



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

DECEMBER 31, 2008 AND 2007

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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, 2008 and 2007, 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 consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated 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 consolidated financial condition of AMB Financial Services Corporation and subsidiary as of December 31, 2008 and 2007, 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 24, 2009

AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
CONSOLIDATED STATEMENT OF FINANCIAL CONDITION

ASSETS

	December 31,	
	2008	2007
Cash and due from banks	\$ 12,021,043	\$ 8,942,743
Interest-bearing deposits in banks	1,021,495	10,479
Federal funds sold	10,495,975	-
Securities available for sale	51,452,612	62,504,547
Federal Home Loan Bank stock	3,256,800	3,256,800
Investment in limited partnership	610,638	684,505
Loans held for sale	853,300	-
Loans receivable, net of allowance for loan losses of \$4,120,238 2008; \$4,105,940 2007	297,096,774	316,530,162
Accrued interest receivable	2,309,887	2,329,611
Premises and equipment, net	12,460,751	13,346,316
Foreclosed real estate	3,887,342	-
Cash surrender value of life insurance policies	7,855,491	7,591,453
Goodwill	497,480	497,480
Other assets	2,674,650	2,017,399
TOTAL ASSETS	\$ 406,494,238	\$ 417,711,495

LIABILITIES AND STOCKHOLDERS' EQUITY

Deposits	\$ 320,439,910	\$ 323,625,153
Federal Home Loan Bank advances	47,615,873	48,731,465
Federal funds purchased	-	5,013,889
Other borrowings	141,872	1,313,448
Accrued interest payable	1,069,981	1,349,674
Other liabilities	2,733,945	3,087,500
Subordinated debentures	7,217,000	7,217,000
Total liabilities	379,218,581	390,338,129
COMMITMENTS (Note 7)		
STOCKHOLDERS' EQUITY		
Capital stock, no par; 2,000,000 shares authorized; 1,581,441 and 1,603,230 shares issued and outstanding in 2008 and 2007, respectively	3,784,792	4,241,931
Retained earnings	23,252,297	22,928,996
Accumulated other comprehensive income	238,568	202,439
Total stockholders' equity	27,275,657	27,373,366
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 406,494,238	\$ 417,711,495

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

	Year Ended December 31,	
	2008	2007
Interest income		
Loans receivable, including fees	\$ 21,728,763	\$ 23,821,597
Securities available for sale	2,444,713	2,346,201
Federal funds sold	76,266	158,634
Interest-bearing deposits	19,785	46,333
Total interest income	<u>24,269,527</u>	<u>26,372,765</u>
Interest expense		
Deposits	6,914,801	8,565,706
Federal Home Loan Bank advances	2,275,644	1,655,137
Other interest expense	526,432	671,626
Total interest expense	<u>9,716,877</u>	<u>10,892,469</u>
Net interest income	14,552,650	15,480,296
Provision for loan losses	2,239,198	774,011
Net interest income after provision for loan losses	<u>12,313,452</u>	<u>14,706,285</u>
Noninterest income		
Service charges	885,116	904,771
Income from trust fiduciary activities	1,264,538	1,382,426
Other income	1,760,284	1,478,467
Total noninterest income	<u>3,909,938</u>	<u>3,765,664</u>
Noninterest expenses		
Salaries and employee benefits	7,511,719	8,252,120
Occupancy	2,459,324	2,934,372
Salary continuance benefit	308,821	24,524
Professional fees	977,388	577,208
Printing and postage	348,071	323,407
Computer	586,887	509,325
Taxes and license	321,112	373,059
Communications	197,941	201,436
Advertising	150,801	176,720
Insurance	410,956	208,839
Directors fees	222,000	184,000
Exchange	266,348	269,911
Foreclosed real estate valuation adjustment	1,350,287	-
Other	1,112,807	1,278,093
Total noninterest expense	<u>16,224,462</u>	<u>15,313,014</u>
Income (loss) before income taxes	(1,072)	3,158,935
Federal income tax (benefit) expense	(564,442)	686,365
NET INCOME	<u>\$ 563,370</u>	<u>\$ 2,472,570</u>
Basic earnings per share	<u>\$ 0.35</u>	<u>\$ 1.52</u>
Diluted earnings per share	<u>\$ 0.35</u>	<u>\$ 1.51</u>

See accompanying notes.

