2007

	<u>2008</u>	<u>2007</u>
<b>ASSETS</b>		
Cash and due from financial institutions	\$ 6,095,999	\$ 5,250,292
Interest-bearing deposits in other financial institutions	<u>2,347,131</u>	<u>2,372,525</u>
Total cash and cash equivalents	8,443,130	7,622,817
Securities available for sale (AFS)	60,367,678	55,673,248
Loans receivable, net of allowance for loan losses of \$2,768,622 in 2008 and \$2,654,064 in 2007	227,839,891	207,776,065
Loans held for sale	77,000	178,250
Federal Home Loan Bank stock, at cost	3,627,100	3,627,100
Accrued interest receivable	1,560,163	1,730,689
Premises and equipment, net	4,040,369	4,184,657
Mortgage servicing rights	488,452	572,548
Cash surrender value of life insurance	5,815,227	5,579,962
Goodwill	1,213,898	1,213,898
Other assets	<u>2,412,579</u>	<u>2,386,208</u>
Total assets	<u>\$ 315,885,487</u>	<u>\$ 290,545,442</u>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Deposits		
Noninterest-bearing	\$ 13,737,624	\$ 13,706,178
Interest-bearing	<u>230,446,720</u>	<u>196,758,171</u>
Total deposits	244,184,344	210,464,349
Borrowings	45,283,087	52,194,061
Accrued expenses and other liabilities	<u>2,856,193</u>	<u>2,898,526</u>
Total liabilities	292,323,624	265,556,936
Shareholders' equity		
Preferred stock, \$.01 par; 500,000 shares authorized; none issued		
Common stock, \$.01 par; 2,000,000 shares authorized; issued: 1,836,328		
outstanding: 1,100,260 - 2008 and 1,201,478 - 2007	18,363	18,363
Additional paid-in capital	9,530,608	9,481,340
Retained earnings	25,965,339	24,334,484
Accumulated other comprehensive income (loss)	(653,825)	(164,556)
Treasury stock, at cost; 736,068 shares – 2008 and 634,850 shares – 2007	<u>(11,298,622)</u>	<u>(8,681,125)</u>
Total shareholders' equity	<u>23,561,863</u>	<u>24,988,506</u>
Total liabilities and shareholders' equity	<u>\$ 315,885,487</u>	<u>\$ 290,545,442</u>

See accompanying notes.

FFW CORPORATION  
CONSOLIDATED STATEMENTS OF INCOME  
Years ended June 30, 2008, 2007 and 2006

	<u>2008</u>	<u>2007</u>	<u>2006</u>
Interest and dividend income			
Loans, including fees	\$ 15,549,609	\$ 14,571,409	\$ 11,803,366
Taxable securities	2,752,774	2,605,289	2,458,339
Nontaxable securities	608,708	694,172	751,030
Other	<u>109,255</u>	<u>137,296</u>	<u>162,913</u>
Total interest and dividend income	19,020,346	18,008,166	15,175,648
Interest expense			
Deposits	7,619,880	7,241,910	4,835,761
Borrowings	<u>2,576,098</u>	<u>2,805,680</u>	<u>2,831,985</u>
Total interest expense	10,195,978	10,047,590	7,667,746
Net interest income	8,824,368	7,960,576	7,507,902
Provision for loan losses	<u>602,000</u>	<u>480,000</u>	<u>491,000</u>
Net interest income after provision for loan losses	8,222,368	7,480,576	7,016,902
Noninterest income			
Net gains on sales of securities	70,944	365,206	60,599
Net gains on sales of loans	197,464	117,919	220,574
Other than temporary impairment on securities	(308,000)	-	-
Commission income	534,276	523,654	513,184
Service charges and fees	1,164,627	1,310,037	1,284,609
Earnings on life insurance	268,707	255,842	243,255
Other	<u>204,938</u>	<u>16,598</u>	<u>145,601</u>
Total noninterest income	2,132,956	2,589,256	2,467,822
Noninterest expense			
Salaries and benefits	3,496,775	3,272,530	3,144,557
Occupancy and equipment	838,517	875,914	810,901
Professional	213,365	223,486	264,470
Marketing	268,311	172,258	114,135
Deposit insurance premium	24,338	24,160	23,565
Regulatory assessment	87,590	82,246	77,461
Correspondent bank charges	88,136	111,001	145,870
Data processing	561,664	633,096	557,802
Printing, postage and supplies	217,729	196,451	221,523
Expense on life insurance	76,076	100,184	95,221
Contribution expense	40,886	129,369	21,658
Other	<u>987,099</u>	<u>793,310</u>	<u>866,714</u>
Total noninterest expense	6,900,486	6,614,005	6,343,877
Income before income taxes	3,454,838	3,455,827	3,140,847
Income tax expense	<u>852,849</u>	<u>584,135</u>	<u>504,479</u>
Net income	<u>\$ 2,601,989</u>	<u>\$ 2,871,692</u>	<u>\$ 2,636,368</u>
Earnings per share			
Basic	\$ 2.24	\$ 2.36	\$ 2.11
Diluted	\$ 2.23	\$ 2.34	\$ 2.08

See accompanying notes.

FFW CORPORATION  
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY  
Years ended June 30, 2008, 2007 and 2006

	Common <u>Stock</u>	Additional Paid-In <u>Capital</u>	Retained <u>Earnings</u>	Accumulated Other Comprehensive <u>Income (Loss)</u>	Treasury <u>Stock</u>	Total Shareholders' <u>Equity</u>
<b>Balance at July 1, 2005</b>	\$ 18,363	\$ 9,390,828	\$ 20,657,787	\$ 201,639	\$ (6,940,603)	\$ 23,328,014
Cash dividends - \$0.72 per share	-	-	(904,447)	-	-	(904,447)
Issued 3,014 shares on stock options	-	(688)	-	-	36,972	36,284
Purchased 39,068 shares	-	-	-	-	(846,747)	(846,747)
Amortization of MRP contribution	-	49,812	-	-	-	49,812
Net income	-	-	2,636,368	-	-	2,636,368
Other comprehensive income, net of tax:						
Unrealized appreciation (depreciation)						
on securities AFS, net of tax of (\$327,060)	-	-	-	(423,645)	-	-
Total other comprehensive income	-	-	-	(423,645)	-	(423,645)
Comprehensive income	-	-	-	-	-	2,212,723
<b>Balance at June 30, 2006</b>	18,363	9,439,952	22,389,708	(222,006)	(7,750,378)	23,875,639
Cash dividends - \$0.76 per share	-	-	(926,916)	-	-	(926,916)
Issued 10,908 shares on stock options	-	7,070	-	-	144,284	151,354
Purchased 43,511 shares	-	-	-	-	(1,100,931)	(1,100,931)
Issuance of 2,000 shares under MRP	-	(25,900)	-	-	25,900	-
Amortization of MRP contribution	-	51,431	-	-	-	51,431
Stock option expense	-	8,787	-	-	-	8,787
Net income	-	-	2,871,692	-	-	2,871,692
Other comprehensive income, net of tax:						
Unrealized appreciation (depreciation)						
on securities AFS, net of tax of (\$7,688)	-	-	-	57,450	-	-
Total other comprehensive income	-	-	-	57,450	-	57,450
Comprehensive income	-	-	-	-	-	2,929,142
<b>Balance at June 30, 2007</b>	18,363	9,481,340	24,334,484	(164,556)	(8,681,125)	24,988,506

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FFW CORPORATION

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY  
Years ended June 30, 2008, 2007 and 2006

	Common Stock	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Total Shareholders' Equity
<b>Balance at June 30, 2007</b>	\$ 18,363	\$ 9,481,340	\$ 24,334,484	\$ (164,556)	\$ (8,681,125)	\$ 24,988,506
Cash dividends - \$0.84 per share	-	-	(971,134)	-	-	(971,134)
Issued 5,700 shares on stock options	-	769	-	-	80,147	80,916
Purchased 106,918 shares	-	-	-	-	(2,697,644)	(2,697,644)
Amortization of MRP contribution	-	40,635	-	-	-	40,635
Stock option expense	-	7,864	-	-	-	7,864
Net income	-	-	2,601,989	-	-	2,601,989
Other comprehensive income, net of tax:						
Unrealized appreciation (depreciation)						
on securities AFS, net of tax of (\$178,213)	-	-	-	(489,269)	-	-
Total other comprehensive income	-	-	-	(489,269)	-	(489,269)
Comprehensive income	-	-	-	-	-	2,112,720
<b>Balance at June 30, 2008</b>	<u>\$ 18,363</u>	<u>\$ 9,530,608</u>	<u>\$ 25,965,339</u>	<u>\$ (653,825)</u>	<u>\$(11,298,622)</u>	<u>\$ 23,561,863</u>

See accompanying notes.

