



**INDEPENDENT AUDITOR'S REPORT AND
CONSOLIDATED FINANCIAL STATEMENTS**

DECEMBER 31, 2006 AND 2005

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INDEPENDENT AUDITOR'S REPORT

Board of Directors and Stockholders
AMB Financial Services Corporation and Subsidiary
Bainbridge Island, Washington

We have audited the consolidated statements of financial condition of AMB Financial Services Corporation and subsidiary (the Corporation) as of December 31, 2006 and 2005, and the related consolidated statements of income, changes in stockholders' equity, and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the 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 condition of AMB Financial Services Corporation and subsidiary as of December 31, 2006 and 2005, and the results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Moss Adams LLP

Spokane, Washington
March 16, 2007

AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
CONSOLIDATED STATEMENT OF FINANCIAL CONDITION

ASSETS

	December 31,	
	<u>2006</u>	<u>2005</u>
Cash and due from banks	\$ 9,699,431	\$ 7,471,327
Interest-bearing deposits in banks	5,098,140	3,520
Federal funds sold	4,477,922	5,028,207
Securities available for sale	50,012,434	49,941,251
Federal Home Loan Bank stock	3,256,800	3,256,800
Investment in limited partnership	760,374	852,710
Loans receivable, net of allowance for loan losses of \$3,413,705 2006; \$3,672,904 2005	289,379,892	258,114,938
Accrued interest receivable	2,171,480	1,731,923
Premises and equipment, net	13,369,207	14,422,461
Foreclosed real estate	118,000	1,818,900
Cash surrender value of life insurance policies	7,339,106	5,613,319
Goodwill	497,480	497,480
Other assets	2,074,204	4,858,452
TOTAL ASSETS	\$ 388,254,470	\$ 353,611,288

LIABILITIES AND STOCKHOLDERS' EQUITY

Deposits	\$ 305,736,129	\$ 280,410,760
Federal Home Loan Bank advances	42,898,131	34,064,798
Obligation to KSOP Plan	74,000	148,000
Other borrowings	1,667,071	1,863,241
Accrued interest payable	1,250,685	586,335
Other liabilities	2,733,886	2,881,286
Subordinated debentures	7,217,000	7,217,000
Total liabilities	361,576,902	327,171,420
COMMITMENTS (Note 7)		
STOCKHOLDERS' EQUITY		
Capital stock, no par; 2,000,000 shares authorized; 548,013 and 563,525 shares issued and outstanding in 2006 and 2005, respectively	5,450,217	6,733,119
Retained earnings	21,317,918	19,816,895
Accumulated other comprehensive loss	(90,567)	(110,146)
Total stockholders' equity	26,677,568	26,439,868
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 388,254,470	\$ 353,611,288

**AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
CONSOLIDATED STATEMENT OF INCOME**

	Year Ended December 31,	
	2006	2005
Interest income		
Loans receivable, including fees	\$ 21,895,400	\$ 19,176,496
Securities available for sale	2,137,294	1,856,823
Federal funds sold	72,544	244,906
Interest-bearing deposits	21,687	61,206
Total interest income	<u>24,126,925</u>	<u>21,339,431</u>
Interest expense		
Deposits	5,927,101	4,517,529
Federal Home Loan Bank advances	2,067,481	1,350,406
Other interest expense	814,016	490,748
Total interest expense	<u>8,808,598</u>	<u>6,358,683</u>
Net interest income	15,318,327	14,980,748
Provision for loan losses	880,000	560,000
Net interest income after provision for loan losses	<u>14,438,327</u>	<u>14,420,748</u>
Noninterest income		
Service charges	946,178	969,934
Income from trust fiduciary activities	1,229,659	1,131,381
Other income	1,770,586	1,799,189
Total noninterest income	<u>3,946,423</u>	<u>3,900,504</u>
Noninterest expenses		
Salaries and employee benefits	8,316,047	7,344,657
Occupancy	2,622,925	2,569,420
Salary continuance benefit	60,704	397,411
Professional fees	703,362	961,118
Printing and postage	319,258	292,265
Computer	502,765	452,488
Taxes and license	314,597	289,725
Communications	198,152	214,446
Advertising	172,188	175,328
Insurance	217,737	237,052
Directors fees	170,000	138,000
Exchange	273,749	235,492
Other	1,341,049	1,377,483
Total noninterest expense	<u>15,212,533</u>	<u>14,684,885</u>
Income before income taxes	3,172,217	3,636,367
Federal income tax expense	786,762	714,920
NET INCOME	<u>\$ 2,385,455</u>	<u>\$ 2,921,447</u>
Basic earnings per share	<u>\$ 4.29</u>	<u>\$ 5.16</u>
Diluted earnings per share	<u>\$ 4.19</u>	<u>\$ 4.99</u>

AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY

	Shares of Common Stock	Total Stockholders' Equity
	<u> </u>	<u> </u>
Balance, December 31, 2004	571,627	\$ 25,570,836
Net income for 2005	-	2,921,447
Cash dividends (\$1.20 per share)	-	(678,202)
Dividend payable on January 15, 2006 (\$.40 per share)	-	(225,410)
Repurchase of shares	(468)	(84,915)
Exercise of stock options	123	61,697
Shares repurchased from KSOP	(13,231)	(1,044,635)
Shares issued to KSOP	5,474	432,446
Net change in unrealized loss on securities available for sale, net of taxes	-	(513,396)
	<u> </u>	<u> </u>
Comprehensive income		
Balance, December 31, 2005	563,525	26,439,868
Net income for 2006	-	2,385,455
Cash dividends (\$1.20 per share)	-	(665,227)
Dividend payable on January 15, 2007 (\$.40 per share)	-	(219,205)
Repurchase of shares	(6,552)	(490,242)
Exercise of stock options	2,328	149,547
Stock option expense	-	17,273
Shares repurchased from KSOP	(11,288)	(959,480)
Net change in unrealized loss on securities available for sale, net of taxes	-	19,579
	<u> </u>	<u> </u>
Comprehensive income		
Balance, December 31, 2006	<u>548,013</u>	<u>\$ 26,677,568</u>

**AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY**

<u>Capital Stock</u>	<u>Retained Earnings</u>	<u>Accumulated Comprehensive Income (Loss)</u>	<u>Comprehensive Income</u>
\$ 7,368,526	\$ 17,799,060	\$ 403,250	
-	2,921,447	-	\$ 2,921,447
-	(678,202)	-	
-	(225,410)	-	
(84,915)	-	-	
61,697	-	-	
(1,044,635)	-	-	
432,446	-	-	
-	-	(513,396)	(513,396)
			<u>\$ 2,408,051</u>
6,733,119	19,816,895	(110,146)	
-	2,385,455	-	\$ 2,385,455
-	(665,227)	-	
-	(219,205)	-	
(490,242)	-	-	
149,547	-	-	
17,273	-	-	
(959,480)	-	-	
-	-	19,579	19,579
			<u>\$ 2,405,034</u>
<u>\$ 5,450,217</u>	<u>\$ 21,317,918</u>	<u>\$ (90,567)</u>	

See accompanying notes.

AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
CONSOLIDATED STATEMENT OF CASH FLOWS

	Year Ended December 31,	
	2006	2005
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	\$ 2,385,455	\$ 2,921,447
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	1,516,675	1,414,381
Provision for loan losses	880,000	560,000
Amortization (accretion) of investment premium (discount), net	198,854	350,588
(Increase) decrease in deferred taxes	(294,482)	400,888
Loss on investment in limited partnership	92,336	147,290
Realized gain on sale of foreclosed real estate	(190,918)	(23,557)
Loss on sale of premises and equipment	3,507	2,346
Stock-based compensation expense	17,273	-
Net (increase) decrease in accrued interest receivable and other assets	2,629,058	(3,565,631)
Net increase in cash surrender value of life insurance	(130,787)	(223,558)
Increase in accrued interest payable and other liabilities	523,155	448,650
	7,630,126	2,432,844
CASH FLOWS FROM INVESTING ACTIVITIES		
Net decrease in federal funds sold	550,285	(2,528,207)
Net (increase) decrease in interest-bearing deposits in banks	(5,094,620)	5,222,551
Loans made and principal collected, net	(32,144,954)	(10,812,299)
Activity in available for sale securities:		
Proceeds from maturities, calls, and principal repayments of securities	10,390,143	8,567,313
Purchases of securities	(10,630,486)	(15,898,275)
Purchase of Federal Home Loan Bank stock	-	(13,600)
Proceeds from Federal Home Loan Bank stock redemption	-	116,700
Purchase of life insurance policy	(1,595,000)	-
Purchases of premises and equipment	(467,553)	(3,078,367)
Proceeds from sales of premises and equipment	625	-
Proceeds from sales of foreclosed real estate	1,891,818	1,255,673
	(37,099,742)	(17,168,511)

**AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
CONSOLIDATED STATEMENT OF CASH FLOWS**

	Year Ended December 31,	
	2006	2005
CASH FLOWS FROM FINANCING ACTIVITIES		
Net increase in deposits	\$ 25,325,369	\$ 18,185,698
Net increase in Federal Home Loan Bank advances	8,833,333	87,608
Dividends paid on common stock	(890,637)	(906,853)
Proceeds from issuance of common stock	149,547	61,697
Repurchase of common stock	(1,449,722)	(697,104)
Repayment of KSOP loan	(74,000)	(74,000)
Proceeds from other borrowings	250,000	-
Repayment of other borrowings	(446,170)	(289,757)
	31,697,720	16,367,289
NET CHANGE IN CASH AND DUE FROM BANKS	2,228,104	1,631,622
Cash and due from banks at January 1	7,471,327	5,839,705
Cash and due from banks at December 31	\$ 9,699,431	\$ 7,471,327
 SUPPLEMENTAL DISCLOSURE OF CASH FLOWS INFORMATION		
Cash paid during the year for:		
Interest	\$ 8,144,248	\$ 6,339,121
Income taxes	\$ 785,000	\$ 507,000
 SUPPLEMENTAL SCHEDULE OF NONCASH INVESTING ACTIVITIES		
Net change in unrealized gain on securities available for sale	\$ 29,694	\$ (777,873)
Acquisition of real estate and other repossessed assets in settlement of loans	\$ -	\$ 7,000
Completion of development of property held for sale	\$ -	\$ 1,677,171

See accompanying notes.

AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1 - Summary of Significant Accounting Policies

Basis of consolidation:

The consolidated financial statements include the accounts of AMB Financial Services Corporation (the Corporation) and its wholly-owned subsidiary, American Marine Bank, after eliminating all significant intercompany accounts and transactions.

Nature of business:

The Corporation's primary business activities are conducted through its Bank subsidiary. American Marine Bank is a state chartered commercial bank under the laws of the state of Washington. The Corporation and its subsidiary are subject to the regulations of certain federal and state agencies and undergoes periodic examinations by those regulatory agencies.

Use of estimates:

In preparing consolidated financial statements in conformity with accounting principles generally accepted in the United States of America, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the statement of financial condition and certain revenues and expenses during the reporting period. Actual results could differ, either positively or negatively, from those estimates. Material estimates that are particularly susceptible to significant change in the near-term relate to the determination of the allowance for loan losses and the valuation of real estate acquired in connection with foreclosures or in satisfaction of loans. In connection with the determination of the allowances for loan losses and other real estate owned, management obtains independent appraisals for significant properties.

Management believes that the allowances for loan losses and other real estate owned are adequate. While management uses currently available information to recognize losses on loans and other real estate, future additions to the allowances may be necessary based on changes in economic conditions. In addition, various regulatory agencies, as an integral part of their examination process, periodically review the Corporation's allowances for loan losses and other real estate owned. Such agencies may require the Corporation to recognize additions to the allowances based on their judgments of information available to them at the time of their examination.

Cash and due from banks:

For the purpose of presentation in the statement of cash flows, cash and due from banks include cash on hand and amounts due from banks. The Corporation is required to maintain minimum balances with the Federal Reserve Bank. The total required minimum balance at December 31, 2006, was \$145,000.

Concentration of cash:

The Corporation places its cash with high credit quality institutions. The amount on deposit fluctuates, and at times exceeds the insured limit by the U.S. Federal Deposit Insurance Corporation, and this potentially subjects the Corporation to credit risk.

**AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

Note 1 - Summary of Significant Accounting Policies (Continued)

Interest-bearing deposits in banks:

Interest-bearing deposits in banks generally mature within one year and are carried at cost.

Securities:

Debt securities that management has the positive intent and ability to hold to maturity are classified as held to maturity and recorded at amortized cost. Securities not classified as held to maturity, including equity securities with readily determinable fair values, are classified as available for sale and recorded at fair value, with unrealized gains and losses excluded from earnings and reported in other comprehensive income. The Corporation had no investments classified as held to maturity at December 31, 2006 or 2005.

Purchased premiums and discounts are recognized in interest income using the interest method over the terms of the securities. Declines in the fair value of held to maturity and available for sale securities below their cost that are deemed to be other than temporary are reflected in earnings as realized losses. Gains and losses on the sale of securities are recorded on the trade date and are determined using the specific identification method.

Federal Home Loan Bank stock:

The Corporation holds stock in the Federal Home Loan Bank (FHLB). Federal Home Loan Bank stock is a required investment for institutions that are members of the FHLB. The required investment in common stock is based on a predetermined formula and is carried at par value on the consolidated statement of financial condition. The stock can be sold back to the FHLB at cost, but is restricted as to purchase and sale based on the level of business activity the Corporation is engaged in with the FHLB.

On October 11, 2006, the Federal Housing Finance Board approved changes to the Capital Plan of the Federal Home Loan Bank of Seattle. The Capital Plan amendments provided for consolidation of the class B(1) and B(2) stock into a single class B stock and created a new class A stock with a six-month redemption period. Members of the FHLB Seattle can purchase class A stock when they have fully utilized their class B stock and want to continue borrowing from FHLB. The Corporation had \$3,256,800 in class B stock at December 31, 2006, which was converted from B(1) stock in its entirety at December 31, 2005.