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

	Shares of Common Stock	Total Stockholders' Equity	Capital Stock	Retained Earnings	Accumulated Comprehensive Income (Loss)	Comprehensive Income
Balance, December 31, 2006	548,013	\$ 26,677,568	\$ 5,450,217	\$ 21,317,918	\$ (90,567)	
Net income for 2007	-	2,472,570	-	2,472,570	-	\$ 2,472,570
Stock split, 3 to 1 ratio, April 27, 2007	1,096,026	-	-	-	-	
Cash dividends (\$0.67 per share)	-	(653,072)	-	(653,072)	-	
Dividend payable on January 15, 2008 (\$0.13 per share)	-	(208,420)	-	(208,420)	-	
Exercise of stock options	4,956	92,592	92,592	-	-	
Stock option expense	-	17,273	17,273	-	-	
Shares repurchased from KSOP	(45,765)	(1,318,151)	(1,318,151)	-	-	
Net change in unrealized loss on securities available for sale, net of taxes	-	293,006	-	-	293,006	293,006
Comprehensive income						\$ 2,765,576
Balance, December 31, 2007	1,603,230	27,373,366	4,241,931	22,928,996	202,439	
Net income for 2008	-	563,370	-	563,370	-	\$ 563,370
Cash dividends (\$0.15 per share)	-	(240,069)	-	(240,069)	-	
Stock option expense	-	17,983	17,983	-	-	
Shares repurchased from KSOP	(21,789)	(475,122)	(475,122)	-	-	
Net change in unrealized loss on securities available for sale, net of taxes	-	36,129	-	-	36,129	36,129
Reclassification adjustment	-	-	-	-	-	(160,299)
Comprehensive income						\$ 439,200
Balance, December 31, 2008	1,581,441	\$ 27,275,657	\$ 3,784,792	\$ 23,252,297	\$ 238,568	

AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
CONSOLIDATED STATEMENT OF CASH FLOWS

	Year Ended December 31,	
	2008	2007
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	\$ 563,370	\$ 2,472,570
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	1,268,855	1,543,915
Provision for loan losses	2,239,198	774,011
Amortization of investment premium, net	128,128	147,967
Realized gain on sale of securities	(227,153)	-
Change in deferred taxes	165,603	(435,281)
Loss on investment in limited partnership	73,867	75,869
Valuation allowance for foreclosed real estate	1,350,287	-
Realized loss on sale of foreclosed real estate	31,074	19,880
Loss on sale of premises and equipment	-	12,295
Origination of loans held for sale	(21,542,538)	-
Proceeds from sales of loans held for sale	20,689,238	-
Stock-based compensation expense	17,983	17,273
Net (increase) decrease in accrued interest receivable and other assets	(821,742)	183,041
Net increase in cash surrender value of life insurance	(264,038)	(252,347)
Net Increase (decrease) in accrued interest payable and other liabilities	(633,248)	118,221
Net cash provided by operating activities	<u>3,038,884</u>	<u>4,677,414</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Net (increase) decrease in federal funds sold	(10,495,975)	4,477,922
Net (increase) decrease in interest-bearing deposits in banks	(1,011,016)	5,087,661
Net (increase) decrease in loans receivable	11,092,403	(27,924,281)
Activity in available for sale securities:		
Proceeds from sales, maturities, calls, and principal repayments of securities	28,633,920	22,452,575
Purchases of securities	(17,428,219)	(34,648,735)
Purchases of premises and equipment	(383,290)	(1,539,336)
Proceeds from sales of premises and equipment	-	6,017
Proceeds from sales of foreclosed real estate	833,084	98,120
Net cash provided (used) by investing activities	<u>11,240,907</u>	<u>(31,990,057)</u>

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

	Year Ended December 31,	
	2008	2007
CASH FLOWS FROM FINANCING ACTIVITIES		
Net (increase) decrease in deposits	\$ (3,185,243)	\$ 17,889,024
Net (increase) decrease in Federal Home Loan Bank advances	(1,115,592)	5,833,334
Dividends paid on common stock	(240,069)	(872,277)
Proceeds from issuance of common stock	184,465	92,592
Repurchase of common stock	(659,587)	(1,318,151)
Repayment of KSOP loan	-	(74,000)
Proceeds from other borrowings	-	625,000
Repayment of other borrowings	(1,171,576)	(633,456)
Net (increase) decrease in federal funds purchased	(5,013,889)	5,013,889
	(11,201,491)	26,555,955
Net cash provided (used) by financing activities		
	3,078,300	(756,688)
NET CHANGE IN CASH AND DUE FROM BANKS		
	8,942,743	9,699,431
Cash and due from banks at January 1		
	\$ 12,021,043	\$ 8,942,743
SUPPLEMENTAL DISCLOSURE OF CASH FLOWS INFORMATION		
Cash paid during the year for:		
Interest	\$ 10,543,874	\$ 10,793,480
Income taxes	\$ 675,000	\$ 425,000
SUPPLEMENTAL SCHEDULE OF NONCASH INVESTING ACTIVITIES		
Acquisition of real estate and other repossessed assets in settlement of loans	\$ 6,101,787	\$ -
Net change in unrealized gain on securities available for sale	\$ 54,741	\$ 443,920

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 (the 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 consolidated 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 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 consolidated 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, 2008, 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, which 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, 2008 or 2007.

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). FHLB 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.

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 note payable to the limited partnership (see Note 11). Net losses were recorded by the Corporation for the years ended December 31, 2008 and 2007, in the amount of \$73,867 and \$75,869, 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 foreclosure or deeds in lieu of foreclosure and are stated at the lower of cost or estimated net realizable value. When the property is acquired, any excess of the loan balance over the estimated net realizable value is charged to the allowance for loan losses. Holding costs, subsequent write downs to net realizable value, if any, or any disposition gains or losses are included in noninterest income and expenses. Costs of development and improvement of the property are capitalized.