FFW CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS  
Years ended June 30, 2008, 2007 and 2006

	<u>2008</u>	<u>2007</u>	<u>2006</u>
<b>Cash flows from operating activities</b>			
Net income	\$ 2,601,989	\$ 2,871,692	\$ 2,636,368
Adjustments to reconcile net income to net cash from operating activities			
Depreciation and amortization	581,972	567,367	662,917
Provision for loan losses	602,000	480,000	491,000
Net (gains) losses on sales of:			
Securities	(70,944)	(365,206)	(60,599)
Loans held for sale	(197,464)	(117,919)	(220,574)
REOs and repossessed assets	(22,598)	62,546	(2,714)
Fixed assets	299	-	-
Other than temporary impairment on securities	308,000	-	-
Originations of loans held for sale	(13,004,013)	(6,292,676)	(6,008,741)
Proceeds from sales of loans held for sale	13,218,883	6,256,069	6,542,615
Net increase in cash surrender value of life insurance	(235,265)	(224,206)	(213,243)
Amortization of MRP contribution	40,635	51,431	49,812
Net change in AIR and other assets	458,554	58,857	(482,813)
Amortization of customer list intangible	5,029	5,032	5,032
Stock option expense	7,864	8,787	-
Net change in AIP and other liabilities	(42,333)	336,871	487,378
Net cash from operating activities	<u>4,252,608</u>	<u>3,698,645</u>	<u>3,886,438</u>
<b>Cash flows from investing activities</b>			
Proceeds from:			
Sales, calls and maturities of securities AFS	4,774,568	22,912,776	5,380,576
Sales of REOs and repossessed assets	793,820	567,986	1,054,444
Purchase of securities AFS	(17,203,626)	(14,980,271)	(20,819,046)
Principal collected on mortgage-backed securities	6,821,722	5,727,424	12,589,001
Proceeds from redemption of FHLB stock	-	147,000	-
Net change in loans receivable	(21,584,484)	(23,008,081)	(24,117,025)
Purchases of premises and equipment, net	(261,675)	(284,248)	(700,569)
Net cash used in investing activities	<u>(26,653,454)</u>	<u>(8,917,414)</u>	<u>(26,612,619)</u>
<b>Cash flows from financing activities</b>			
Net change in deposits	33,719,995	14,914,029	17,637,727
Proceeds from borrowings	78,738,400	77,200,000	30,800,000
Repayment of borrowings	(85,649,374)	(83,916,445)	(25,514,786)
Proceeds from stock options	80,916	151,354	36,284
Purchase of treasury stock	(2,697,644)	(1,100,931)	(846,747)
Cash dividends paid	(971,134)	(926,916)	(904,447)
Net cash from financing activities	<u>23,221,159</u>	<u>6,321,091</u>	<u>21,208,031</u>
Net change in cash and cash equivalents	820,313	1,102,322	(1,518,150)
Beginning cash and cash equivalents	<u>7,622,817</u>	<u>6,520,495</u>	<u>8,038,645</u>
<b>Ending cash and cash equivalents</b>	<u>\$ 8,443,130</u>	<u>\$ 7,622,817</u>	<u>\$ 6,520,495</u>
Supplemental disclosure of cash flow information			
Cash paid during the period			
Interest	\$ 10,223,446	\$ 9,896,055	\$ 7,595,034
Income taxes	630,156	495,000	480,000
Transfers from loans to REO	918,658	796,351	743,920

See accompanying notes.

FFW CORPORATION  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
June 30, 2008, 2007 and 2006

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**NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

Principles of Consolidation: The consolidated financial statements include FFW Corporation (the Company), and its wholly-owned subsidiaries, Crossroads Bank, formerly First Federal Savings Bank of Wabash (the Bank) and Insurance 1 Services, Inc. Also included in the consolidated financial statements is Wabash Investments, Inc., a wholly-owned subsidiary of the Bank, which is a Nevada corporation that manages a portion of the Bank's investment portfolio. All intercompany transactions and balances are eliminated in consolidation.

Nature of Business and Concentrations of Credit Risk: The primary source of income for the Company is interest income derived from origination of commercial and residential real estate loans (see Note 15).

Use of Estimates In Preparing Financial Statements: To prepare financial statements in conformity with accounting principles generally accepted in the United States of America (or with U.S. generally accepted accounting principles) management makes estimates and assumptions based on available information. These estimates and assumptions affect the amounts reported in the financial statements and the disclosures provided, and actual results could differ. The allowance for loan losses, mortgage servicing rights, and fair values of securities and other financial instruments are particularly subject to change.

Cash Flow Reporting: For reporting cash flows, cash and cash equivalents include cash on hand, due from financial institutions and interest-bearing deposits in other financial institutions. Net cash flows are reported for customer loan and deposit transactions.

Restrictions on Cash: Cash on hand or on deposit with the Federal Reserve Bank of \$818,000 and \$570,000 was required to meet regulatory reserve and clearing requirements at June 30, 2008 and 2007, respectively. These balances do not earn interest.

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 AFS when they might be sold before maturity. Securities AFS are carried at fair value, with unrealized holding gains and losses reported separately in shareholders' equity, net of tax. Securities are classified as trading when held for short term periods in anticipation of market gains, and are carried at fair value. Declines in the fair value of securities below their cost that are other than temporary are reflected as realized losses. 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.

Gains and losses on sales are determined using the amortized cost of the specific security sold. Interest income includes amortization of purchase premiums and discounts.

Loans Receivable: Loans receivable are reported at the principal balance outstanding, net of deferred loan fees and costs, and an allowance for loan losses. Interest income is reported on the interest method and includes amortization of net deferred loan fees and costs over the loan term.

FFW CORPORATION  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
June 30, 2008, 2007 and 2006

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**NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES** (Continued)

Interest income on mortgage and commercial loans is discontinued at the time a loan is 90 days delinquent unless the loan is well-secured and in process of collection. Consumer loans are typically charged off no later than 120 days past due. Past due status is based on the contractual terms of the loan. 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.

Allowance for Loan and Lease Losses: The allowance for loan losses is a valuation allowance for probable incurred credit losses. 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. 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.

The allowance consists of specific and general components. The specific component relates to loans that are individually classified as impaired or loans otherwise classified as substandard or doubtful. The general component covers non-classified loans and is based on historical loss experience adjusted for current factors.

A loan is impaired when full payment under the loan terms is not expected. Commercial loans are individually evaluated for impairment. 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. Large groups of smaller balance homogeneous loans, such as consumer and residential real estate loans, are collectively evaluated for impairment, and accordingly, they are not separately identified for impairment disclosures.

Loans Held for Sale: Mortgage loans originated and intended for sale in the secondary market are carried at the lower of aggregate cost or market, as determined by outstanding commitments from investors. Net unrealized losses, if any, are recorded as a valuation allowance and charged to earnings.

Mortgage loans held for sale are generally sold with servicing rights retained. The carrying value of mortgage loans sold is reduced by the amount allocated to the servicing right. Gains and losses on sales of mortgage loans are based on the difference between the selling price and the carrying value of the related loan sold.

Federal Home Loan Bank (FHLB) Stock: The Bank is a member of the FHLB system. Members are required to own a certain amount of stock based on the level of borrowings and other factors, and may invest in additional amounts. FHLB stock is carried at cost, classified as a restricted security, and periodically evaluated for impairment based on ultimate recovery of par value. Both cash and stock dividends are reported as income.

Premises and Equipment: Premises and equipment are stated at cost less accumulated depreciation. Land is carried at cost. Buildings and related components are depreciated using the straight-line or other accelerated methods with useful lives ranging from 7 to 39 years. Furniture, fixtures and equipment are depreciated using the straight-line or other accelerated methods with useful lives ranging from 3 to 15 years. These assets are reviewed for impairment when events indicate the carrying amount may not be recoverable.

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(Continued)

FFW CORPORATION  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
June 30, 2008, 2007 and 2006

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**NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

Mortgage Servicing Rights: Servicing rights are recognized separately when they are acquired through sales of loans. For sales of mortgage loans prior to July 1, 2007, a portion of the cost of the loan was allocated to the servicing right based on relative fair values. The Company adopted SFAS No. 156 on July 1, 2007, and for sales of mortgage loans beginning in fiscal year 2008, servicing rights are initially recorded at fair value with the income statement effect recorded in gains on sales of loans. Fair value is based on market prices for comparable mortgage servicing contracts, when available, or alternatively, is based on a valuation model that calculates the present value of estimated future net servicing income. The valuation model incorporates assumptions that market participants would use in estimating future net servicing income, such as the cost to service, the discount rate, the custodial earnings rate, an inflation rate, ancillary income, prepayment speeds and default rates and losses. All classes of servicing assets are subsequently measured using the amortization method which requires servicing rights to be amortized into noninterest income in proportion to, and over the period of, the estimated future net servicing income of the underlying loans.