Investment in limited partnership:

The Corporation owns two units of Homestead Equity Fund A, a limited partnership. The investment is accounted for in accordance with the equity method of accounting for investments. The initial investment was partially funded by a \$980,000 note payable to the limited partnership (see Note 11). Net losses were recorded by the Corporation for the years ended December 31, 2006 and 2005, in the amount of \$92,336 and \$147,290, respectively, which is included in other noninterest expenses on the consolidated statement of income.

Loans receivable:

The Corporation grants mortgage, commercial, and consumer loans to customers. The ability of the Corporation's debtors to honor their contracts is dependent mostly upon the real estate and general economic conditions in western Washington.

AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1 - Summary of Significant Accounting Policies (Continued)

Loans receivable (continued):

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

Loans are placed in a nonaccrual status when there is concern that principal and interest may not be fully collected or the loan has been in default for a period of 90 days or more. Loans that are in default over 90 days may continue to accrue interest if the loan is well collateralized and in the process of collection. Once in nonaccrual, no interest is taken into income unless received in cash or until such time as the borrower demonstrates the ability to resume payments to principal and interest. Interest previously accrued but not collected is generally reversed and charged against income at the time the loan is placed on nonaccrual status. In general, the Corporation considers nonaccrual loans, as well as certain watch list and internally classified loans, to be impaired.

The accrual of interest on impaired loans is discontinued when, in management's opinion, the borrower may be unable to meet payments as they become due. When interest accrual is discontinued, all unpaid accrued interest is reversed. Interest income is subsequently recognized only to the extent cash payments are received.

Allowances for loan losses:

The allowance for loan losses is increased by charges to income and decreased by charge offs (net of recoveries). Management's periodic evaluation of the adequacy of the allowance is based on the Corporation's past loan loss experience, known and inherent risks in the portfolio, adverse situations that may affect the borrower's ability to repay, the estimated value of any underlying collateral, and current economic conditions.

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

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

**AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

Note 1 - Summary of Significant Accounting Policies (Continued)

Foreclosed real estate:

Real estate properties acquired through, or in lieu of, foreclosure are to be sold and are initially recorded at fair value at the date of foreclosure establishing a new cost basis. After foreclosure, valuations are periodically performed by management and the real estate is carried at the lower of carrying amount or fair value less selling cost.

Premises and equipment:

Premises and equipment are stated at cost less accumulated depreciation over estimated useful lives which range from 3 to 40 years. Depreciation and amortization expense is computed using primarily the straight-line method for financial statement purposes. Accelerated depreciation methods are used for federal income tax purposes. Normal costs of maintenance and repairs are charged to expense as incurred.

Long-lived assets:

The Corporation evaluates the carrying value of long-lived assets based on current and anticipated discounted cash flows and recognizes impairment when such cash flows will be less than the carrying value of the asset. At December 31, 2006 and 2005, no assets had been written down for impairment.

Income taxes:

Deferred income taxes are reported for temporary differences between items of income or expense reported in the financial statements and those reported for income tax purposes. Federal income tax expense differs from income taxes computed at the statutory tax rates due to permanent and temporary differences in the recognition of certain items for tax versus book purposes. These differences are primarily related to the treatment of depreciation expense, the provision for loan losses, loan-fee amortization, tax-exempt net interest income, salary continuance agreements, and certain other expenses, which are treated differently for book and tax purposes.

Trust operations:

Assets held in a fiduciary or agency capacity for customers are not assets of the Corporation and, accordingly, are not included in the consolidated statement of financial condition.

Retained earnings:

Banking regulations limit the amount of dividends that may be paid to the amount of retained earnings then on hand, less any net losses and bad debts. An exception may be made only with the prior approval of the Board and stockholders representing at least two-thirds of the shares of stock outstanding.

Employee Stock Ownership Plan:

The Corporation sponsors an Employee Stock Ownership Plan with 401(k) provisions (KSOP). The KSOP is accounted for in accordance with the American Institute of Certified Public Accountants Statement of Position No. 93-6, *Employer's Accounting for Employee Stock Ownership Plans*.

AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1 - Summary of Significant Accounting Policies (Continued)

Stock options:

The Corporation has established an incentive stock option plan for key employees, and a nonqualified stock option plan for Directors of the Corporation, which are described more fully in Note 13. Effective January 1, 2006, the Corporation adopted Statement on Financial Accounting Standards (SFAS) No. 123(R), *Share-Based Payment*, a revision of SFAS 123, *Accounting for Stock-Based Compensation*. The revision requires the Corporation to recognize compensation cost as a reduction of net income for the fair value of stock-based compensation. The cost is based on the grant-date fair value of the award and is recorded over the vesting period of the stock award.

The following table illustrates the effect on net income and earnings per share if the Corporation had applied the fair value recognition provisions of this standard to stock-based employee compensation in the prior year:

	December 31, 2005
Net income, as reported	\$ 2,921,447
Deduct total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	<u>(15,518)</u>
Pro forma net income	<u>\$ 2,905,929</u>
Earnings per share:	
Basic-as reported	<u>\$ 5.16</u>
Basic-pro forma	<u>\$ 5.13</u>
Diluted-as reported	<u>\$ 4.99</u>
Diluted-pro forma	<u>\$ 4.87</u>

Earnings per share:

All per share amounts have been calculated on the basis of basic weighted-average number of shares outstanding during each year. Earnings per share assuming full dilution reflects additional common shares that would have been outstanding if dilutive potential common shares had been issued, as well as any adjustment to income that would result from the assumed issuance. Potential common shares that may be issued by the Corporation related solely to outstanding stock options are determined using the treasury stock method.

Total weighted-average shares outstanding were 555,698 and 566,520 at December 31, 2006 and 2005, respectively.

**AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

Note 1 - Summary of Significant Accounting Policies (Continued)

Comprehensive income:

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

The components of other comprehensive income and related tax effects are as follows:

	Year Ended December 31	
	2006	2005
Unrealized holding gains (losses) on available for sale securities	\$ 29,694	\$ (777,873)
Reclassification adjustment for gains realized in income	-	-
	29,694	(777,873)
Net unrealized gains (losses)	29,694	(777,873)
Tax effect	(10,115)	264,477
	NET OF TAX AMOUNT	NET OF TAX AMOUNT
	\$ 19,579	\$ (513,396)

Recent accounting pronouncements:

SFAS No. 155, Accounting for Certain Hybrid Instruments

This standard amends the guidance in SFAS Nos. 133 and 140 and is effective for all financial instruments acquired or issued after the beginning of an entity's first fiscal year that begins after September 15, 2006. SFAS No. 155 allows financial instruments that have embedded derivatives to be accounted for as a whole (eliminating the need to bifurcate the derivative from its host) if the holder elects to account for the whole instrument on a fair value basis. This statement allows an entity to make an irrevocable election to measure such a hybrid financial instrument at fair value in its entirety, with changes in fair value recognized in earnings. The election may be made on an instrument-by-instrument basis and can be made only when a hybrid financial instrument is initially recognized or when certain events occur that constitute a remeasurement (i.e., new basis) event for a previously recognized hybrid financial instrument. An entity must document its election to measure a hybrid financial instrument at fair value, either concurrently or via a preexisting policy for automatic election. Once the fair value election has been made, that hybrid financial instrument may not be designated as a hedging instrument pursuant to SFAS No. 133.

AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1 - Summary of Significant Accounting Policies (Continued)

Recent accounting pronouncements (continued):

SFAS No. 155, Accounting for Certain Hybrid Instruments (continued)

The FASB believes the issuance of SFAS No. 155 provides for the following:

- Clarifies which interest-only strips and principal-only strips are not subject to the requirements of SFAS No. 133;
- Establishes a requirement to evaluate interests in securitized financial assets to identify interests that are freestanding derivatives or that are hybrid financial instruments that contain an embedded derivative requiring bifurcation;
- Clarifies that concentrations of credit risk in the form of subordination are not embedded derivatives; and
- Amends SFAS No. 140 to eliminate the prohibition on a qualifying special-purpose entity from holding a derivative financial instrument that pertains to a beneficial interest other than another derivative financial instrument.

SFAS No. 155 is not expected to have a material impact on the Corporation.

SFAS No. 156, Accounting for Servicing of Financial Assets—an amendment of FASB Statement No. 140

This standard amends the guidance in SFAS No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities, to simplify the accounting for servicing assets and liabilities, such as those common with mortgage securitization activities. Specifically, the new Standard addresses the recognition and measurement of separately recognized servicing assets and liabilities and provides an approach to simplify efforts to obtain hedge-like (offset) accounting. The standard clarifies when an obligation to service financial assets should be separately recognized as a servicing asset or a servicing liability. This standard also requires all separately recognized servicing assets and servicing liabilities to be initially measured at fair value, if practicable, and permits an entity to choose either the amortization method or the fair value measurement method for subsequent measurement of each class of separately recognized servicing assets and servicing liabilities. SFAS No. 156 is effective as of the beginning of an entity's first fiscal year that begins after September 15, 2006. Earlier adoption is permitted as of the beginning of an entity's fiscal year, provided the entity has not issued financial statements. The Corporation does not believe this statement will have a material impact on the financial statements.

SFAS No. 157, Fair Value Measurements

This statement defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. This statement applies under other accounting pronouncements that require or permit fair value measurements. Accordingly, this statement does not require any new fair value measurements. This statement is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. SFAS No. 157 is not expected to have a material impact on the Corporation.

**AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

Note 1 - Summary of Significant Accounting Policies (Continued)

Recent accounting pronouncements (continued):

FASB Interpretation (FIN) No. 48, Accounting for Uncertainty in Income Taxes - An Interpretation of FASB Statement No. 109

FIN No. 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with SFAS No. 109, Accounting for Income Taxes. FIN No. 48 also prescribes a consistent 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. The new FASB standard also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition.

The evaluation of a tax position in accordance with FIN No. 48 is a two-step process. The first step is a recognition process whereby the enterprise determines whether it is more likely than not that a tax position will be sustained upon examination, including resolution of any related appeals or litigation processes, based on the technical merits of the position. In evaluating whether a tax position has met the more-likely-than-not recognition threshold, the enterprise should presume that the position will be examined by the appropriate taxing authority that has full knowledge of all relevant information. The second step is a measurement process whereby a tax position that meets the more-likely-than-not recognition threshold is calculated to determine the amount of benefit to recognize in the financial statements. The tax position is measured at the largest amount of benefit that is greater than 50% likely of being realized upon ultimate settlement.

The provisions of FIN No. 48 are effective for fiscal years beginning after December 15, 2006. Earlier application is permitted as long as the enterprise has not yet issued financial statements, including interim financial statements, in the period of adoption. The provisions of FIN No. 48 are to be applied to all tax positions upon initial adoption of this standard. Only tax positions that meet the more-likely-than-not recognition threshold at the effective date may be recognized or continue to be recognized upon adoption of FIN No. 48. The cumulative effect of applying the provisions of FIN No. 48 should be reported as an adjustment to the opening balance of retained earnings (or other appropriate components of equity or net assets in the statement of financial position) for that fiscal year. FIN No. 48 is not expected to have a material impact on the Corporation.

Reclassifications:

Certain reclassifications have been made in the December 31, 2005, consolidated financial statements in order to conform with the December 31, 2006, presentation with no effect on previously reported net income or equity.

AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 2 - Securities

Debt securities have been classified in the consolidated statement of financial condition according to management's intent. The carrying amounts of securities and their approximate fair values were as follows:

	December 31, 2006			Fair Value
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	
Securities available for sale:				
U.S. government and agency	\$ 25,360,890	\$ 37,127	\$ (270,881)	\$ 25,127,136
State, county, and municipal	18,780,815	244,090	(63,436)	18,961,469
Corporate bonds	1,522,260	17,178	(18,793)	1,520,645
Mortgage backed securities	4,485,663	6,801	(89,280)	4,403,184
	\$ 50,149,628	\$ 305,196	\$ (442,390)	\$ 50,012,434

	December 31, 2005			Fair Value
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	
Securities available for sale:				
U.S. government and agency	\$ 26,843,693	\$ 56,376	\$ (398,487)	\$ 26,501,582
State, county, and municipal	15,094,759	348,564	(63,358)	15,379,965
Corporate bonds	1,549,405	31,943	(29,742)	1,551,606
Mortgage backed securities	6,620,143	14,147	(126,192)	6,508,098
	\$ 50,108,000	\$ 451,030	\$ (617,779)	\$ 49,941,251

The following table shows the Corporation's gross unrealized losses and fair value of investments, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, at December 31, 2006. These securities consist primarily of debt securities and are not considered other than temporarily impaired because their impairment is due primarily to short term fluctuations in interest rates.

	December 31, 2006					
	Impaired Less Than 12 Months		Impaired 12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. government and agency	\$ 20,533,953	\$ (249,974)	\$ 4,042,654	\$ (20,907)	\$ 24,576,607	\$ (270,881)
State, county, and municipal	2,821,228	(27,785)	6,212,891	(35,651)	9,034,119	(63,436)
Corporate bonds	1,010,943	(18,793)	-	-	1,010,943	(18,793)
Mortgage backed securities	3,396,255	(80,943)	873,226	(8,337)	4,269,481	(89,280)
	\$ 27,762,379	\$ (377,495)	\$ 11,128,771	\$ (64,895)	\$ 38,891,150	\$ (442,390)

**AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

Note 2 - Securities (Continued)

The scheduled maturities of securities available for sale at December 31, 2006, were as follows. Expected maturities will differ from contractual maturities because borrowers have the right to call or prepay obligations with or without penalties. As such mortgage-backed securities are not classified by maturity due to the variation of the timing in which payments will be received.