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 consolidated 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, 2008 and 2007, 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 consolidated 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)

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, reflect 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 1,598,018 and 1,623,924 at December 31, 2008 and 2007, respectively.

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	
	2008	2007
Net change in unrealized holding gains on available for sale securities	\$ 54,741	\$ 443,920
Tax effect	(18,612)	(150,914)
NET OF TAX AMOUNT	\$ 36,129	\$ 293,006
Reclassification adjustment for gains realized in net income	\$ (242,877)	\$ -
Tax effect	82,578	-
NET OF TAX AMOUNT	\$ (160,299)	\$ -

Recent accounting pronouncements:

In February 2008, the Financial Accounting Standards Board (FASB) issued FASB Staff Position (FSP) Statement of Financial Accounting Standards (SFAS) No. 157-2, *Effective Date of FASB Statement No. 157*. SFAS No. 157-2 delays the effective date of SFAS No. 157 for fair value measurements of nonfinancial assets and nonfinancial liabilities until fiscal years beginning after November 15, 2008, except assets and liabilities that are recognized or disclosed at fair value in the consolidated financial statements on a recurring basis (at least annually). SFAS No. 157-2 is not expected to have a material impact on the Company's financial statements.

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

Note 1 - Summary of Significant Accounting Policies (Continued)

Recent accounting pronouncements (continued):

In March 2008, the FASB issued SFAS No. 161, *Disclosures about Derivative Instruments and Hedging Activities – an amendment of FASB Statement No. 133*. The statement is intended to improve financial reporting about derivative instruments and hedging activities by requiring enhanced disclosures to enable investors to better understand the effects of derivative instruments on an entity's financial position, financial performance, and cash flows. SFAS No. 161 is effective for any reporting period beginning after November 15, 2008. SFAS No. 161 is not expected to have a material impact on the Company's financial condition or results of operations.

In May 2008, the FASB issued SFAS No. 162, *The Hierarchy of Generally Accepted Accounting Principles*. The objective of SFAS No. 162 is to improve financial reporting by identifying a consistent framework, or hierarchy, for selecting accounting principles to be used in preparing financial statements that are presented in conformity with U.S. generally accepted accounting principles (GAAP) for nongovernmental entities. The Public Company Accounting Oversight Board (PCAOB) has proposed an auditing standard that would remove the GAAP hierarchy from its interim auditing standards. SFAS No. 162 was effective November 15, 2008. SFAS No. 162 did not have a material impact on the Company's financial condition or results of operations. In September 2006, the FASB issued statement of SFAS No. 157, *Fair Value Measurements*. This statement defines fair value, establishes a framework for measuring fair value in accounting principles generally accepted in the United States of America, 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. On November 14, 2007, the FASB proposed to defer the effective date of SFAS No. 157 for all nonfinancial assets and liabilities, except those items recognized or disclosed at fair value on an annual or more frequently recurring basis, until years beginning after November 15, 2008. SFAS No. 157 is not expected to have a material impact on the Company's financial statements.

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 standard also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition.

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

Note 1 - Summary of Significant Accounting Policies (Continued)

Recent accounting pronouncements (continued):

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 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.

Pursuant to the FASB FSP No. 48-3, management has elected to defer the application of FASB FIN No. 48, *Accounting for Uncertainty in Income Taxes*, to fiscal years beginning after December 15, 2008.

For the financial statements for 2008 and 2007, the Company has accounted for uncertain tax positions in accordance with SFAS No. 5, *Accounting for Contingencies*, whereby the effect of the uncertainty would be recorded if the outcome was considered probable and was reasonably estimable. As of December 31, 2008 and 2007, the Company did not have accruals related to uncertain tax positions.

Reclassifications:

Certain reclassifications have been made in the December 31, 2007, consolidated financial statements in order to conform with the December 31, 2008, presentation with no effect on previously reported net income or equity.

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, 2008			Fair Value
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	
Securities available for sale:				
U.S. government and agency	\$ 3,096,542	\$ 16,945	\$ (2,425)	\$ 3,111,062
State, county, and municipal	31,026,587	487,717	(447,106)	31,067,198
Corporate bonds	-	-	-	-
Mutual equity fund securities	500,000	2,615	-	502,615
Mortgage backed securities	16,468,016	308,203	(4,482)	16,771,737
	\$ 51,091,145	\$ 815,480	\$ (454,013)	\$ 51,452,612

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

Note 2 - Securities (Continued)

	December 31, 2007			Fair Value
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	
Securities available for sale:				
U.S. government and agency	\$ 10,800,620	\$ 81,561	\$ (21,462)	\$ 10,860,719
State, county, and municipal	37,064,299	338,661	(155,407)	37,247,553
Corporate bonds	496,314	10,292	-	506,606
Mutual equity fund securities	250,000	1,908	-	251,908
Mortgage backed securities	13,586,588	98,193	(47,020)	13,637,761
	<u>\$ 62,197,821</u>	<u>\$ 530,615</u>	<u>\$ (223,889)</u>	<u>\$ 62,504,547</u>