Servicing assets are evaluated for impairment based upon the fair value of the rights as compared to carrying amount. Impairment is determined by stratifying rights into groupings based on predominant risk characteristics, such as interest rate, loan type and investor type. Impairment is recognized through a valuation allowance for an individual grouping, to the extent that fair value is less than the carrying amount. If the Company later determines that all or a portion of the impairment no longer exists for a particular grouping, a reduction of the allowance may be recorded as an increase to income. Changes in the valuation allowance are reported with service charges and fees. The fair values of servicing rights are subject to significant fluctuations as a result of changes in estimated and actual prepayment speeds and default rates and losses.

Company Owned Life Insurance: Life insurance plans are provided for certain executive officers on a split dollar basis. The Company is the owner of the split dollar policies. The officers are entitled to a sum equal to two times the employee's annual salary at death, if actively employed. The Company is entitled to the remainder of the death proceeds. The employees have the right to designate a beneficiary(s) to receive their share of the proceeds payable upon death. Upon adoption of EITF 06-5, which is discussed further below, Company owned life insurance is recorded at the amount that can be realized under the insurance contract at the balance sheet date, which is the cash surrender value adjusted for other charges or other amounts due that are probable at settlement. Prior to adoption of EITF 06-5, the Company recorded owned life insurance at its cash surrender value.

In September 2006, the FASB Emerging Issues Task Force finalized Issue No. 06-5, *Accounting for Purchases of Life Insurance - Determining the Amount That Could Be Realized in Accordance with FASB Technical Bulletin No. 85-4 (Accounting for Purchases of Life Insurance)*. This Issue requires that a policyholder consider contractual terms of a life insurance policy in determining the amount that could be realized under the insurance contract. It also requires that if the contract provides for a greater surrender value if all individual policies in a group are surrendered at the same time, that the surrender value be determined based on the assumption that policies will be surrendered on an individual basis. Lastly, the Issue requires disclosure when there are contractual restrictions on the Company's ability to surrender a policy. The adoption of EITF 06-5 on July 1, 2007 had no impact on the Company's financial condition or results of operation.

The cash surrender value of these life insurance policies, life insurance policies related to the Company's Salary Continuation Plan and other company owned life insurance policies totaled approximately \$5,815,000 and \$5,580,000 as of June 30, 2008 and 2007.

Goodwill and Other Intangible 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.

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(Continued)

FFW CORPORATION  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
June 30, 2008, 2007 and 2006

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**NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES** (Continued)

Other intangible assets are included with other assets and consist of an insurance customer list arising from the acquisition of Insurance 1 Services, Inc. This intangible asset was initially measured at fair value and then amortized on a straight-line basis over 7 years.

Foreclosed Real Estate: Real estate properties acquired through, or in lieu of, foreclosure are initially recorded at fair value less estimated costs to sell at acquisition, establishing a new cost basis. Any reduction to fair value from the carrying value of the related loan at the time of acquisition is accounted for as a loan loss and charged against the allowance for loan losses. Valuations are periodically performed by management and valuation allowances are adjusted through a charge to income for changes in fair value or estimated selling costs. Operating costs after acquisition are expensed.

Stock-Based Compensation: Effective July 1, 2006, the Company adopted Statement of Financial Accounting Standards ("SFAS") No. 123(R), *Share-based Payment*, using the modified prospective transition method. Accordingly, the Company has recorded stock-based employee compensation cost using the fair value method starting in fiscal year 2007. Prior to July 1, 2006, employee compensation expense under stock options was reported using the intrinsic value method; therefore, no stock-based compensation cost is reflected in net income for the year ending June 30, 2006, as all options granted had an exercise price equal to or greater than the market price of the underlying common stock at date of grant.

The following table illustrates the effect on net income and earnings per share if expense was measured using the fair value recognition provisions of FASB Statement No. 123, *Accounting for Stock-Based Compensation*, for the year ending June 30, 2006.

Net income as reported	\$ 2,636,368
Less: Stock-based compensation expense determined under fair value based method	<u>7,440</u>
Pro forma net income	<u>\$ 2,628,928</u>
Basic earnings per share as reported	\$ 2.11
Pro forma basic earnings per share	2.10
Diluted earnings per share as reported	2.08
Pro forma diluted earnings per share	2.07

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.

Retirement Plans: Pension expense is the net of service and interest cost, return on plan assets and amortization of gains and losses not immediately recognized. Employee 401(k) and profit sharing plan expense is the amount of matching contributions. Deferred compensation and supplemental retirement plan expense allocates the benefits over years of service.

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FFW CORPORATION  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
June 30, 2008, 2007 and 2006

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**NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

Earnings Per Common Share: Basic earnings per share is net income divided by the weighted average number of common shares outstanding during the period. Management Retention Plan (MRP) shares are considered outstanding for basic earnings per share as they become vested. Diluted earnings per common share includes the dilutive effect of additional potential common shares issuable under stock option plans and nonvested shares issued under the MRP. Earnings and dividends per share are restated for all stock splits and stock dividends through the issuance of the financial statements.

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

Equity: Stock dividends in excess of 20% are reported by transferring the par value of the stock issued from retained earnings to common stock. Stock dividends for 20% or less are reported by transferring the fair value, as of the ex-dividend date, of the stock issued from retained earnings to common stock and additional paid-in capital.

Dividend Restrictions: Banking regulations require maintaining certain capital levels and may limit the dividends paid by the Bank to the holding company or by the holding company to shareholders.

Loan Commitments and Related Financial Instruments: Financial instruments include off-balance sheet credit instruments, such as commitments to make loans and commercial 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. A summary of these commitments is disclosed in Note 14.

Long-Term Assets: Premises and equipment, core deposit and other intangible assets, and other long-term assets are reviewed for impairment when events indicate their carrying amount may not be recoverable from future undiscounted cash flows. If impaired, the assets are recorded at fair value.

Transfers of Financial Assets: Transfers of financial assets are accounted for as sales, when control over the assets has been relinquished. Control over transferred assets is deemed to be surrendered when the assets have been isolated from the Company, the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

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 financial statements.

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.

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FFW CORPORATION  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
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**NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES** (Continued)

Adoption of New Accounting Standards: In February 2006, the FASB issued Statement of Financial Accounting Standards No. 155, *Accounting for Certain Hybrid Financial Instruments* (SFAS No. 155), which permits fair value remeasurement for hybrid financial instruments that contain an embedded derivative that otherwise would require bifurcation. Additionally, SFAS No. 155 clarifies the accounting guidance for beneficial interests in securitizations. Under SFAS No. 155, all beneficial interests in a securitization will require an assessment in accordance with SFAS No. 133 to determine if an embedded derivative exists within the instrument. In January 2007, the FASB issued Derivatives Implementation Group Issue B40, *Application of Paragraph 13(b) to Securitized Interests in Prepayable Financial Assets* (DIG Issue B40). DIG Issue B40 provides an exemption from the embedded derivative test of paragraph 13(b) of SFAS No. 133 for instruments that would otherwise require bifurcation if the test is met solely because of a prepayment feature included within the securitized interest and prepayment is not controlled by the security holder. SFAS No. 155 and DIG Issue B40 are effective for fiscal years beginning after September 15, 2006. The adoption of SFAS No. 155 and DIG Issue B40 did not have a material impact on the Company's consolidated financial position or results of operations.

Effect of Newly Issued But Not Yet Effective Accounting Standards: In September 2006, the FASB issued Statement No. 157, *Fair Value Measurements*. This Statement defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. This Statement establishes a fair value hierarchy about the assumptions used to measure fair value and clarifies assumptions about risk and the effect of a restriction on the sale or use of an asset. The standard is effective for fiscal years beginning after November 15, 2007. In February 2008, the FASB issued Staff Position (FSP) 157-2, *Effective Date of FASB Statement No. 157*. This FSP delays the effective date of FAS 157 for all nonfinancial assets and nonfinancial liabilities, except those that are recognized or disclosed at fair value on a recurring basis (at least annually) to fiscal years beginning after November 15, 2008, and interim periods within those fiscal years. The Company has not completed its evaluation of the impact of the adoption of this standard.

In February 2007, the FASB issued Statement No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities*. The standard provides companies with an option to report selected financial assets and liabilities at fair value and establishes presentation and disclosure requirements designed to facilitate comparisons between companies that choose different measurement attributes for similar types of assets and liabilities. The new standard is effective for the Company on July 1, 2008. The Company did not elect the fair value option for any financial assets or financial liabilities as of July 1, 2008.