	Amortized Cost	Fair Value
Maturing in less than one year	\$ 17,913,234	\$ 17,794,624
Maturing in one to five years	15,952,720	15,849,176
Maturing in five to ten years	5,020,273	5,149,353
Maturing after ten years	6,777,738	6,816,097
Mortgage backed securities	4,485,663	4,403,184
	<u>\$ 50,149,628</u>	<u>\$ 50,012,434</u>

The carrying amount of securities pledged to secure public deposits and for other purposes, and their approximate fair values at December 31 were as follows:

	2006		2005	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
To secure short term borrowings and trust collateral	\$ 3,583,361	\$ 3,566,760	\$ 2,047,035	\$ 2,064,108
Treasury tax and loan account	1,067,904	1,065,524	118,094	124,456
To secure public deposits	1,055,203	1,021,875	1,067,051	1,035,000
	<u>\$ 5,706,468</u>	<u>\$ 5,654,159</u>	<u>\$ 3,232,180</u>	<u>\$ 3,223,564</u>

No securities available for sale were sold during the years ended December 31, 2006 or 2005.

AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 3 - Loans Receivable and Allowance for Credit Losses

Major classifications of loans at December 31 were as follows:

	<u>2006</u>	<u>2005</u>
Commercial and real estate	\$ 261,108,889	\$ 230,221,465
Home equity	24,652,534	22,499,751
Consumer installment loans	4,940,382	6,853,383
Credit cards	2,667,998	2,825,313
	293,369,803	262,399,912
Allowance for loan losses	(3,413,705)	(3,672,904)
Deferred loan fees, net of deferred costs	(576,206)	(612,070)
	\$ 289,379,892	\$ 258,114,938

The interest rates on loans are segregated into the following fixed and variable components at December 31:

	<u>2006</u>	<u>2005</u>
Fixed	\$ 184,531,870	\$ 170,480,274
Variable	108,837,933	91,919,638
	\$ 293,369,803	\$ 262,399,912

Impairment of loans having recorded investments of \$7,662,618 and \$6,425,448 at December 31, 2006 and 2005, respectively, has been recognized in conformity with SFAS No. 114 as amended by SFAS No. 118. The total allowance for loan losses related to these loans was \$436,480 and \$491,467 at December 31, 2006 and 2005, respectively. The Corporation is not committed to lend additional funds to debtors whose loans have been modified. The average recorded investment in impaired loans during the years ended December 31, 2006 and 2005, was \$8,443,245 and \$7,068,308, respectively. Interest income on impaired loans of \$680,592 and \$550,211 was recognized for cash payments received in 2006 and 2005, respectively. The Corporation had loans with a balance of \$122,038 and \$65,547 on nonaccrual status at December 31, 2006 and 2005, respectively. Total loans past due 90 days or more and still accruing interest were \$-0- and \$1,767,903 at December 31, 2006 and 2005, respectively.

**AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

Note 3 - Loans Receivable and Allowance for Credit Losses (Continued)

An analysis of the changes in the allowance for loan losses is as follows:

	<u>2006</u>	<u>2005</u>
Allowance for loan losses:		
Balance, beginning of year	\$ 3,672,904	\$ 3,670,159
Provision charged to expense	874,129	560,000
Losses charged to allowance	(1,143,869)	(308,049)
Recoveries of losses previously charged off	10,541	48,432
Reclassification of reserve for undisbursed loans	-	(297,638)
	<u>\$ 3,413,705</u>	<u>\$ 3,672,904</u>
Reserve for unfunded commitments, included in other liabilities on the accompanying balance sheet:		
Balance, beginning of year	\$ 297,638	\$ -
Provision charged to expense	5,871	-
	<u>-</u>	<u>297,638</u>
	<u>\$ 303,509</u>	<u>\$ 297,638</u>
Allowance for credit losses:		
Allowance for loan losses	\$ 3,413,705	\$ 3,672,904
Reserve for unfunded commitments	303,509	297,638
	<u>\$ 3,717,214</u>	<u>\$ 3,970,542</u>

Loans serviced for others are not included in the accompanying consolidated balance sheet. The unpaid principal balances of mortgage and other loans serviced for others were \$60,282,425 and \$47,932,799 at December 31, 2006 and 2005, respectively.

Note 4 - Foreclosed Real Estate

Loans transferred into foreclosed real estate during the years ended December 31, 2006 and 2005, were \$0 and \$7,000, respectively. In addition, property for sale totaling \$1,677,171 was transferred from premises and equipment into foreclosed real estate during the year ended December 31, 2005. Foreclosed real estate was adjusted to net realizable value when it was originally transferred in from the loan balance and was adjusted down again when management received revised estimates of fair value during the year. Proceeds from the sale of foreclosed real estate were \$1,832,318 and \$1,255,673 for the years ended December 31, 2006 and 2005, respectively. There was no valuation allowance recognized on foreclosed real estate at December 31, 2006 and 2005.

AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 5 - Premises and Equipment

Major classifications of premises and equipment at December 31 were as follows:

	<u>2006</u>	<u>2005</u>
Land	\$ 1,193,006	\$ 1,193,006
Buildings and leasehold improvements	11,459,778	11,368,060
Equipment	8,440,150	8,374,599
	21,092,934	20,935,665
Less accumulated depreciation and amortization	(7,875,712)	(6,674,238)
Construction in process	151,985	161,034
	<u>\$ 13,369,207</u>	<u>\$ 14,422,461</u>

Depreciation and amortization expense for the years ended December 31, 2006 and 2005, was \$1,516,675 and \$1,414,381, respectively.

The Corporation has entered into certain noncancelable operating lease agreements for branch facilities and equipment that have initial or remaining terms in excess of one year as of December 31, 2006. Net rent expense under operating leases was \$548,937 and \$499,389 for the years ended December 31, 2006 and 2005, respectively.

The future minimum annual payments under these agreements at December 31, 2006, exclusive of taxes and other charges, were as follows:

Years ending December 31,	
2007	\$ 483,758
2008	562,601
2009	572,367
2010	595,435
2011	600,196
Thereafter	<u>4,703,996</u>
	<u>\$ 7,518,353</u>

**AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

Note 6 - Deposits

Major classifications of deposits at December 31 were as follows:

	<u>2006</u>	<u>2005</u>
Demand	\$ 14,436,492	\$ 36,531,404
Interest checking and Money Market	122,373,800	104,159,363
Savings	23,381,862	27,677,225
Time, \$100,000 and over	69,346,113	55,732,321
Other time	60,410,845	41,236,329
IRA	7,684,140	6,787,077
Other	8,102,877	8,287,041
	<u>\$ 305,736,129</u>	<u>\$ 280,410,760</u>

The following is a schedule by years of maturities for time deposits as of December 31, 2006:

Years ending December 31,	
2007	\$ 101,731,298
2008	19,276,056
2009	3,837,773
2010	3,071,128
2011	1,741,756
2012	98,947
	<u>\$ 129,756,958</u>

Note 7 - Commitments

The Corporation is a party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit and standby letters of credit. Those instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the statement of financial condition. The contract or notional amounts of those instruments reflect the extent of involvement the Corporation has in particular classes of financial instruments.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Corporation evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained if deemed necessary by the Corporation upon extension of credit is based on management's credit evaluation of the counterparty. Collateral held varies but may include accounts receivable, inventory, property, plant, and equipment, and income producing commercial properties.

AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 7 - Commitments (Continued)

At December 31, 2006, commitments to extend credit were as follows:

	Contract or Notional Amount	
	<u>2006</u>	<u>2005</u>
Loan commitments, including credit cards	\$ 72,311,906	\$ 77,533,243
Standby and performance letters of credit	1,418,178	1,183,178
TOTAL CREDIT COMMITMENTS	<u>\$ 73,730,084</u>	<u>\$ 78,716,421</u>

In addition, the Corporation has a courtesy overdraft protection program for customers who meet certain qualifications. Under this program, the Corporation advances funds to cover overdrawn accounts up to \$300, \$500, \$1,000, or \$5,000 per account, depending on the customer's account type. The commitment related to this program as of December 31, 2006, was \$3,813,381, of which \$32,256 was utilized. The commitment as of December 31, 2005, was \$4,682,872, of which \$21,672 was utilized.

The Corporation's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and standby letters of credit is represented by the above contractual notional amount.

The Corporation does not anticipate any material losses as a result of the commitments.

Substantially all the Corporation's loans, commitments, and commercial and standby letters of credit have been granted to customers in the Corporation's market area. As such, significant changes in economic conditions in the Pierce, King, Kitsap, and Jefferson Counties areas or with its primary industries could adversely effect the Corporation's ability to collect loans. The majority of such customers are depositors of the Corporation. The concentrations of credit by type of loan are set forth in Note 3. Commercial and standby letters of credit were granted primarily to commercial borrowers. The Corporation, bound by statutory limits, does not extend credit to any single borrower or group of related borrowers in excess of \$6,752,408. By Bank policy, however, this amount is not to exceed \$4,000,000.

Note 8 - Income Taxes

The components of income tax expense consisted of the following for the years ended December 31:

	<u>2006</u>	<u>2005</u>
Current tax expense	\$ 1,081,216	\$ 314,032
Deferred tax (benefit) expense	(294,454)	400,888
INCOME TAX EXPENSE	<u>\$ 786,762</u>	<u>\$ 714,920</u>

**AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

Note 8 - Income Taxes (Continued)

The net deferred tax assets are included in other assets in the accompanying statement of financial condition and consisted of the following components at December 31:

	<u>2006</u>	<u>2005</u>
Deferred tax assets:		
Allowance for loan losses	\$ 1,088,600	\$ 1,130,603
Salary continuance plan	627,733	688,238
Nondeductible acquisition costs	36,162	36,162
Net unrealized losses on securities available for sale	46,655	56,742
Other	19,725	1,557
	<u>1,818,875</u>	<u>1,913,302</u>
Deferred tax liabilities:		
Accumulated depreciation and amortization	(504,230)	(845,665)
Goodwill	(63,427)	(50,742)
Loan origination costs	(79,581)	(22,409)
FHLB stock dividends	(321,072)	(328,678)
Book-tax basis differential in limited partnership	(5,006)	(10,797)
Prepaid expenses	(81,227)	(158,913)
Mortgage servicing rights	(16,201)	(32,334)
	<u>(1,070,744)</u>	<u>(1,449,538)</u>
Total deferred tax liabilities	<u>(1,070,744)</u>	<u>(1,449,538)</u>
NET DEFERRED TAX ASSET	<u>\$ 748,131</u>	<u>\$ 463,764</u>

At December 31, 2006 and 2005, an income tax liability of \$16,627 and \$113,446, respectively, was included in other liabilities on the consolidated statement of financial condition.

The effective tax rate differs from the statutory federal tax rate for the years presented as follows:

	<u>2006</u>	<u>2005</u>
Federal income tax at statutory rate	\$ 1,078,553	\$ 1,236,365
Effect of permanent differences	(244,374)	(279,274)
Effect of income tax credits	(66,643)	(182,438)
Other	19,226	(59,733)
	<u>786,762</u>	<u>714,920</u>
FEDERAL INCOME TAX EXPENSE	<u>\$ 786,762</u>	<u>\$ 714,920</u>

AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 9 - Related Party Transactions

Loans and deposits with related parties:

In the normal course of business, the Corporation makes loans to and takes deposits from its executive officers, directors, and companies affiliated with these individuals. The aggregate dollar amount of loans to such individuals was approximately \$7,819,249 and \$5,005,057 at December 31, 2006 and 2005, respectively. The aggregate dollar amount of deposits from such individuals was \$667,444 and \$595,639 at December 31, 2006 and 2005, respectively.

Other related party transactions:

Throughout 2006 and 2005, the Corporation transacted with a company directly related to a Board member. The activity indirectly resulted in a total of \$152,050 and \$337,550 in fees paid by the Corporation's borrowers to this related company as of December 31, 2006 and 2005, respectively.

Note 10 - Federal Home Loan Bank Advances

At December 31, 2006, FHLB advances were scheduled to mature as follows:

	<u>Weighted- Average Rate</u>	<u>Amount</u>
Years ending December 31,		
2007	5.25%	\$ 22,166,667
2008	5.06%	2,115,592
2009	4.89%	7,566,667
2010	4.43%	66,667
2011	2.87%	5,066,667
Thereafter	6.80%	<u>5,915,871</u>
		<u>\$ 42,898,131</u>

As provided for in the Advances, Security, and Deposit Agreement with the FHLB, advances are collateralized by all FHLB stock owned by the Corporation, deposits with the FHLB, and certain mortgages or deeds of trust securing such properties. As a member of the FHLB of Seattle, the Corporation has an available maximum credit line equal to 30% of American Marine Bank's assets subject to collateralization requirements.

**AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

Note 11 - Other Borrowings

The Corporation has borrowed additional funds as follows:

	2006	2005
<p>Note payable with KeyBank, with monthly principal payments of \$31,368 maturing April 30, 2009, with interest at the one-month LIBOR plus 2.25%, currently 7.625% at December 31, 2006. The note is secured by American Marine Bank stock, and is guaranteed by the Corporation.</p>	\$ 561,301	\$ 883,241
<p>Note payable to Homestead Equity Fund A, secured by two units of Homestead Equity Fund A limited partnership interest. The note is payable on demand or in full on March 31, 2012. The note does not have a stated interest rate.</p>	855,770	980,000
<p>Revolving line of credit with KeyBank, maturing September 29, 2007, with interest at the three-month LIBOR plus 2.00%, currently 7.367% at December 31, 2006. The line of credit is secured by American Marine Bank stock and has a limit of \$1,000,000.</p>	250,000	-
	\$ 1,667,071	\$ 1,863,241

At December 31, 2006, other borrowings were scheduled to mature as follows:

	Weighted- Average Rate	Amount
<p>Years ending December 31,</p>		
On demand	0.000%	\$ 855,770
2007	7.493%	490,558
2008	7.625%	240,558
2009	7.625%	80,185
		\$ 1,667,071

AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 11 - Other Borrowings (Continued)

In February 2004, the Corporation issued junior subordinated debentures aggregating \$7,217,000 to American Marine Trust I (the Trust), with interest at three-month LIBOR plus 2.85%, repricing quarterly, which was 8.22% at December 31, 2006. The Trust issued \$217,000 of common securities to the Corporation and capital securities with an aggregate liquidation amount of \$7,000,000 (\$1,000 per capital security) to third party investors. The common securities are included in investment in subsidiaries on the consolidated balance sheet. The securities have a coupon rate of LIBOR plus 2.85%, repricing quarterly, which was 8.22% at December 31, 2006. The subordinated debentures are included as Tier 1 capital for regulatory purposes. The subordinated debentures and the capital securities pay interest and dividends, respectively, on a quarterly basis, which are included in interest expense. The subordinated debentures will mature in April 2034, at which time the capital securities must be redeemed. The subordinated debentures and capital securities can be redeemed, in whole or in part, beginning February 1, 2009, at a redemption price of \$1,000 per capital security. The Corporation has provided a full and unconditional guarantee of the obligations of the Trust under the capital securities in the event of default. Debt issuance costs related to the issuance of trust preferred securities of \$52,500 were capitalized during 2004, and are being amortized over 30 years.