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, 2008 and 2007. 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, 2008					
	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	\$ -	\$ -	\$ 90,224	\$ (2,425)	\$ 90,224	\$ (2,425)
State, county, and municipal	5,680,599	(203,444)	8,019,574	(243,662)	13,700,173	(447,106)
Mortgage backed securities	-	-	833,172	(4,482)	833,172	(4,482)
	<u>\$ 5,680,599</u>	<u>\$ (203,444)</u>	<u>\$ 8,942,970</u>	<u>\$ (250,569)</u>	<u>\$ 14,623,569</u>	<u>\$ (454,013)</u>

	December 31, 2007					
	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	\$ -	\$ -	\$ 5,119,383	\$ (21,462)	\$ 5,119,383	\$ (21,462)
State, county, and municipal	10,152,044	(121,820)	5,540,504	(33,587)	15,692,548	(155,407)
Mortgage backed securities	2,122,957	(12,559)	1,972,738	(34,461)	4,095,695	(47,020)
	<u>\$ 12,275,001</u>	<u>\$ (134,379)</u>	<u>\$ 12,632,625</u>	<u>\$ (89,510)</u>	<u>\$ 24,907,626</u>	<u>\$ (223,889)</u>

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, 2008, 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.

	<u>Amortized Cost</u>	<u>Fair Value</u>
Maturing in less than one year	\$ 3,605,072	\$ 3,633,820
Maturing in one to five years	5,543,314	5,731,450
Maturing in five to ten years	5,144,431	5,325,163
Maturing after ten years	20,330,312	19,990,401
Mortgage backed securities	<u>16,468,016</u>	<u>16,771,778</u>
	<u>\$ 51,091,145</u>	<u>\$ 51,452,612</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:

	<u>2008</u>		<u>2007</u>	
	<u>Amortized Cost</u>	<u>Estimated Fair Value</u>	<u>Amortized Cost</u>	<u>Estimated Fair Value</u>
To secure short-term borrowings and trust collateral	\$ 19,584,747	\$ 19,875,076	\$ 3,710,927	\$ 3,702,035
Treasury tax and loan account	1,029,222	1,045,170	1,042,653	1,058,919
To secure public deposits	1,061,275	1,092,230	1,042,870	1,052,500
	<u>\$ 21,675,244</u>	<u>\$ 22,012,476</u>	<u>\$ 5,796,450</u>	<u>\$ 5,813,454</u>

For the years ended December 31, 2008 and 2007, proceeds from sales of securities available for sale amounted to \$26,216,448 and \$-0-, respectively. Gross realized gains amounted to \$278,540 and \$-0-, respectively. Gross realized losses amounted to \$51,387 and \$-0- during the years ended December 31, 2008 and 2007, respectively. The tax provision applicable to these net realized gains and losses amounted to \$77,232 and \$-0- during years ended December 31, 2008 and 2007, respectively. Cost was determined by using the specific identification method.

**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>2008</u>	<u>2007</u>
Commercial real estate	\$ 83,845,856	\$ 96,592,640
Construction, land development, and other land	74,070,646	76,527,154
Commercial and industrial	30,774,266	38,263,181
Residential real estate	76,843,828	76,362,958
Consumer and other	<u>36,097,355</u>	<u>33,410,386</u>
	301,631,951	321,156,319
Allowance for loan losses	(4,120,238)	(4,105,940)
Deferred loan fees, net of deferred costs	(414,939)	<u>(520,217)</u>
	<u>\$ 297,096,774</u>	<u>\$ 316,530,162</u>

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

	<u>2008</u>	<u>2007</u>
Fixed	\$ 224,242,935	\$ 194,530,570
Variable	77,389,016	126,625,749
	<u>\$ 301,631,951</u>	<u>\$ 321,156,319</u>

Impaired loan information as of December 31:

	<u>2008</u>	<u>2007</u>
Impaired Loans:		
Impaired loans with specific allowance for loan losses	\$ 13,962,943	\$ 22,462,547
Impaired loans without a specific allowance for loan losses	43,037,567	-
	<u>\$ 57,000,510</u>	<u>\$ 22,462,547</u>
Allowance for losses on impaired loans	<u>\$ 2,356,786</u>	<u>\$ 818,759</u>
Average impaired loans	<u>\$ 48,523,280</u>	<u>\$ 15,062,583</u>

Impairment has been recognized in conformity with SFAS No. 114 as amended by SFAS No. 118. The Corporation is not committed to lend additional funds to borrowers whose loans have been modified.

AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

Interest income on impaired loans of \$3,033,087 and \$1,144,189 has been recognized for cash payments received in 2008 and 2007, respectively. Total loans past due 90 days or more and still accruing interest were \$7,504,977 and \$3,973,122 with accrued interest of \$605,761 and \$172,628 at December 31, 2008 and 2007, respectively.