In September 2006, the FASB Emerging Issues Task Force finalized Issue No. 06-4, *Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements*. This issue requires that a liability be recorded during the service period when a split-dollar life insurance agreement continues after participants' employment or retirement. The required accrued liability will be based on either the post-employment benefit cost for the continuing life insurance or based on the future death benefit depending on the contractual terms of the underlying agreement. This issue is effective for fiscal years beginning after December 15, 2007. Management anticipates there will be no impact of adoption, given that the Company's split-dollar life insurance agreements do not continue after participants' employment or retirement.

In July 2006, the FASB issued FASB Interpretation 48, *Accounting for Uncertainty in Income Taxes – an Interpretation of FASB Statement No. 109* ("FIN 48"), which prescribes the recognition threshold and measurement attribute for 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, disclosure and transaction. FIN 48 is required to be adopted for periods beginning after December 15, 2007 for non-public companies. The Company does not expect that the adoption of FIN 48 for the fiscal year beginning July 1, 2008 will have a material effect on the consolidated financial position or results of operations of the Company.

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(Continued)

FFW CORPORATION  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
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**NOTE 2 – EARNINGS PER SHARE**

A reconciliation of the numerators and denominators used in the computation of basic earnings per share and diluted earnings per share is presented below:

	<u>2008</u>	Year ended June 30, <u>2007</u>	<u>2006</u>
<b>Basic Earnings Per Share</b>			
Numerator: Net income	\$ 2,601,989	\$ 2,871,692	\$ 2,636,368
Denominator: Weighted average shares outstanding	1,159,847	1,221,396	1,256,726
Less: Average non-vested MRP shares	<u>(708)</u>	<u>(5,761)</u>	<u>(6,781)</u>
Weighted average shares outstanding	<u>1,159,139</u>	<u>1,215,635</u>	<u>1,249,945</u>
Basic earnings per share	<u>\$ 2.24</u>	<u>\$ 2.36</u>	<u>\$ 2.11</u>

	<u>2008</u>	Year ended June 30, <u>2007</u>	<u>2006</u>
<b>Diluted Earnings Per Share</b>			
Numerator: Net income	\$ 2,601,989	\$ 2,871,692	\$ 2,636,368
Denominator: Weighted average shares outstanding for basic earnings per share	1,159,139	1,215,635	1,249,945
Add: Dilutive effects of assumed exercise of stock options and nonvested MRP shares	<u>7,677</u>	<u>11,801</u>	<u>18,896</u>
Weighted average shares and dilutive potential shares outstanding	<u>1,166,816</u>	<u>1,227,436</u>	<u>1,268,841</u>
Diluted earnings per share	<u>\$ 2.23</u>	<u>\$ 2.34</u>	<u>\$ 2.08</u>

Share awards for 5,250 and 5,000 shares of common stock were not considered in computing diluted earnings per common share for 2008 and 2007, respectively, because they were antidilutive. There were no share awards considered antidilutive for 2006.

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(Continued)

FFW CORPORATION  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
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**NOTE 3 - 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:

	<u>Fair Value</u>	<u>Gross Unrealized Gains</u>	<u>Gross Unrealized Losses</u>
<u>2008</u>			
CD's and other interest bearing	\$ 340,674	\$ -	\$ -
State and municipal	14,967,982	290,343	(69,303)
Corporate bonds	2,607,480	4,751	(697,220)
Mortgage backed	34,483,412	197,503	(486,807)
Equity	7,968,130	-	(151,420)
	<u>\$ 60,367,678</u>	<u>\$ 492,597</u>	<u>\$ (1,404,750)</u>

	<u>Fair Value</u>	<u>Gross Unrealized Gains</u>	<u>Gross Unrealized Losses</u>
<u>2007</u>			
U.S. government and agency	\$ 2,873,939	\$ -	\$ (20,922)
State and municipal	14,304,571	249,322	(29,834)
Corporate bonds	3,314,478	8,950	(17,823)
Mortgage backed	34,220,394	23,036	(507,628)
Equity	250,450	-	-
Mutual funds	709,416	50,228	-
	<u>\$ 55,673,248</u>	<u>\$ 331,536</u>	<u>\$ (576,207)</u>

Sales/calls of available for sale securities were as follows:

	<u>2008</u>	<u>2007</u>	<u>2006</u>
Sales	\$ 1,730,131	\$ 15,934,262	\$ 230,576
Calls	2,394,437	6,978,513	2,650,000
Gross gains	70,945	437,162	61,900
Gross losses	-	(71,956)	(1,301)

Contractual maturities of debt securities at June 30, 2008 were as follows. Expected maturities may differ from contractual maturities because borrowers may call or prepay obligations. Securities not due at a single maturity date are shown separately.

	<u>Fair Value</u>
Due in one year or less	\$ 795,012
Due from one to five years	3,216,965
Due from five to ten years	3,249,025
Due after ten years	10,655,134
Mortgage backed	34,483,412
Equity	7,968,130
	<u>\$ 60,367,678</u>

(Continued)

FFW CORPORATION  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
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**NOTE 3 – SECURITIES (Continued)**

Securities with unrealized losses at June 30, 2008, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, are as follows:

<u>Description of Securities</u>	<u>Less than</u> <u>12 Months</u>		<u>12 Months</u> <u>or More</u>		<u>Total</u>	
	<u>Fair</u> <u>Value</u>	<u>Unrealized</u> <u>Loss</u>	<u>Fair</u> <u>Value</u>	<u>Unrealized</u> <u>Loss</u>	<u>Fair</u> <u>Value</u>	<u>Unrealized</u> <u>Loss</u>
State and municipal	\$ 3,736,545	\$ (69,303)	\$ -	\$ -	\$ 3,736,545	\$ (69,303)
Mortgage backed	19,260,849	(446,422)	1,543,358	(40,385)	20,804,207	(486,807)
Equity	275,680	(151,420)	-	-	275,680	(151,420)
Corporate bonds	<u>2,086,350</u>	<u>(697,220)</u>	<u>-</u>	<u>-</u>	<u>2,086,350</u>	<u>(697,220)</u>
Total temporarily impaired	<u>\$25,359,424</u>	<u>\$(1,364,365)</u>	<u>\$1,543,358</u>	<u>\$ (40,385)</u>	<u>\$26,902,782</u>	<u>\$(1,404,750)</u>

Securities with unrealized losses at June 30, 2007 not recognized in income are as follows:

<u>Description of Securities</u>	<u>Less than</u> <u>12 Months</u>		<u>12 Months</u> <u>or More</u>		<u>Total</u>	
	<u>Fair</u> <u>Value</u>	<u>Unrealized</u> <u>Loss</u>	<u>Fair</u> <u>Value</u>	<u>Unrealized</u> <u>Loss</u>	<u>Fair</u> <u>Value</u>	<u>Unrealized</u> <u>Loss</u>
U.S. government and agency	\$ 991,880	\$ (8,120)	\$ 1,882,059	\$ (12,802)	\$ 2,873,939	\$ (20,922)
State and municipal	-	-	1,713,649	(29,834)	1,713,649	(29,834)
Mortgage backed	16,903,343	(203,628)	13,741,097	(304,000)	30,644,440	(507,628)
Corporate bonds	<u>-</u>	<u>-</u>	<u>1,305,529</u>	<u>(17,823)</u>	<u>1,305,529</u>	<u>(17,823)</u>
Total temporarily impaired	<u>\$ 17,895,223</u>	<u>\$(211,748)</u>	<u>\$18,642,334</u>	<u>\$ (364,459)</u>	<u>\$ 36,537,557</u>	<u>\$ (576,207)</u>

Unrealized losses on debt securities have not been recognized into income because the securities are of high credit quality, management has the intent and ability to hold for the foreseeable future and the decline in fair value is largely due to changes in interest rates and recent market events, and not due to credit quality. The fair value is expected to recover as the bonds approach their maturity dates or as market conditions stabilize.

Unrealized losses on corporate bonds in 2008 relate primarily to investments in pooled trust preferred securities, issued primarily by banks. The decline in value is attributable to current illiquidity in the market related to these securities and not a decline in the expected cash flows or the credit quality of the securities.

The Company's equity securities includes fixed rate preferred stock issued by the Federal National Mortgage Association (FNMA). For the year ended June 30, 2008, the Company recognized a \$308,000 charge for the other-than-temporary decline in fair value. As required by SFAS 115, when a decline in fair value below cost is deemed to be other-than-temporary, the unrealized loss must be recognized as a charge to earnings. The determination that the FNMA preferred stock was impaired at June 30, 2008 was largely attributable to events occurring subsequent to the balance sheet date. See Note 20. Unrealized losses on other equity securities were not considered other than temporary due to small amounts and short duration.