Note 12 - Retirement Plans

KSOP Plan:

The Corporation has a deferred compensation plan known as the Employee Stock Ownership Plan with 401(k) provisions (KSOP). Employees are eligible to participate in the KSOP after attaining age 18 and completing 1,000 hours of service in a plan year. Participants may make contributions to the KSOP.

Contributions to the KSOP by the Corporation, the employer, are discretionary and can be made in cash or common stock of the Corporation. There are two types of employer contributions: optional contributions (vesting in increments of 20%, fully vested after six years of service) and employer matching contributions (fully vested).

The KSOP Trust has outstanding borrowings from a correspondent bank of \$74,000 and \$148,000 at December 31, 2006 and 2005.

Compensation expense is recorded equal to the fair value of shares held by the KSOP, which are deemed committed to be released. KSOP compensation expense was approximately \$285,932 and \$253,490 for the years ended December 31, 2006 and 2005, respectively. As of December 31, 2006 and 2005, allocated shares were 120,848 and 130,326, respectively, and no shares were unallocated. Dividends declared on shares held by the KSOP were \$196,887 in 2006 and \$208,144 in 2005.

**AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

Note 12 - Retirement Plans (Continued)

KSOP Plan (continued):

The Corporation is required by regulation to provide a repurchase option to participants holding the Corporation's stock, as the stock is not readily tradable. The Corporation is required to repurchase stock at market value. At December 31, 2006, there are approximately 24,170 shares subject to this repurchase requirement with a market value of \$2,085,871.

Life insurance and salary continuation:

The Corporation maintains individual executive supplemental income plans for the benefit of certain officers. The plans are funded by the purchase of corporate owned life insurance policies covering the lives of the individual officers. The Corporation is the owner and beneficiary of these insurance policies.

The individual plans provide for monthly payments to such persons, or their beneficiaries, for periods of 15 years following death prior to retirement or 15 years to life following retirement. Benefit payments to individuals vary and are predetermined in the individual contracts through reference to salaries and years of service.

The projected unit credit cost method is used to allocate the costs of these plans during the period of service of the individuals. The net post-retirement benefit cost plus mortality expense recognized during the years ended December 31, 2006 and 2005, was \$60,704 and \$397,411, respectively.

The present value of the accumulated post-retirement benefit obligation attributable to years of service through December 31, 2006 and 2005, is approximately \$1,846,273 and \$2,024,229, respectively. The Corporation has accrued these amounts in other liabilities on the consolidated statement of financial condition.

The insurance cash surrender value was approximately \$7,339,106 and \$5,613,319 at December 31, 2006 and 2005, respectively, and is included on the consolidated statement of financial condition.

Note 13 - Stock Option Plans

In previous years, the Board of Directors, upon stockholder approval, approved two stock option plans (the Plans); one for key employees and one for directors of the Corporation. The Incentive Stock Option Plan permits the grant of stock options to authorized key employees for up to 30,000 shares of common stock. These option awards generally vest based on five years of continuous service. The Director Non-Qualified Stock Option Plan permits the grant of stock options to directors for up to 15,000 shares of common stock. Director option awards are fully vested on the date of grant. Option awards under both Plans are generally granted with an exercise price equal to the market price of the Corporation's stock at the date of grant and have 10-year contractual terms. Stock options granted are eligible for adjustment in the event that the outstanding common stock of the Corporation changes as a result of a stock dividend, stock split, or other changes to existing stock. The Plans will terminate on March 21, 2011.

**AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

Note 13 - Stock Option Plans (Continued)

The fair value of each option is estimated on the date of grant using the Black-Scholes-Merton option pricing model with the following weighted-average assumptions used for unvested grants as of December 31, 2006, was as follows:

Risk free interest rate	5.0%
Expected volatility	5.6%
Expected cash dividends	2.4%
Expected life	7 years

A summary of option activity under the Plans as of December 31, 2006, and changes during the year then ended is presented below:

	<u>Shares</u>	<u>Weighted- Average Exercise Price</u>	<u>Weighted- Average Remaining Contractual Term</u>	<u>Aggregate Intrinsic Value</u>
Outstanding options, beginning of year	19,271	\$ 61.91		
Granted	-	\$ -		
Exercised	(2,328)	\$ 56.43		
Forfeited or expired	(792)	\$ 66.00		
Outstanding options, end of year	<u>16,151</u>	<u>\$ 62.50</u>	6.48 years	\$ 1,298,863
Exercisable options, end of year	<u>14,409</u>	<u>\$ 62.07</u>	6.42 years	\$ 1,158,772

The total intrinsic value of options exercised during the years ended December 31, 2006 and 2005, was \$55,842 and \$30,932, respectively.

The following table summarizes information about stock options outstanding at December 31, 2006:

	<u>Options Outstanding</u>			<u>Exercisable Options</u>	
	Number Outstanding at End of Year	Weighted- Average Remaining Contractual Life (Years)	Weighted- Average Exercise Price	Number Exercisable at End of Year	Weighted- Average Exercise Price
Price range (\$51.50)	3,903	4.95	\$ 51.50	3,903	\$ 51.50
Price range (\$66.00)	<u>12,248</u>	6.97	66.00	<u>10,506</u>	66.00
	<u>16,151</u>			<u>14,409</u>	

**AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

Note 13 - Stock Option Plans (Continued)

SFAS 123(R) requires all share-based payments to employees, including grants of employee stock options, to be recognized in the income statement based on their fair values. Compensation cost is recorded as if each vesting portion of the award is a separate award. The adoption of this standard, as of January 1, 2006, using the modified prospective method, resulted in \$17,273 of compensation expense for the year ended December 31, 2006, related to the unvested portion of options granted in prior years. Net of taxes for the year ended December 31, 2006, this reduced net income by \$11,400 or \$0.02 on both a basic and diluted earnings per share basis. Unrecognized compensation cost remaining at December 31, 2006, was \$17,273 or \$11,400 net of tax.

SFAS 123(R) requires the recognition of stock-based compensation for the number of awards that are expected to vest. Recognized stock compensation expense was not reduced by estimated forfeitures because management believes the future effect to be minimal. Estimated forfeitures will be continually evaluated in subsequent periods and may change based on new facts and circumstances.