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

	<u>2008</u>	<u>2007</u>
Allowance for loan losses:		
Balance, beginning of year	\$ 4,105,940	\$ 3,413,705
Provision charged to expense	2,239,198	774,011
Losses charged to allowance	(2,601,256)	(104,411)
Recoveries of losses previously charged off	376,356	22,635
BALANCE, END OF YEAR	<u>\$ 4,120,238</u>	<u>\$ 4,105,940</u>
Reserve for unfunded commitments, included in other liabilities on the accompanying balance sheet:		
Balance, beginning of year	\$ 214,498	\$ 303,509
Provision charged to expense	1,315	(89,011)
BALANCE, END OF YEAR	<u>\$ 215,813</u>	<u>\$ 214,498</u>
Allowance for credit losses:		
Allowance for loan losses	\$ 4,120,238	\$ 4,105,940
Reserve for unfunded commitments	215,813	214,498
TOTAL ALLOWANCE FOR CREDIT LOSSES	<u>\$ 4,336,051</u>	<u>\$ 4,320,438</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 \$40,825,412 and \$48,594,557 at December 31, 2008 and 2007, respectively.

Note 4 - Foreclosed Real Estate

An analysis of the changes in foreclosed real estate is as follows:

	<u>2008</u>	<u>2007</u>
Foreclosed Real Estate:		
Balance, beginning of year	\$ -	\$ 118,000
Transfers from loans receivable	6,101,787	-
Valuation adjustment	(1,350,287)	-
Proceeds from sales	(833,084)	(98,120)
Realized loss on sale, net	(31,074)	(19,880)
BALANCE, END OF YEAR	<u>\$ 3,887,342</u>	<u>\$ -</u>

**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>2008</u>	<u>2007</u>
Land	\$ 1,193,006	\$ 1,193,006
Buildings and leasehold improvements	11,492,962	11,491,276
Equipment	9,010,861	8,782,952
	21,696,829	21,467,234
Less accumulated depreciation and amortization	(9,266,341)	(8,127,091)
Construction in process	30,263	6,173
	<u>\$ 12,460,751</u>	<u>\$ 13,346,316</u>

Depreciation and amortization expense for the years ended December 31, 2008 and 2007, was \$1,268,855 and \$1,543,915, 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 \$412,186 and \$447,313 for the years ended December 31, 2008 and 2007, respectively.

The future minimum annual payments under these agreements at December 31, 2008, exclusive of taxes and other charges, are as follows:

Years ending December 31,	
2009	\$ 470,305
2010	493,401
2011	501,739
2012	506,216
2013	508,429
Thereafter	<u>5,178,623</u>
	<u>\$ 7,658,713</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>2008</u>	<u>2007</u>
Demand	\$ 11,930,335	\$ 13,002,625
Interest checking and money market	119,652,560	123,727,460
Savings	21,510,461	21,583,004
Time, \$100,000 and over	75,343,202	84,197,237
Other time	75,631,313	64,320,638
IRA	8,770,258	8,411,939
Other	7,601,781	8,382,250
	<u>\$ 320,439,910</u>	<u>\$ 323,625,153</u>

Included in time deposits in denominations of \$100,000 at December 31, 2008, are approximately \$44.37 million of time deposits in denominations of more than \$100,000 but not exceeding \$250,000 with maturities prior to December 31, 2009, as these qualify for expanded FDIC insurance coverage.

The following is a schedule by years of maturities for time deposits as of December 31, 2008:

Years ending December 31,	
2009	\$ 130,963,655
2010	11,434,625
2011	2,469,888
2012	2,396,154
2013	2,940,974
2014	769,219
	<u>\$ 150,974,515</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 consolidated 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.

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

Note 7 - Commitments (Continued)

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.

At December 31 commitments to extend credit were as follows:

	<u>Contract or Notional Amount</u>	
	<u>2008</u>	<u>2007</u>
Loan commitments, including credit cards	\$ 49,293,711	\$ 69,444,070
Standby and performance letters of credit	905,966	959,466
TOTAL CREDIT COMMITMENTS	\$ 50,199,677	\$ 70,403,536

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 \$1,500 per account, depending on the customer's account type. The commitment related to this program as of December 31, 2008, was \$3,989,900, of which \$24,686 was utilized. The commitment related to this program as of December 31, 2007, was \$4,253,707, of which \$16,205 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 Mason, 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 \$6,691,235. By Bank policy, however, this amount is not to exceed \$2,000,000.

AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 8 - Income Taxes

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

	<u>2008</u>	<u>2007</u>
Current tax (benefit) expense	\$ (732,903)	\$ 787,210
Deferred tax (benefit) expense	<u>168,461</u>	<u>(100,845)</u>
INCOME TAX (BENEFIT) EXPENSE	\$ (564,442)	\$ 686,365

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>2008</u>	<u>2007</u>
Deferred tax assets:		
Allowance for loan losses	\$ 1,188,305	\$ 1,263,086
Salary continuance plan	616,144	571,225
Nondeductible acquisition costs	36,162	36,162
Nonaccrual loan interest	266,445	-
OREO impairment loss	306,000	-
Other	<u>18,238</u>	<u>99,989</u>
Total deferred tax assets	<u>2,431,294</u>	<u>1,970,462</u>
Deferred tax liabilities:		
Accumulated depreciation and amortization	(1,127,726)	(548,861)
Goodwill	(88,798)	(76,112)
Loan origination costs	(101,351)	(74,265)
FHLB stock dividends	(321,072)	(321,072)
Book-tax basis differential in limited partnership	(38,878)	(9,427)
Prepaid expenses	(95,947)	(126,669)
Net unrealized gains on securities available for sale	(122,899)	(104,287)
Mortgage servicing rights	(422)	(11,735)
Other	<u>(23,240)</u>	<u>-</u>
Total deferred tax liabilities	<u>(1,920,333)</u>	<u>(1,272,428)</u>
NET DEFERRED TAX ASSETS	\$ 510,961	\$ 698,034

At December 31, 2008, a current income tax receivable of \$1,036,582 was included in other assets on the consolidated statement of financial condition. At December 31, 2007, a current income tax payable of \$396,847 was included in other liabilities on the consolidated statement of financial condition.