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**NOTE 4 - LOANS RECEIVABLE, NET**

Loans receivable as of June 30 were as follows:

	<u>2008</u>	<u>2007</u>
Mortgage loans		
Secured by one-to-four family residences (conventional)	\$ 93,304,054	\$ 89,747,350
Secured by other properties (commercial)	37,599,220	34,630,862
Construction	<u>3,171,594</u>	<u>2,858,720</u>
	134,074,868	127,236,932
Undisbursed portion of construction loans	(665,606)	(1,018,482)
Net deferred loan origination fees	<u>(89,598)</u>	<u>(88,503)</u>
Total mortgage loans	133,319,664	126,129,947
Consumer and other loans		
Automobile	8,443,023	10,091,515
Manufactured home	315,901	300,210
Home equity and improvement	20,352,732	19,108,701
Commercial	33,794,697	27,204,083
Leases	16,265,881	12,757,659
Other	<u>18,085,611</u>	<u>14,812,314</u>
	97,257,845	84,274,482
Net deferred loan origination costs	<u>31,004</u>	<u>25,700</u>
Total consumer and other loans	<u>97,288,849</u>	<u>84,300,182</u>
Total loans	230,608,513	210,430,129
Allowance for loan losses	<u>(2,768,622)</u>	<u>(2,654,064)</u>
	<u>\$ 227,839,891</u>	<u>\$ 207,776,065</u>

Activity in the allowance for loan losses was as follows:

	<u>2008</u>	<u>2007</u>	<u>2006</u>
Beginning balance	\$ 2,654,064	\$ 2,959,513	\$ 2,670,277
Provision for loan losses	602,000	480,000	491,000
Charge-offs	(696,467)	(931,271)	(371,081)
Recoveries	<u>209,025</u>	<u>145,822</u>	<u>169,317</u>
Ending balance	<u>\$ 2,768,622</u>	<u>\$ 2,654,064</u>	<u>\$ 2,959,513</u>

Individually impaired loans were as follows:

	<u>2008</u>	<u>2007</u>	<u>2006</u>
Year end loans with no allowance for loan losses allocated	\$ 674,816	\$ -	\$ -
Year end loans with allowance for loan losses allocated	288,188	1,827,374	2,788,591
Amount of allowance for loan losses allocated	38,957	217,804	1,111,219
Average of individually impaired loans during the year	1,742,371	2,648,575	1,726,393
Interest income recognized during impairment	42,537	67,623	176,755
Cash-basis interest income recognized	42,058	60,901	173,513

(Continued)

FFW CORPORATION  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
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**NOTE 4 - LOANS RECEIVABLE, NET** (Continued)

Nonaccrual loans and loans past due 90 days still on accrual were as follows:

	<u>2008</u>	<u>2007</u>	<u>2006</u>
Loans past due over 90 days still on accrual	\$ -	\$ -	\$ -
Nonaccrual loans	2,415,477	1,741,868	1,915,206

Nonaccrual loans and loans past due 90 days still on accrual include both smaller balance homogeneous loans that are collectively evaluated for impairment and individually classified impaired loans.

The components of the Company's direct financing leases as of June 30 are summarized below:

	<u>2008</u>	<u>2007</u>
Future minimum lease payments	\$ 18,179,503	\$ 14,769,722
Residual interests	630,080	254,690
Initial direct costs	71,660	19,609
Unearned income	<u>(2,615,362)</u>	<u>(2,286,362)</u>
	<u>\$ 16,265,881</u>	<u>\$ 12,757,659</u>

Future minimum lease payments are as follows:

	<u>2008</u>
2009	\$ 5,334,109
2010	5,264,399
2011	3,879,003
2012	2,328,841
2013	869,204
Thereafter	<u>503,947</u>
Total	<u>\$ 18,179,503</u>

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(Continued)

FFW CORPORATION  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
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**NOTE 5 - LOAN SERVICING**

Loans serviced for others are not reported as assets in the balance sheets. These loans totaled \$68,444,000 and \$68,456,000 at June 30, 2008 and 2007. Related escrow deposit balances were \$337,000 and \$213,000 at June 30, 2008 and 2007.

Activity for capitalized mortgage servicing rights for the years ended June 30 follows:

	<u>2008</u>	<u>2007</u>	<u>2006</u>
Servicing rights:			
Beginning of year	\$ 572,548	\$ 601,690	\$ 521,852
Additions	83,844	56,276	154,200
Amortized to expense	<u>(77,379)</u>	<u>(66,719)</u>	<u>(74,362)</u>
	<u>579,013</u>	<u>591,247</u>	<u>601,690</u>
Valuation allowance	<u>\$ (90,561)</u>	<u>\$ (18,699)</u>	<u>\$ -</u>
End of year	<u>\$ 488,452</u>	<u>\$ 572,548</u>	<u>\$ 601,690</u>

As of June 30, 2008 and 2007, a valuation allowance was recorded to reflect impairment in groupings of underlying loans. As of June 30, 2006 the carrying value of mortgage servicing rights approximated fair value.

**NOTE 6 - PREMISES AND EQUIPMENT, NET**

Premises and equipment at June 30 were as follows:

	<u>2008</u>	<u>2007</u>
Land	\$ 690,666	\$ 690,666
Construction in progress	-	7,556
Buildings	4,520,241	4,511,614
Furniture, fixtures and equipment	<u>2,247,065</u>	<u>2,012,689</u>
Total cost	7,457,972	7,222,525
Accumulated depreciation	<u>(3,417,603)</u>	<u>(3,037,868)</u>
	<u>\$ 4,040,369</u>	<u>\$ 4,184,657</u>

Depreciation expense on premises and equipment was \$406,000 and \$464,000 for fiscal 2008 and 2007.

**NOTE 7 - ACQUISITIONS AND MERGERS**

On July 1, 2005, the Company purchased Insurance 1 Services, Inc. to expand the financial services it can provide to its customers. The purchase price for Insurance 1 was \$274,000, which is payable over five years. As of June 30, 2008, the Company has recorded a liability of \$97,000, representing the amount that is expected to be paid by July 1, 2010. The Company recorded goodwill of \$238,000 and a customer list intangible of \$36,000. The customer list intangible is being amortized on a straight-line basis over 7 years and amortization expense was approximately \$5,000 for fiscal 2008.

FFW CORPORATION  
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**NOTE 8 - DEPOSITS**

Deposit accounts individually exceeding \$100,000 totaled approximately \$77,281,000 and \$60,442,000 at June 30, 2008 and 2007.

At June 30, 2008, stated maturities of certificates of deposit for the years ended June 30 were:

2009	\$ 103,081,674
2010	34,398,228
2011	3,782,415
2012	7,174,677
2013	4,226,936
Thereafter	<u>23,703</u>
	<u>\$ 152,687,633</u>

Included in the total amount of certificates of deposit is \$23,128,000 placed with the Certificate of Deposit Account Registry Service (CDARS). Funds deposited through the CDARS network are divided among participating banks to ensure there is never more than \$100,000 at any one institution; therefore these are fully eligible for FDIC insurance.

**NOTE 9 – BORROWINGS**

Federal Home Loan Bank (FHLB) advances totaled \$44,024,687 and \$52,194,061 at June 30, 2008 and 2007. The advances are a mix of variable rate, fixed rate bullet, fixed rate amortizing and putable advances. The advances carry interest rates ranging from 3.06% to 4.75% for fixed rate bullet, 5.05% for fixed rate amortizing and 2.89% to 6.88% for putable advances while the Company's variable advances were at a rate of 2.42% as of June 30, 2008. The scheduled maturities during the years ended June 30 are as follows:

2009	\$ 7,000,000
2010	13,200,000
2011	10,000,000
2012	824,687
2013	9,500,000
Thereafter	<u>3,500,000</u>
	<u>\$ 44,024,687</u>

The Company also maintains lines of credit with other financial institutions in the amounts of \$2,000,000 and \$1,000,000, which terminate on March 20, 2009 and July 2, 2009, respectively. As of June 30, 2008, a balance of \$1,258,400 was outstanding against these lines. No amount was outstanding as of June 30, 2007.

FHLB borrowings are secured by all stock in the FHLB, qualifying first mortgage loans, government, agency and mortgage-backed securities. At June 30, 2008, collateral of approximately \$114,539,000 is pledged to the FHLB to secure advances outstanding. Additionally, the \$2,000,000 line of credit is secured by shares of Crossroads Bank.

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**NOTE 10 - EMPLOYEE BENEFITS**

Employee Pension Plan: The pension plan is part of a noncontributory multi-employer defined-benefit pension plan covering substantially all employees. There is no separate actuarial valuation of plan benefits nor segregation of plan assets specifically for the Company. As of July 1, 2007, 2006 and 2005, the actuarially determined value of total vested benefits exceeded plan assets and a contribution and expense were required for fiscal 2008, 2007 and 2006. During fiscal 2008, 2007 and 2006, expense of \$76,000, \$120,000 and \$149,000 was recorded. For the years ending June 30, 2008, 2007, and 2006, administrative pension expenses were \$4,000 each year.