Prior to January 1, 2006, employee stock options were accounted for under the intrinsic value method as allowed under APB No. 25. Stock options are generally granted at exercise prices not less than the fair market value of the Company's common stock on the date of grant. Under APB No. 25, no compensation expense was recognized pursuant to the Company's stock option plans for stock options.

Note 14 - Regulatory Capital Requirements

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

Quantitative measures established by regulation to ensure capital adequacy require the Corporation to maintain minimum amounts and ratios (set forth in the following table) of Tier 1 capital (as defined in the regulations) to total average assets (as defined), and minimum ratios of Tier 1 and total capital (as defined) to risk-weighted assets (as defined). Under the regulatory framework for prompt corrective action, the Corporation must maintain minimum Tier 1 leverage, Tier 1 risk-based, and total risk-based ratios as set forth in the table.

As of the most recent notification from the Corporation's regulator, the Corporation was categorized as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, the Corporation must maintain minimum capital ratios as set forth in the following table. There are no conditions or events since that notification that management believes have changed the institution's category.

**AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

Note 14 - Regulatory Capital Requirements (Continued)

The Corporation's actual capital amounts and ratios are presented as follows:

	Actual		Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
December 31, 2006						
Tier 1 capital (to average assets):						
AMB Financial Services Corporation	\$ 33,248,000	8.64%	\$ 15,400,600	≥ 4.00%	NA	≥ NA
American Marine Bank	33,805,000	8.90%	15,186,000	≥ 4.00%	\$ 18,982,500	≥ 5.00%
Tier 1 capital (to risk-weighted assets):						
AMB Financial Services Corporation	33,248,000	10.57%	12,579,320	≥ 4.00%	NA	≥ NA
American Marine Bank	33,805,000	10.76%	12,563,280	≥ 4.00%	18,844,920	≥ 6.00%
Total capital (to risk-weighted assets):						
AMB Financial Services Corporation	36,966,000	11.75%	25,158,640	≥ 8.00%	NA	≥ NA
American Marine Bank	37,523,000	11.95%	25,126,560	≥ 8.00%	31,408,200	≥ 10.00%

	Actual		Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
December 31, 2005						
Tier 1 capital (to average assets):						
AMB Financial Services Corporation	\$ 33,046,000	9.57%	\$ 13,817,320	≥ 4.00%	NA	≥ NA
American Marine Bank	32,979,000	9.56%	13,802,080	≥ 4.00%	\$ 17,252,600	≥ 5.00%
Tier 1 capital (to risk-weighted assets):						
AMB Financial Services Corporation	33,046,000	11.11%	11,902,920	≥ 4.00%	NA	≥ NA
American Marine Bank	32,979,000	11.10%	11,886,080	≥ 4.00%	17,829,120	≥ 6.00%
Total capital (to risk-weighted assets):						
AMB Financial Services Corporation	36,769,000	12.36%	23,805,840	≥ 8.00%	NA	≥ NA
American Marine Bank	36,697,000	12.35%	23,772,160	≥ 8.00%	29,715,200	≥ 10.00%

**AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
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Note 15 - Earnings Per Share

The calculation of earnings per share and earnings per share assuming full dilution is as follows:

	Year Ended December 31, 2006		
	Income (Numerator)	Average Number of Shares (Denominator)	Per Share Amount
Basic EPS			
Income available to common stockholders	\$ 2,385,455	555,698	\$ 4.29
Effect of Dilutive Securities			
Stock options		13,847	
Diluted EPS			
Income available to common stockholders plus assumed conversions	\$ 2,385,455	569,545	\$ 4.19
	Year Ended December 31, 2005		
	Income (Numerator)	Shares (Denominator)	Per Share Amount
Basic EPS			
Income available to common stockholders	\$ 2,921,447	566,520	\$ 5.16
Effect of Dilutive Securities			
Stock options		18,593	
Diluted EPS			
Income available to common stockholders plus assumed conversions	\$ 2,921,447	585,113	\$ 4.99

The Corporation's stock is traded on a limited basis. The average market price per share during 2006 was used in the determination of the dilutive effect of stock options.

AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 16 - Fair Value of Financial Instruments

The estimated fair values of the Corporation's financial instruments are as follows:

	2006		2005	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Financial Assets:				
Cash and due from banks	\$ 9,699,431	\$ 9,699,431	\$ 7,471,327	\$ 7,471,327
Interest-bearing deposits in banks	5,098,140	5,098,140	3,520	3,520
Federal funds sold	4,477,922	4,477,922	5,028,207	5,028,207
Securities available for sale	50,012,434	50,012,434	49,941,251	49,941,251
Federal Home Loan Bank stock	3,256,800	3,256,800	3,256,800	3,256,800
Investment in limited partnership	760,374	760,374	852,710	852,710
Loans receivable	293,369,803	300,477,388	262,399,912	260,170,206
Accrued interest receivable	2,171,480	2,171,480	1,731,923	1,731,923
Financial Liabilities:				
Deposits	305,736,129	305,556,763	280,410,760	280,290,484
FHLB advances	42,898,131	41,272,717	34,064,798	33,226,182
Obligation to KSOP plan	74,000	74,000	148,000	148,000
Other borrowings	1,667,071	1,667,071	1,863,241	1,863,241
Accrued interest payable	1,250,685	1,250,685	586,335	586,335

The following methods and assumptions were used to estimate the fair value of each class of financial instruments:

Cash and due from banks, interest-bearing deposits in banks, and federal funds sold:

The carrying amount approximates fair value because of the short maturity of these investments.

Securities available for sale and Federal Home Loan Bank stock:

The fair values of marketable securities are based on quoted market prices or dealer quotes. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities. Federal Home Loan Bank stock fair value is based on current redemption values.

Loans receivable:

Fair values are estimated for portfolios of loans with similar financial characteristics. Loans are segregated by type such as real estate, commercial, consumer, credit card, and other. Each loan category is further segmented into fixed and adjustable rate interest terms. The fair values for fixed-rate loans are 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. For variable rate loans that reprice frequently and have no significant change in credit risk, fair values are based on carrying values.

Fair values for loans held for sale are based on estimated market prices. Fair values for impaired loans are estimated using discounted cash flow analyses or underlying collateral values, where applicable.

**AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

Note 16 - Fair Value of Financial Instruments (Continued)

Accrued interest:

The carrying amounts of accrued interest approximate their fair values.

Deposits:

The fair value of demand deposits, savings accounts, and interest checking and money market deposits is the amount payable on demand at the reporting date. The fair value of fixed-maturity time deposits is estimated using the rates currently offered for deposits of similar remaining maturities.

Federal Home Loan Bank advances, obligation to KSOP, and other borrowings:

The fair values of the Corporation's long-term debt are estimated using discounted cash flow analyses based on the Corporation's current incremental borrowing rates for similar types of borrowing arrangements.

Federal funds purchased:

The carrying amount approximates fair value because of the short maturity of these borrowings.

Off-balance-sheet instruments:

Fair values of off-balance-sheet lending commitments are based on fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the counterparties' credit standing. The fair value of the fees at December 31, 2006 and 2005, were insignificant. See Note 7 for the notional amount of the commitments to extend credit.