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

Note 8 - Income Taxes (Continued)

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

	2008	2007
Federal income tax at statutory rate	\$ (365)	\$ 1,074,425
Effect of permanent differences	(586,338)	(400,541)
Other	22,261	12,481
FEDERAL INCOME TAX (BENEFIT) EXPENSE	\$ (564,442)	\$ 686,365

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 deposits from such individuals was \$972,900 and \$748,600 at December 31, 2008 and 2007, respectively. The aggregate dollar amount of loans to such individuals were as follows:

	2008	2007
Balance at beginning of year	\$ 7,660,810	\$ 9,385,832
New loans and advances	390,338	5,529,809
Repayments	(748,844)	(7,254,831)
Balance at end of year	\$ 7,302,304	\$ 7,660,810

Other related party transactions:

The Corporation leases a property for branch operations from one of its Board members. The lease agreement commenced on April 1, 2007, with a term of 144 months with two five-year options to extend. The total rent expense paid was \$53,767 and \$-0- as of December 31, 2008 and 2007, respectively.

AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 10 - Federal Home Loan Bank Advances

At December 31, 2008, FHLB advances were scheduled to mature as follows:

	<u>Weighted- Average Rate</u>	<u>Amount</u>
Years ending December 31,		
2009	4.29%	\$ 20,066,667
2010	3.07%	12,066,667
2011	4.57%	7,066,667
2012	5.13%	5,066,667
2013	5.02%	2,066,667
Thereafter	5.39%	<u>1,282,538</u>
		<u>\$ 47,615,873</u>

As provided 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.

Note 11 - Other Borrowings

The Corporation has borrowed additional funds as follows:

	<u>2008</u>	<u>2007</u>
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 4.15% at December 31, 2008. The note is secured by American Marine Bank stock, and is guaranteed by the Corporation.	\$ -	\$ 216,134
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.	141,872	722,314

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

Note 11 - Other Borrowings (Continued)

	2008	2007
Revolving line of credit with KeyBank, maturing September 29, 2008, with interest at the three-month LIBOR plus 2.00%, currently 4.40% at December 31, 2008. The line of credit is secured by American Marine Bank stock and has a limit of \$1,000,000.	\$ -	\$ 375,000
	\$ 141,872	\$ 1,313,448

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 7.67% at December 31, 2008. 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 7.67% at December 31, 2008. 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 no outstanding borrowings at December 31, 2008 and 2007.

AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 12 - Retirement Plans (Continued)

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 related to employer matching contributions was approximately \$142,758 and \$147,510 for the years ended December 31, 2008 and 2007, respectively. KSOP compensation expense related to the employer's optional contribution was \$-0- and \$153,513 for the years ended December 31, 2008 and 2007, respectively. As of December 31, 2008 and 2007, allocated shares were 330,156 and 351,945, respectively, and no shares were unallocated. Allocated shares were adjusted to take into account a three for one stock split that took place on April 30, 2007. Dividends declared on shares held by the KSOP were \$52,417 in 2008 and \$191,470 in 2007.

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, 2008, there were approximately 330,151 shares subject to this repurchase requirement with a market value of \$4,787,262.

Life insurance and salary continuation:

The Corporation maintains individual executive supplemental income plans (the 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, 2008 and 2007, was \$308,821 and \$24,524, respectively.

The present value of the accumulated post-retirement benefit obligation attributable to years of service through December 31, 2008 and 2007, is approximately \$1,812,187 and \$1,680,074, respectively. The Corporation has accrued these amounts in other liabilities on the consolidated statement of financial condition.

The insurance cash surrender value was approximately \$7,855,491 and \$7,591,453 at December 31, 2008 and 2007, respectively, and is included on the consolidated statement of financial condition.

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

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.

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, 2008, 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, 2008, and changes during the years then ended is presented below:

	2008		2007	
	Shares	Weighted-Average Exercise Price	Shares	Weighted-Average Exercise Price
Outstanding options, beginning of year	33,033	\$ 21.01	45,453	\$ 20.75
Granted	-	\$ -	-	\$ -
Exercised	-	\$ -	(4,956)	\$ 17.17
Forfeited or expired	(3,120)	\$ 22.00	(7,464)	\$ 22.00
Outstanding options, end of year	<u>29,913</u>	\$ 20.91	<u>33,033</u>	\$ 21.01
Exercisable options, end of year	<u>29,913</u>	\$ 20.91	<u>33,033</u>	\$ 21.01

AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 13 - Stock Option Plans (Continued)