Effective July 1, 2008, the Bank approved a freeze of benefits accrued under the employee pension plan and no benefits for future employee service will be accrued.

401(k) Plan: A retirement savings 401(k) plan covers full time employees 21 or older that have completed one year of service. Participants may defer up to 50% of compensation. The Company matches 100% of elective deferrals on the first 4% of the participants' compensation, and the Company matches 50% of elective deferrals on the next 2% of the participant's compensation. Additionally, the Company may contribute up to 4% of each participant's compensation regardless of the participant's personal contributions to their 401(k) account depending on earnings and other benefit expenses. Expenses under this plan were \$96,000, \$91,000 and \$78,000 for 2008, 2007 and 2006.

Salary Continuation Plan: The Company maintains a Salary Continuation Plan (Plan) for certain executive officers. The Company is recording an expense equal to the projected present value of the payments due after retirement based on the participants' vesting schedules and projected remaining years of service. The accrued liability for this plan as of June 30, 2008 and 2007 was approximately \$313,000 and \$284,000 with expense of \$67,000, \$69,000 and \$65,000 recorded during the years ended June 30, 2008, 2007 and 2006.

**NOTE 11 – STOCK-BASED COMPENSATION**

The Company has two share based compensation plans as described below.

Stock Option Plan:

The 1992 Stock Option and Incentive Plan authorizes options of 169,000 shares of common stock. The 1999 Omnibus Incentive Plan authorizes 142,000 shares of common stock for options, restricted stock and stock appreciation rights. For both plans when options are granted, the option price is at least 100% of the market value of common stock on the date of grant and the option term cannot exceed 10 years. Options awarded may be exercised at a rate of 25% per year. Exercised options are generally issued from treasury stock. Total compensation cost that has been charged against income for this plan was \$5,000 and \$6,000 for fiscal year 2008 and 2007, respectfully, net of tax. No compensation expense was required to be recognized for stock options for 2006.

The fair value of each option award is established on the date of grant using a closed form option valuation (Black-Scholes) model that uses the assumptions noted in the table below. Expected volatilities are based on historical volatilities of the Company's common stock. The Company uses historical data to estimate option exercise and post-vesting termination behavior. (Employee and management options are tracked separately.) The expected term of options granted is based on historical data and represents the period of time that options granted are expected to be outstanding, which takes into account that the options are not transferable. The risk-free interest rate for the expected term of the option is based on the U.S. Treasury yield curve in effect at the time of the grant.

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**NOTE 11 – STOCK-BASED COMPENSATION** (Continued)

The fair value of options granted was determined using the following weighted-average assumptions as of the grant date. There were no options granted in 2008 or 2006.

	<u>2008</u>	<u>2007</u>	<u>2006</u>
Risk-free interest rate	n/a	4.77%	n/a
Expected option life in years	n/a	4.5	n/a
Expected stock price volatility	n/a	20.93%	n/a
Dividend yield	n/a	3.46%	n/a

Stock option plans are used to reward directors and certain executive officers and provide them with an additional equity interest. Options are issued for 10 year periods with varying vesting periods. A summary of the activity in the stock option plan for the year ended June 30, 2008 follows:

	Number of Outstanding Options	Exercise Price	Weighted Average Exercise Price
Outstanding, June 30, 2007	27,131	\$11.38 – 23.25	\$16.26
Granted	-	-	-
Forfeited or expired	-	-	-
Exercised	<u>5,700</u>	\$11.38 – 18.50	\$14.20
Outstanding, June 30, 2008	<u>21,431</u>	\$11.38 – 23.25	\$16.81

Information related to the stock option plan during the years ended June 30 follows:

	<u>2008</u>	<u>2007</u>	<u>2006</u>
Intrinsic value of options exercised	\$ 65,795	\$ 123,883	\$ 25,006
Cash received from option exercises	80,916	151,354	36,284
Tax benefit realized from option exercises	-	-	-
Weighted average fair value of options granted	-	3.99	-

As of June 30, 2008, there was \$18,000 of total unrecognized compensation cost related to nonvested stock options granted under the Plan. The cost is expected to be recognized over a weighted-average period of 1.8 years.

The weighted average remaining contractual life of options outstanding at June 30, 2008 was 4.9 years. Stock options exercisable at June 30, 2008 totaled 16,431 at a weighted average exercise price of \$15.03 with a weighted average remaining contractual life of 4.0 years. As of June 30, 2008, 71,668 options remain available for future grants.

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(Continued)

FFW CORPORATION  
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**NOTE 11 – STOCK-BASED COMPENSATION (Continued)**

Management Recognition and Retention Plans: The Management Recognition and Retention Plans (MRP) provide directors, officers and other key employees with a proprietary interest in the Company to encourage such persons to remain with the Company. Eligible directors, officers and other key employees of the Company become vested in shares of common stock awarded on a discretionary basis at a rate of 25% per year beginning on the date of grant. Expense of \$41,000, \$51,000 and \$50,000 was recorded for these plans for the years ended June 30, 2008, 2007 and 2006.

A summary of changes in the Company's nonvested shares for the year follows:

<u>Nonvested Shares</u>	<u>Shares</u>	<u>Weighted-Average Grant-Date Fair Value</u>
Nonvested at July 1, 2006	5,000	\$ 20.89
Granted	2,000	23.25
Vested	(2,000)	21.36
Forfeited	<u>-</u>	-
Nonvested at June 30, 2007	<u>5,000</u>	\$ 21.64
Granted	-	
Vested	(2,500)	21.74
Forfeited	<u>-</u>	-
Nonvested at June 30, 2008	<u>2,500</u>	\$ 21.55

As of June 30, 2008, there was \$40,000 of total unrecognized compensation cost related to nonvested shares granted under the Plan. The cost is expected to be recognized over a weighted-average period of 1.7 years. The total fair value of shares vested during the years ended June 30, 2008, 2007, and 2006 was \$41,000, \$51,000 and \$50,000.

**NOTE 12 - INCOME TAXES**

Income tax expense for the years ended June 30 was:

	<u>2008</u>	<u>2007</u>	<u>2006</u>
Federal			
Current	\$ 771,072	\$ 559,994	\$ 538,412
Deferred	<u>52,287</u>	<u>32,675</u>	<u>(51,334)</u>
	823,359	592,669	487,078
State			
Current	15,315	(3,996)	22,077
Deferred	<u>14,175</u>	<u>(4,538)</u>	<u>(4,676)</u>
	<u>29,490</u>	<u>(8,534)</u>	<u>17,401</u>
Income tax expense	<u>\$ 852,849</u>	<u>\$ 584,135</u>	<u>\$ 504,479</u>

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(Continued)

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**NOTE 12 - INCOME TAXES** (Continued)

Income tax expense differed from amounts computed using the U.S. federal income tax rate of 34% as follows:

	<u>2008</u>	<u>2007</u>	<u>2006</u>
Income taxes at 34% statutory rate	\$ 1,174,645	\$ 1,174,981	\$ 1,067,888
Tax effect of:			
Tax-exempt income, net	(186,263)	(214,715)	(259,922)
State tax, net of federal income tax effect	19,463	(5,632)	11,485
Earnings on life insurance	(79,990)	(76,230)	(72,502)
Dividends received deduction	(93,800)	(72,202)	(132,597)
Change in valuation allowance	177,125	(128,008)	-
Low income housing credits	(55,283)	(65,250)	(72,304)
Other	<u>(103,048)</u>	<u>(28,809)</u>	<u>(37,569)</u>
Total income tax expense	<u>\$ 852,849</u>	<u>\$ 584,135</u>	<u>\$ 504,479</u>

Components of the net deferred tax liability as of June 30 are:

	<u>2008</u>	<u>2007</u>	<u>2006</u>
Deferred tax assets:			
Bad debts	\$ 1,087,146	\$ 1,051,275	\$ 1,172,263
Deferred compensation	123,011	112,329	86,077
Core deposit intangible and goodwill	31,242	48,553	65,589
Other than temporary security impairment	120,941	-	613,615
Capital loss carry forward	541,791	485,607	-
Depreciation on debt securities AFS	258,327	80,116	87,804
Net deferred loan fees	23,008	14,688	-
Nonaccrual interest	2,692	80,877	-
General business credit carry forward	-	60,884	91,829
State net operating loss carry forward	-	17,549	15,516
Other	<u>64,380</u>	<u>52,383</u>	<u>38,793</u>
	2,252,538	2,004,261	2,171,486
Deferred tax liabilities:			
Accretion	(108,601)	(128,714)	(119,446)
Net deferred loan costs	-	-	(757)
Mortgage servicing rights	(191,799)	(226,786)	(238,329)
FHLB stock dividend	(140,835)	(142,067)	(147,825)
Prepaid expenses	(154,030)	(95,948)	(95,948)
Other	<u>(15,400)</u>	<u>(57,747)</u>	<u>(52,349)</u>
	(610,665)	(651,262)	(654,654)
Valuation allowance	<u>(662,732)</u>	<u>(485,607)</u>	<u>(613,615)</u>
Net deferred tax asset (liability)	<u>\$ 979,141</u>	<u>\$ 867,392</u>	<u>\$ 903,217</u>

The capital loss carry forward relates to sales of equity securities which expire in 2012.