The following table summarizes information about stock options outstanding at December 31, 2008:

	Weighted-Average Remaining Contractual Life (Years)	Options Outstanding			Exercisable Options		
		Number Outstanding at End of Year	Aggregate Intrinsic Value	Weighted-Average Exercise Price	Number Exercisable at End of Year	Aggregate Intrinsic Value	Weighted-Average Exercise Price
Exercise prices:							
Price range (\$17.17)	2.95	6,753	\$ 19,931	\$ 17.17	6,753	\$ 19,931	\$ 17.17
Price range (\$22.00)	4.96	23,160	114,960	22.00	23,160	114,960	22.00
		29,913	\$ 134,891		29,913	\$ 134,891	

Information on the exercise of options was as follows during the years ended December 31:

	2008	2007
Option shares exercised	-	4,956
Fair value of shares exercised	\$ -	\$ 143,030
Proceeds from the exercise of options	-	85,078
INTRINSIC VALUE OF OPTIONS EXERCISED	\$ -	\$ 57,952

SFAS 123(R) requires all share-based payments to employees, including grants of employee stock options, to be recognized in the consolidated 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 \$17,983 and \$17,273 of compensation expense for the years ended December 31, 2008 and 2007, respectively, related to the unvested portion of options granted in prior years. Net of taxes for the years ended December 31, 2008 and 2007, reduced net income by \$11,869 and \$11,400, respectively. The basic and diluted earnings per share basis effect in December 31, 2008 and 2007, was \$0.00 and \$0.01, respectively. There was no unrecognized compensation cost remaining at December 31, 2008.

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.

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

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 consolidated 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 Corporation's category.

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, 2008						
Tier 1 capital (to average assets):						
AMB Financial Services Corporation	\$ 33,302,000	8.25%	\$ 16,144,360	≥ 4.00%	NA	≥ NA
American Marine Bank	33,227,000	8.19%	16,228,520	≥ 4.00%	\$ 20,285,650	≥ 5.00%
Tier 1 capital (to risk-weighted assets):						
AMB Financial Services Corporation	33,302,000	10.57%	12,596,600	≥ 4.00%	NA	≥ NA
American Marine Bank	33,227,000	10.56%	12,858,560	≥ 4.00%	18,878,340	≥ 6.00%
Total capital (to risk-weighted assets):						
AMB Financial Services Corporation	37,244,000	11.83%	25,193,200	≥ 8.00%	NA	≥ NA
American Marine Bank	37,166,000	11.81%	25,171,120	≥ 8.00%	31,463,900	≥ 10.00%

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

Note 14 - Regulatory Capital Requirements (Continued)

	Actual		Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
December 31, 2007						
Tier 1 capital (to average assets):						
AMB Financial Services Corporation	\$ 33,671,000	8.24%	\$ 16,354,200	≥ 4.00%	NA	≥ NA
American Marine Bank	33,627,000	8.41%	15,991,680	≥ 4.00%	\$ 19,989,600	≥ 5.00%
Tier 1 capital (to risk-weighted assets):						
AMB Financial Services Corporation	33,671,000	10.06%	13,393,200	≥ 4.00%	NA	≥ NA
American Marine Bank	33,627,000	10.06%	13,372,400	≥ 4.00%	20,058,600	≥ 6.00%
Total capital (to risk-weighted assets):						
AMB Financial Services Corporation	37,858,000	11.31%	26,786,400	≥ 8.00%	NA	≥ NA
American Marine Bank	37,808,000	11.31%	26,744,800	≥ 8.00%	33,431,000	≥ 10.00%

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, 2008		
	Income (Numerator)	Weighted-Average Number of Shares (Denominator)	Per Share Amount
Basic EPS			
Income available to common stockholders	<u>\$ 563,370</u>	<u>1,598,018</u>	<u>\$ 0.35</u>
Effect of Dilutive Securities			
Stock options		<u>6,753</u>	
Diluted EPS			
Income available to common stockholders plus assumed conversions	<u>\$ 563,370</u>	<u>1,604,771</u>	<u>\$ 0.35</u>

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

Note 15 - Earnings Per Share (Continued)

	Year Ended December 31, 2007		
	Income (Numerator)	Weighted- Average Number of Shares (Denominator)	Per Share Amount
Basic EPS			
Income available to common stockholders	\$ 2,472,570	1,623,924	\$ 1.52
Effect of Dilutive Securities			
Stock options		8,979	
Diluted EPS			
Income available to common stockholders plus assumed conversions	\$ 2,472,570	1,632,903	\$ 1.51

The Corporation's stock is traded on a limited basis. The average market price per share during 2008 was used in the determination of the dilutive effect of stock options.

Note 16 - Fair Value of Financial Instruments

On January, 1, 2008, the Corporation partially adopted SFAS No. 157, *Fair Value Measurements*. Full adoption of SFAS No. 157 has been deferred, as provided in FSF No. FAS 157-2, until January 1, 2009, and interim periods within that fiscal year. SFAS No. 157 provides enhanced guidance for measuring assets and liabilities using fair value and applies to situations where other standards require or permit assets or liabilities to be measured at fair value. SFAS No. 157 also requires expanded disclosure of items that are measured at fair value, the information used to measure fair value and the effect of fair value measurements on earnings. The partial deferral in implementation of SFAS No. 157 applies to nonfinancial assets and liabilities that the Corporation measures at fair value on a nonrecurring basis. These primarily include fair value assessments of goodwill, other indefinite-lived intangible assets, and foreclosed real estate and other foreclosed assets owned for which fair value measurements are made on a nonrecurring basis in evaluating impairment. Valuation techniques are based upon observable and unobservable inputs. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect our market assumptions. These two types of inputs create a fair value hierarchy. Level 1 includes quoted prices for identical instruments in active markets. Level 2 includes quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations whose inputs are observable. Level 3 includes instruments whose significant value input assumptions are unobservable.

AMB FINANCIAL SERVICES CORPORATION AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 16 - Fair Value of Financial Instruments (Continued)

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

	2008		2007	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Financial Assets:				
Cash and due from banks	\$ 12,021,043	\$ 12,021,043	\$ 8,942,743	\$ 8,942,743
Interest-bearing deposits in banks	1,021,495	1,021,495	10,479	10,479
Federal funds sold	10,495,975	10,495,975	-	-
Securities available for sale	51,452,612	51,452,612	62,504,547	62,504,547
Federal Home Loan Bank stock	3,256,800	3,256,800	3,256,800	3,256,800
Investment in limited partnership	610,638	610,638	684,505	684,505
Loans receivable	301,631,951	315,822,543	321,156,319	331,676,134
Accrued interest receivable	2,309,887	2,309,887	2,329,611	2,329,611
Financial Liabilities:				
Deposits	320,439,910	322,455,130	323,625,153	324,390,864
FHLB advances	47,615,873	46,339,589	48,731,465	47,364,356
Federal funds purchased	-	-	5,013,889	5,013,889
Other borrowings	141,872	141,872	1,313,448	1,313,448
Accrued interest payable	1,069,981	1,069,981	1,349,674	1,349,674

The following table summarizes the Corporation's financial instruments that were measured at fair value on a recurring basis at December 31, 2008:

	Fair Value	Fair Value Measurements Using		
		Level 1	Level 2	Level 3
Recurring				
Securities available for sale	\$ 51,452,612	\$ -	\$ 51,452,612	\$ -

Additionally, certain assets are measured at fair value on a nonrecurring basis. These adjustments to fair value generally result from the application of lower-of-cost-or-market accounting or write-downs of individual assets due to impairment. The following table summarizes the Corporation's financial instruments that were measured at fair value on a nonrecurring basis at December 31, 2008, and the total change resulting from these fair value adjustments for the year ended December 31, 2008:

	Fair Value	Fair Value Measurements Using			December 31, 2008 Total Loss
		Level 1	Level 2	Level 3	
Nonrecurring					
Impaired Loans	\$ 57,000,510	\$ -	\$ -	\$ 57,000,510	\$ 2,326,698
Foreclosed real estate and other foreclosed assets	\$ 3,887,342	\$ -	\$ -	\$ 3,887,342	\$ 1,350,287

Note 16 - Fair Value of Financial Instruments (Continued)

Impaired loans included in the table above are collateral dependent and fair value was determined based on the fair value of the underlying collateral, less costs to sell. If the Bank determines the value of the impaired loan is less than the recorded investment in the loan, the carrying value is adjusted through a charge-off. These charge-offs are recorded through the allowance for loan losses. The loss column above represents charge-offs recognized during the year ended December 31, 2008, related to the impaired loans. The foreclosed real estate and other foreclosed assets in the table above have been adjusted to fair value, less costs to sell. At the time of foreclosure, foreclosed assets are recorded at the lower of the carrying amount of the loan or fair value less costs to sell. Any write-downs based on the asset's fair value at the date of acquisition are charged to the allowance for loan losses. After foreclosure, management periodically performs valuations of the foreclosed assets and if additional impairments are deemed necessary, the impairment is recorded in foreclosed real estate and other foreclosed assets expense on the consolidated statements of operations. The loss column above represents impairments charged to the consolidated statements of operations during the year ended December 31, 2008.

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. FHLB 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.

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.

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

Note 16 - Fair Value of Financial Instruments (Continued)

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, 2008 and 2007, were insignificant. See Note 7 for the notional amount of the commitments to extend credit.

Note 17 - Subsequent Events

On February 27, 2009, the FDIC proposed adopting an interim rule to impose an emergency special assessment to financial institutions of \$0.20 per \$100 of insured deposits existing as of June 30, 2009, to be collected September 30, 2009. This interim rule also provides the FDIC may impose an additional special assessment in any quarter after June 30, 2009, to support the Deposit Insurance Fund in an additional amount of up to \$0.10 per \$100 of insured deposits.

This interim rule is subject to a comment period and regulatory approval and it is currently scheduled to be effective on April 1, 2009. Management considers it reasonably possible for this special assessment to be imposed during 2009. However, the amount of any assessment for the Bank will depend on the final rule and the Bank's level of insured deposits on the measurement date. No accrual for these events has been made in the financial statements as of December 31, 2008.