Federal income tax laws provided savings banks with additional bad debt deductions through 1987, totaling \$1,156,000 for the Bank. Accounting standards do not require a deferred tax liability to be recorded on this amount, which liability otherwise would total \$393,000 at June 30, 2008. If the Bank was liquidated or otherwise ceased to be a bank or if tax laws were to change, the \$393,000 would be recorded as expense.

(Continued)

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**NOTE 13 - REGULATORY MATTERS**

The Bank is subject to regulatory capital requirements administered by federal banking 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.

The prompt corrective action regulations provide five classifications, including 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 undercapitalized, capital distributions are limited, as is asset growth and expansion, and plans for capital restoration are required. At year end 2008 and 2007, the most recent regulatory notifications categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. See Note 20 regarding events since that notification that may change the institution's category.

The Bank's actual capital and required capital amounts and ratios are presented below:

	<u>Actual</u>		<u>Minimum</u>		<u>Minimum</u>		
	<u>Amount</u>	<u>Ratio</u>	<u>For Capital</u>		<u>To Be Well</u>		
			<u>Adequacy Purposes</u>		<u>Capitalized Under</u>		
			<u>Amount</u>	<u>Ratio</u>	<u>Prompt Corrective</u>		
					<u>Action Provisions</u>		
					<u>Amount</u>	<u>Ratio</u>	
			(Dollars in thousands)				
As of June 30, 2008							
Total Capital	\$26,464	10.77%	\$ 19,657	8.00%	\$ 24,571	10.00%	
(to risk weighted assets)							
Tier I (Core) Capital	23,695	9.64%	9,828	4.00%	14,742	6.00%	
(to risk weighted assets)							
Tier I (Core) Capital	23,695	7.51%	12,617	4.00%	15,771	5.00%	
(to adjusted total assets)							
Tangible capital to average assets	23,695	7.85%	4,526	1.50%	N/A		
As of June 30, 2007							
Total Capital	\$25,434	11.82%	\$17,216	8.00%	\$21,520	10.00%	
(to risk weighted assets)							
Tier I (Core) Capital	22,780	10.59%	8,608	4.00%	12,912	6.00%	
(to risk weighted assets)							
Tier I (Core) Capital	22,780	7.89%	11,547	4.00%	14,433	5.00%	
(to adjusted total assets)							
Tangible capital to average assets	22,780	8.02%	4,261	1.50%	N/A		

Regulations of the Office of Thrift Supervision (OTS) limit the amount of dividends and other capital distributions that may be paid by a savings institution without prior approval of the OTS. Under the regulations, the Bank can make without application to the OTS (but only after filing a notification to the OTS), 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 (less any dividends previously paid) as long as the Bank would remain adequately capitalized, as defined in the OTS's prompt corrective action regulations, following the proposed distribution. Accordingly, at June 30, 2008, approximately \$2,817,000 of the Bank's retained earnings was potentially available for distribution to the Company.

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**NOTE 14 - FINANCIAL INSTRUMENTS WITH OFF-BALANCE-SHEET RISK AND CONTINGENCIES**

Various outstanding commitments and contingent liabilities are not reflected in the financial statements. Commitments to make loans at June 30 were as follows:

	<u>2 0 0 8</u>		<u>2 0 0 7</u>	
	<u>Fixed Rate</u>	<u>Variable Rate</u>	<u>Fixed Rate</u>	<u>Variable Rate</u>
Commitments to make loans	\$ 6,170,961	\$ 4,201,975	\$ 4,338,846	944,344
Unused lines of credit	2,727,480	31,164,093	2,694,697	29,518,121
Standby letters of credit	<u>647,890</u>	<u>4,280,405</u>	<u>-</u>	<u>6,696,073</u>
	<u>\$ 9,546,331</u>	<u>\$ 39,646,473</u>	<u>\$ 7,033,543</u>	<u>\$ 37,158,538</u>

Fixed rate loan commitments and unused lines of credit at June 30, 2008 were at current rates ranging from 5.75% to 9.00% for loan commitments and 5.47% to 18.00% for unused lines of credit.

Variable rate loan commitments, unused lines of credit and standby letters of credit at June 30, 2008 were at current rates ranging from 4.75% to 9.00% for loan commitments, 5.00% to 9.00% for unused lines of credit, and primarily at the national prime rate of interest plus 100 to 300 basis points for standby letters of credit.

Since commitments to make loans and to fund unused lines of credit, loans in process and standby letters of credit may expire without being used, the amounts do not necessarily represent future cash commitments. In addition, commitments are agreements to lend to a customer as long as there is no violation of any condition established in the contract. The maximum exposure to credit loss in the event of nonperformance by the other party is the contractual amount of these instruments. The same credit policy is used to make such commitments as is used for loans receivable.

Under employment agreements with 2 of its officers, certain events leading to separation from the Company could result in a lump sum cash payment.

The Company and the Bank are subject to certain claims and legal actions arising in the ordinary course of business. In the opinion of management, after consultation with legal counsel, the ultimate disposition of these matters is not expected to have a material adverse effect on the consolidated financial position or results of operations of the Company.

The Bank has a 3% limited partner interest in a limited partnership formed to construct, own and manage affordable housing projects. The Bank is one of 13 investors. As of June 30, 2008, the Bank had invested \$750,000 and had recorded equity in the operating loss of the limited partnership of \$31,000, \$28,000 and \$31,000 for the years ended June 30, 2008, 2007 and 2006. At both June 30, 2008 and 2007, the obligation due to the limited partnership was \$0. The Bank receives 3% of the eligible tax credits. For the years ended June 30, 2008, 2007 and 2006, the Bank received approximately \$52,000, \$65,000 and \$72,000 in tax credits. The future tax credits are projected to decline over the next 5 years and fully expire in 2013. A \$21,000 and \$69,000 non-cash impairment charge was recognized in 2008 and 2007, respectively, due to the carrying value of the investment exceeding the value of future tax benefits.

(Continued)

FFW CORPORATION  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
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**NOTE 15 - SIGNIFICANT CONCENTRATIONS OF CREDIT RISK**

Real estate and consumer loans, including automobile, home equity and improvement, manufactured home and other consumer loans are granted primarily in Wabash, Kosciusko and Whitley counties. Loans secured by one to four family residential real estate mortgages make up approximately 41% of the loan portfolio. The Company also sells loans and services loans for secondary market agencies.

The policy for collateral on mortgage loans allows borrowings up to 100%, if private mortgage insurance is obtained to reduce the Company's exposure to or below the 80% loan-to-value level on loans held for sale, and 90%, on in-house adjustable rate loans, of the appraised value of the property as established by appraisers approved by the Company's Board of Directors. Loan-to-value percentages and documentation guidelines are designed to protect the Company's interest in the collateral as well as to comply with guidelines for sale in the secondary market.

**NOTE 16 - RELATED PARTY TRANSACTIONS**

Certain directors, executive officers and principal shareholders of the Company, including associates of such persons, are loan customers. Related party loan balances were \$2,400,000 and \$2,316,000 at June 30, 2008 and 2007.

**NOTE 17 - PARENT COMPANY FINANCIAL STATEMENTS**

Presented below are condensed financial statements for the parent company, FFW Corporation.

CONDENSED BALANCE SHEETS  
June 30, 2008 and 2007

	<u>2008</u>	<u>2007</u>
<b>ASSETS</b>		
Cash and cash equivalents	\$ 154,688	\$ 239,019
Investment in subsidiaries	24,200,562	23,596,172
Securities AFS	382,723	1,065,496
Goodwill	238,430	238,430
Amortizable intangible	20,128	25,160
Other assets	7,809	10,558
Total assets	<u>\$ 25,004,340</u>	<u>\$ 25,174,835</u>
<b>LIABILITIES</b>		
Borrowings	\$ 1,258,400	\$ -
Deferred taxes	67,699	16,846
Accrued expenses and other liabilities	116,378	169,483
Total liabilities	<u>1,442,477</u>	<u>186,329</u>
<b>SHAREHOLDERS' EQUITY</b>		
Common stock	18,363	18,363
Additional paid-in capital	9,530,608	9,481,340
Retained earnings	25,965,339	24,334,484
Accumulated other comprehensive income (loss)	(653,825)	(164,556)
Treasury stock	<u>(11,298,622)</u>	<u>(8,681,125)</u>
Total shareholders' equity	<u>23,561,863</u>	<u>24,988,506</u>
Total liabilities and shareholders' equity	<u>\$ 25,004,340</u>	<u>\$ 25,174,835</u>

(Continued)

FFW CORPORATION  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
June 30, 2008, 2007 and 2006

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**NOTE 17 - PARENT COMPANY FINANCIAL STATEMENTS (Continued)**

**CONDENSED STATEMENTS OF INCOME**  
For the years ended June 30, 2008, 2007 and 2006

	<u>2008</u>	<u>2007</u>	<u>2006</u>
Interest income	\$ 33,078	\$ 57,254	\$ 64,324
Gain on the sale of securities AFS	59,225	-	61,900
Dividend income	1,700,000	1,600,000	1,600,000
Other income	<u>-</u>	<u>-</u>	<u>-</u>
	1,792,303	1,657,254	1,726,224
Interest expense	24,363	-	-
Operating expense	133,670	150,348	150,585
Equity in undistributed income of subsidiaries	<u>898,428</u>	<u>1,310,953</u>	<u>975,738</u>
<b>Income before income taxes</b>	2,532,698	2,817,859	2,551,377
Income tax benefit	<u>(69,291)</u>	<u>(53,833)</u>	<u>(84,991)</u>
<b>Net income</b>	<u>\$ 2,601,989</u>	<u>\$ 2,871,692</u>	<u>\$ 2,636,368</u>

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(Continued)

FFW CORPORATION  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
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**NOTE 17 - PARENT COMPANY FINANCIAL STATEMENTS (Continued)**

**CONDENSED STATEMENTS OF CASH FLOWS**  
For the years ended June 30, 2008, 2007 and 2006

	<u>2008</u>	<u>2007</u>	<u>2006</u>
<b>Cash flows from operating activities</b>			
Net income	\$ 2,601,989	\$ 2,871,692	\$ 2,636,368
Adjustments to reconcile net income to net cash from operating activities			
Equity in undistributed income of subsidiaries	(898,428)	(1,310,953)	(975,738)
Gain on the sale of securities	(59,225)	-	(61,900)
Stock option expense	7,864	8,787	-
Other	<u>71,620</u>	<u>38,306</u>	<u>(12,697)</u>
Net cash from operating activities	1,723,820	1,607,832	1,586,033
<b>Cash flows from investing activities</b>			
Proceeds from sales of securities	968,411	6,433	118,499
Maturities/calls of securities AFS	-	-	100,000
Purchases of securities	(427,100)	-	-
Investment in insurance subsidiary	<u>(20,000)</u>	<u>-</u>	<u>-</u>
Net cash from investing activities	521,311	6,433	218,499
<b>Cash flows from financing activities</b>			
Proceeds from borrowings	1,438,400	-	-
Repayment of borrowings	(180,000)	-	-
Proceeds from stock options	80,916	151,354	36,284
Purchase of treasury stock	(2,697,644)	(1,100,931)	(846,747)
Cash dividends paid	<u>(971,134)</u>	<u>(926,916)</u>	<u>(904,447)</u>
Net cash used in financing activities	(2,329,462)	(1,876,493)	(1,714,910)
Net change in cash and cash equivalents	(84,331)	(262,228)	89,622
Beginning cash and cash equivalents	<u>239,019</u>	<u>501,247</u>	<u>411,625</u>
<b>Ending cash and cash equivalents</b>	<u>\$ 154,688</u>	<u>\$ 239,019</u>	<u>\$ 501,247</u>

The extent to which the Company may pay cash dividends to shareholders will depend on the cash currently available at the Company, as well as the Bank's ability to pay dividends to the Company (see Note 13).

(Continued)

FFW CORPORATION  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
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**NOTE 18 - FAIR VALUES OF FINANCIAL INSTRUMENTS**

The following table shows estimated fair values and related carrying amounts of the Company's financial instruments at June 30. Items which are not financial instruments are not included.

	<u>2008</u>		<u>2007</u>	
	<u>Carrying</u> <u>Amount</u> (In thousands)	<u>Estimated</u> <u>Fair Value</u> (In thousands)	<u>Carrying</u> <u>Amount</u> (In thousands)	<u>Estimated</u> <u>Fair Value</u> (In thousands)
Cash and cash equivalents	\$ 8,443	\$ 8,443	\$ 7,623	\$ 7,623
Securities AFS	60,368	60,368	55,673	55,673
Loans receivable, net	227,840	227,185	207,776	205,378
Loans held for sale	77	78	178	180
Federal Home Loan Bank stock	3,627	3,627	3,627	3,627
Accrued interest receivable	1,560	1,560	1,731	1,731
Noninterest-bearing deposits	(13,738)	(13,738)	(13,706)	(13,706)
Interest-bearing deposits	(230,447)	(232,652)	(196,758)	(197,161)
Borrowings	(45,283)	(46,477)	(52,194)	(52,143)
Accrued interest payable	(337)	(337)	(364)	(364)

For purposes of the above disclosures of estimated fair value, the following assumptions were used as of June 30, 2008 and 2007. The estimated fair values for cash and cash equivalents, Federal Home Loan Bank stock, accrued interest receivable, noninterest-bearing deposits and accrued interest payable are considered to approximate cost. The estimated fair value for securities AFS is based on quoted market values for the individual securities or for equivalent securities. The estimated fair value for loans receivable, net, is based on estimates of the rate the Bank would charge for similar loans at June 30, 2008 and 2007 applied for the time period until the loans are assumed to reprice or be paid. The estimated fair value for interest-bearing deposits as well as borrowings is based on estimates of the rate the Bank would pay on such liabilities at June 30, 2008 and 2007, applied for the time period until maturity.

While these estimates of fair value are based on management's judgment of the most appropriate factors, there is no assurance that were the Company to have disposed of such items at June 30, 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 June 30, 2008 and 2007 should not necessarily be considered to apply to subsequent dates.

In addition, other assets and liabilities of the Company that are not defined as financial instruments are not included in the above disclosures, such as premises and equipment. Also, non-financial instruments typically not recognized in financial statements nevertheless may have value but are not included in the above disclosures. These include, among other items, the estimated earnings power of core deposit accounts, the trained work force, customer goodwill and similar items.

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**NOTE 19 – OTHER COMPREHENSIVE INCOME (LOSS)**

Other comprehensive income (loss) components and related taxes were as follows:

	<u>2008</u>	<u>2007</u>	<u>2006</u>
Net change in net unrealized appreciation (depreciation) on securities available for sale			
Net unrealized appreciation (depreciation) arising during the year	\$ (904,538)	\$ 430,344	\$ (690,106)
Reclassification adjustments for:			
Other than temporary impairment	308,000	-	-
(Gains) included in net income	<u>(70,944)</u>	<u>(365,206)</u>	<u>(60,599)</u>
Net change in net unrealized appreciation (depreciation) on securities available for sale	(667,482)	65,138	(750,705)
Tax expense (benefit)	<u>(178,213)</u>	<u>7,688</u>	<u>(327,060)</u>
Total other comprehensive income (loss)	<u>\$ (489,269)</u>	<u>\$ 57,450</u>	<u>\$ (423,645)</u>

**NOTE 20 – SUBSEQUENT EVENTS**

The Company currently holds preferred stock of the Federal National Mortgage Association (FNMA) with a par value of \$7,000,000. Subsequent to June 30 the fair value of this stock has varied widely, but has generally been at much lower levels than the June 30 value. Further, on September 7, 2008 the Federal Housing Finance Agency placed FNMA into conservatorship, which is a statutory process designed to stabilize a troubled institution with the objective of returning the entity to normal business operations. In addition, the dividend on the preferred stock has been suspended beginning September 7, 2008. Following the announcement of the conservatorship, the preferred stock was down-graded below investment grade by all three ratings agencies, and the fair value declined further. These subsequent events led the Company to conclude that the unrealized loss at June 30, 2008 was other than temporary, and the stock was written down to the June 30 fair value. Declines in value since June 30 are applicable to subsequent periods and have not been reflected in these financial statements. The ultimate outcome and time-frame of the conservatorship is not known, and, accordingly, it is not known what value may ultimately be realized from the stock and in what time-frame; however, at September 11, 2008, there is an unrealized loss of \$6,082,000 in the stock.

As discussed in Note 13, at June 30, 2008 the Bank was categorized as well capitalized under the regulatory framework for prompt corrective action. While the Bank expects to continue to meet all minimum requirements for capital adequacy, the decline in the fair value of the FNMA preferred stock is expected to change the Bank's capital classification from well capitalized to adequately capitalized, and this classification would result in the requirement to seek regulatory approval to accept brokered deposits.